MEMORANDUM
December 27, 2007

TO: Executive Committee
Government Affairs Committee
Board of Directors
State Association Presidents / Chairs
State Association Executives

FR: Jason Spence, Assistant Vice President, Federal Government Affairs

CC: Bob Rusbuldt, President and CEO
Charles Symington, Senior Vice President of Government Affairs

RE: **Terrorism Risk Insurance Program Reauthorization Act of 2007 Signed Into Law**

Yesterday, President Bush signed into law the Terrorism Risk Insurance Program Reauthorization Act of 2007 after a long year of debate that included a number of hearings, competing legislation, contentious negotiations and passionate debate regarding both substantive and procedural concerns. Enactment of this legislation marks a tremendous victory for IIABA, which made the extension of a federal backstop a top legislative priority in the 110th Congress. The legislation, which extends TRIA for seven years with only minor changes to the current program, will ensure that terrorism insurance is available and affordable for the policyholders that our members serve. The Big "I" was at the forefront of these deliberations at every stage throughout the process.

Background and History of the Program

After September 11th, the increased threat of another terrorist attack – coupled with tremendous uncertainty in the insurance market and the inability to price for future terrorist risks – caused prices for many types of commercial property-casualty insurance and reinsurance to rise dramatically, while coverage disappeared altogether in some areas. This crisis threatened our country's economic security, potentially impacting current and future construction and development, as well as existing structures that are pillars of our nation's economy. As a result, Congress recognized the importance of terrorism risk insurance for the health of the U.S. economy, and enacted the Terrorism Risk Insurance Act (TRIA) in the 107th Congress. The legislation was signed into law by President Bush in November 2002, and was originally set to expire December 31, 2005.

TRIA established a three-year Terrorism Risk Insurance Program in the Department of the Treasury to pay the federal share of compensation for insured losses resulting from acts of international terrorism. The Act only covered the U.S. commercial property-casualty market, and it required the federal government to share only in an insurer's losses if an attack is certified by the Secretary of the Treasury (Treasury) and the industry's aggregate insured losses exceed $5 million. In addition, an insurer had to pay out a certain number of claims (a "deductible") that is directly proportional to an insurer's size before accessing federal assistance. After this threshold was reached, the federal government would pay 90

percent of insured losses over the deductible and as much as a total of $100 billion in industry losses. However, the amount paid to insurers must be recouped through a surcharge in all commercial insurance premiums in following years if the aggregate industry losses were below an industry retention amount.

Following the passage of TRIA in 2002, the reaction of the marketplace and oversight of the program both indicated that the public-private partnership established by the Act worked well to stabilize the commercial insurance marketplace that underpins the U.S. economy. However, as the original TRIA neared expiration at the end of 2005, it became clear that the marketplace for terrorism insurance had not fully developed and that coverage may not be available without a federal backstop, due largely to a continued threat of a terrorist attack and the inability to price the risk associated with a potential attack. These concerns were supported by a number of observers in the market.

With the insurance market lacking the ability to insure against terrorism without a federal backstop, the Big "I" took a strong position that an extension of a federal backstop – either the current TRIA or a modified program – was necessary for the stability of the commercial insurance marketplace. The Big "I" asserted that extending TRIA, or a modified program, would guarantee access to coverage and ensure a continued boost to construction and job creation, while strengthening our economic growth and security and reducing the impact of any future terrorist attack prior to an attack, all with little cost to the government.

In late 2005 the Big "I" worked closely with Members of Congress and their staff on legislation extending TRIA for two years with some modifications. IIABA staff helped coordinate coalition efforts to pass the legislation, and on December 15, 2005, House-Senate negotiators reached an agreement on legislation. Shortly thereafter, President Bush signed into law the Terrorism Risk Insurance Extension Act of 2005. The law extended the terrorism risk insurance program for two additional years until December 31, 2007. It also reduced the number of covered lines and continued to increase the trigger, deductible, co-pay, and recoupment levels in order to encourage greater private market capacity and reduce taxpayer exposure.

Legislative Process and IIABA involvement

With the two-year TRIA extension of 2005 scheduled to expire on December 31, 2007, both the House and Senate began to hold hearings on the program and the possibility of extending it again early this year. The Big "I" was at the forefront of these deliberations. On February 28, 2007, the Senate Banking Committee held a hearing examining the program and Big "I" Government Affairs Committee Chairman Tom Minkler testified. Shortly thereafter, on March 5, 2007, the House Financial Services Committee Subcommittee on Capital Markets and Insurance held its own hearing on the program and the Big "I" once again testified. In both sets of testimony, the Big "I" stated the need for an extension of the program, advocated for a long-term extension, highlighted the national scope of the issue (as opposed to it being merely a "big city" issue), and asked Congress to take steps to address the lack of available coverage for Nuclear, Biological, Chemical, and Radiological (NBCR) terrorist events. IIABA also worked with other industry stakeholders

(insurance companies, commercial policyholders, etc.) as part of a broad coalition to make the case for extension legislation.

