SUMMARY: The National Terrorism Insurance Act, s. 1743

Introduced by Sen. Ernest F. Hollings – November 29, 2001
Co-Sponsored by Sens. Barbara Boxer (D-CA) and Ron Wyden (D-OR)

BENEFITS OF BILL

- Provides the industry with the certainty they need to price and provide terrorism coverage.
- Avoids massive federal bailouts of insurance companies.
- Forces the industry, which is heavily capitalized -- approximately $300 billion in surplus presently -- to use its resources to continue providing terrorism insurance.
- Provides for Federal grants at levels consistent with the industry's capitalization and capacity and in which protects taxpayers from over exposure.

PURPOSE: The purpose of the National Terrorism Insurance Act is to use the resources of the Federal Government to support the insurance industry's ability to continue providing insurance for terrorism risks, but in a manner that best protects the interests of American taxpayers. The National Terrorism Insurance Act has been structured to accomplish this goal. In essence, the legislation has been designed to allow market forces commercial insurance companies to come together in a manner to provide the property-casualty industry the assurance and backup support it needs to maintain offerings of terrorism insurance. The Federal Government will play a significant role, as it must, but it will be in the form of overseeing the operation of market forces and temporary financial assistance – not massive subsidies for insurance companies. This bill was constructed from *risk pool* proposals submitted by the insurance industry, state insurance commissioners, and consumer and state taxpayers organizations. The legislation already has been endorsed by 13 current state insurance commissioners – Republican and Democrat.

STRUCTURE: The legislation has a two-part structure which will operate within an overall cap of $100 billion. The first $50 billion of potential industry terrorism-related losses will be covered by a national risk pool fund, to be known as the "National Terrorism Insurance Fund." The Fund will be funded via assessments on insurance companies and used to provide the industry the reinsurance it is seeking for terrorism. The remaining $50 billion covered by a government/industry co-sharing grant-aid program. Under this program, the government will agree to assume all insurance related terrorism losses beyond $50 billion on a cost-sharing basis, pursuant to the following formulas: 90/10 share, whereby the government will pickup 90% of the losses once the industry has met its 10% retention and 10% share under the cost-sharing formula; and an 80/20 share under the same guidelines for the second and third years.

NATIONAL TERRORISM INSURANCE FUND: As noted, the legislation would establish a risk pool through the creation of a national fund -- known as the National Terrorism Fund (hereinafter referred to as “the Fund”). A risk pool is a mechanism which allows for the sharing of risks among companies throughout the industry. The Fund will be created within the U.S. Department of Commerce, in conjunction with a 10-member Advisory Committee. The Advisory Committee will include: the Secretary of Treasury; three representatives of the property-casualty industry; a representative of the reinsurance industry; a representative of insurance agents; a representative of the National Consumer Association; a representative of the banking or real estate industries; and two representatives of the National Association of Commissioners (NAIC). The Advisory Committee would be authorized to administer funds, develop procedures for collection of premiums and processing claims, and implement underwriting standards for participating companies.

OPERATION OF THE FUND

- The Fund will be capitalized through an annual assessment of 3 percent of an insurer’s previous calendar year direct written gross premiums. The companies writing the following coverages will be required to participate: fire; allied lines; commercial multiple peril; ocean marine; inland marine; workers compensation; liability; products liability; commercial auto no-fault; commercial auto liability; aircraft; fidelity/surety; burglary and theft; and boiler and machinery. Companies selling other lines, including farm owners, homeowners, mortgage guaranty, financial guaranty, medical malpractice, earthquake, and private passenger automobile insurance, would be permitted to participate on a voluntary basis.

- All commercial insurance companies will be required to participate in the Fund. Providers of personal insurance coverage will have the option of participating if they believe they need additional reinsurance.

- Companies will be authorized to pass through the 3 percent assessment to their policyholders. Companies seeking to raise rates beyond these levels will be required to report and justify, with substantial evidence, such actions to state insurance regulators. This is designed to deter companies from using terrorism as an excuse to raise rates overall. Additionally, the bill will maintain enforcement of states’ fair trade practices and fair claims practices and laws.

- According to actuaries, the 3 percent assessment, based on current premium volumes, should generate between $6-7 billion annually.

FUND DISPENSATION: The Unlike other proposals, which include an industry-wide aggregate loss threshold before federal assistance is applicable, the bill’s payout structure is strictly individually company based. This is a better approach for individual companies. Otherwise, they would have to wait until an industry-wide catastrophe occurs before benefitting from a national reinsurance program. Under the program:

- Each participating insurer would have a 10 percent retention level based on its previous year's direct written premiums. Once a company suffers losses due to terrorism that exceeds its retention level, the company would be permitted to receive payments from the Fund. For example, if a company has direct written premiums of $100 million, its retention would be $10 million. Some have advised that the retention level should be as high as 20 percent. The bill originally contained a 20 percent retention, but it was lowered to 10 percent in response to concerns by the industry.

- Once a company has met its retention levels, the Fund will cover its remaining losses as follows: 90% during the first year (90/10). For the second and third years, a company will be permitted to select the amount of coverage from the following options: 90% coverage of losses for a premium of 5% of its direct written premiums and surplus; 80% coverage for a 4% premium; and 70% coverage for 3% premium.

FEDERAL LOANS: If at any time during the three years of the program, the losses from the participating companies exceed the Fund's capacity, the Fund will be authorized to borrow, from the Federal Treasury, moneys to cover the losses up to $50 billion. The Fund, through assessments on all participating companies, would be required to repay the loan. The Fund and the companies would be given as long as 20 years, if necessary, to repay the loans at standard market interest. If there are outstanding loans due after the expiration of the Fund on December 31, 2004, the companies will continue to be assessed until the loans are repaid.

DISSOLUTION OF FUND/REFUND BACK TO COMPANIES: If at the end of the program the Fund has a positive balance, the participating companies would be allowed to recoup the funds -- based on the proportion of each company's contribution -- contingent upon a guarantee that the money will be placed in a special catastrophic reserve account. That account could only be used to pay for losses related to terrorism, and major catastrophes (earthquakes, hurricanes, and tsunamis). Any company seeking to use the money for other purposes would be subject to criminal penalties.