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Importance of Terrorism Insurance Coverage

Following the horrific 9/11 terrorist attacks, terrorism insurance coverage was virtually non-existent for commercial property owners. Only when Congress enacted the Terrorism Risk Insurance Act (TRIA) in 2002 did coverage for terrorist attacks resume. TRIA established a public-private risk-sharing partnership that allows the federal government and private insurance companies to share losses in the event of a major terrorist attack. Originally enacted as a three-year program, TRIA has been reauthorized by Congress twice. In 2005, Congress passed the Terrorism Risk Insurance Extension Act (TRIEA). The most recent extension – the Terrorism Risk Insurance Reauthorization Act of 2007 (TRIPRA) – extended the program through December 31, 2014.

Today, there is concern that the uncertain future of TRIA may cause insurance prices to fluctuate. Further, this uncertainty may prompt insurers to drop terrorism coverage if a reauthorization of the program is not in place by the end of 2014. This became evident in 2005 when private insurers became more reluctant to offer terrorism coverage due to uncertainty regarding the program's extension. Ultimately, the uncertainty of insurance pricing impacts property owners' net operating income, and the value of their properties. The potential unavailability of this coverage at the end of 2014 will impact financing agreements and potentially hurt the fragile commercial real estate market.

Affordable and available terrorism insurance is a vital component of most commercial real estate transactions. It is estimated that 84 percent of outstanding commercial mortgage balances require terrorism insurance. Thus, if TRIA were to expire, and insurers subsequently dropped terrorism coverage, those loans would be in technical default. While the commercial real estate finance market is starting to show signs of life, any disruption in the availability of terrorism insurance in this sector would have serious consequences on its fragile road to recovery.

Necessity of the Terrorism Risk Insurance Program

The passage of TRIA in 2002 helped stabilize commercial real estate markets following the disruptions of the 9/11 terrorist attacks by making terrorism coverage available and, over time, more affordable. According to a 2010 President's Working Group on Capital Markets (PWG) and 2008 Government Accountability Office (GAO) study, TRIA and its subsequent extensions have generally kept terrorism insurance affordable and available nationwide. Improved access and lower premiums are due in part to the continued improvement in an insurer's ability to model and measure their aggregate loss exposure, and thereby manage terrorism risk.

However, despite improvements in these measurements, the frequency and severity of terrorism attacks cannot be reliably assessed by insurance companies. Primary insurers remain largely averse to exposing themselves to potentially catastrophic terrorism losses and continue to have limited ability to predict the frequency and magnitude of future terrorist attacks. Thus, without the federal backstop for potential insurance losses related to terrorism, coverage availability could decline significantly. In fact, without TRIA providing reimbursement for insured losses that exceed the amount of an insurer's deductible, coverage could decline by more than 95 percent, according to one insurance company cited in the GAO report.

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Quite simply, an effective homeland security strategy is central to the nation's economic security. American businesses must have adequate terrorism risk coverage. Without terrorism insurance, the nation's economic infrastructure is totally exposed to large-scale business disruptions after an attack. Specifically, accessible and reasonably priced terrorism insurance is an integral part of the health of the commercial real estate markets. Given that the reinsurance industry has not yet been able to develop a long-term solution that would eliminate the need for some form of federal assistance, NAR is concerned that the potential sunset of TRIA will result in a spike in terrorism coverage premiums, and cause coverage to become unavailable in numerous markets.

NAR believes the TRIA program has been a success because it provides for the sharing of risk between government, private insurers, and policyholders. Ultimately, it is critical for the U.S. economy that commercial policyholders be able to obtain coverage for terrorism risk. Therefore, TRIA must be extended beyond its current 2014 authorization.