House Legislative Action

In June, Rep. Michael Capuano (D-MA) and House Financial Services Committee Chairman Barney Frank (D-MA) introduced H.R. 2761, the Terrorism Risk Insurance Revision and Extension Act of 2007 (TRIREA) and the House Subcommittee on Capital Markets and Insurance held a hearing on the proposed legislation. The bill would, among other things, extend the program for 10 years with current deductible and co-pay levels, lower the trigger from $100 million to $50 million, include coverage for NBCR events, create a reset provision for previously impacted areas, and add coverage for group life insurance. The Big "I" was well represented at the hearing by New York agent/broker Sharon Emek who did an excellent job offering the perspective of our members across the country. In her written and oral statement, Sharon expressed IIABA's support for H.R. 2761 and described how the provisions of the bill met the needs of agent and brokers, particularly the long-term extension, inclusion of NBCR coverage, reasonable trigger, deductible and co-pay levels, elimination of program distinction between foreign and domestic terrorism events, and mechanisms for developing long-term solutions.

Treasury Assistant Secretary David Nason also testified at the June hearing. Treasury's testimony laid out three critical elements that must be met for it to support a TRIA extension: 1) the program must remain temporary and short-term; 2) private sector retentions must be increased; and 3) no expansion of the program. Assistant Secretary Nason stated that these elements "reflect the positive experience under TRIA to date, and are grounded in the basic principle of limited government involvement in private markets." Nason concluded that H.R. 2761 does not meet these critical elements and declared, "It would be better to have no TRIA than a bad TRIA."

In late July, the House Subcommittee on Capital Markets and Insurance held a markup of H.R. 2761 and passed it out of the subcommittee, with amendment, by a voice vote. The following week, on August 1st, the full House Financial Services Committee marked up H.R. 2761 and passed it out of committee with a number of amendments, most notably an amendment to extend the program for 15 years instead of 10 years.

After lawmakers returned from the August recess, the full House of Representatives passed H.R. 2761 on September 19th. The most significant debate on the House floor dealt with a provision adopted in order to overcome the estimated cost of the program. The Congressional Budget Office estimated that the legislation could cost the U.S. Treasury over $8 billion over the next 10 years. Under pay-as-you-go (Pay-Go) rules adopted at the beginning of this Congress, the cost of any new authorization must be offset by an equal amount of spending cuts or new revenue. In order to overcome this obstacle, Chairman Frank and Democratic leadership included a provision that stipulated that no federal funds would be spent for the TRIA program until a terrorist event occurred and that required a post-event joint resolution of Congress to release funds for the program. This "second vote" requirement was very problematic because it would negatively impact the certainty

that the program was intended to create. However, in an attempt to assuage concerns about this provision, House Democratic leadership pledged to remove it in conference and resolve the Pay-Go issue another way. With the looming year-end expiration of the program, it was important that the legislative process moved forward despite this problem. As a result, the Big "I" supported House passage and sent a letter of support to House leadership.

As expected, prior to House approval of H.R. 2761, the White House issued a very strongly worded Statement of Administration Policy (SAP) expressing opposition to the bill as an expansion of the federal government's role in terrorism insurance. The SAP stated, "if H.R. 2761 as reported were presented to the President, his senior advisors would recommend that he veto the bill." Despite this veto threat, the bill was passed by an overwhelming vote of 312-110 with strong bipartisan support. The extension legislation, as passed by the House, would have extended the program for 15 years, expanded TRIA to include NBCR coverage, maintained the current insurer deductible (20%) and industry-wide co-payment level (15%) for conventional terrorism acts, set insurer deductible for NBCR events at 3.5% in the first year plus an additional .5% each year thereafter, set industry-wide co-payment levels for NBCR events on sliding scale, set the program trigger at $50 million, established a reset mechanism in the event of a terrorist attack of $1 billion or greater, changed TRIA's definition of terrorism to include acts of domestic terrorism, added group life insurance coverage, created a voluntary terrorism buy-down fund at the Treasury Department, established NBCR form and rate transition periods, and continued to require studies of the development of a private market for terrorism risk insurance.

Senate Legislative Action

In October, the Senate Banking Committee held a markup of original legislation to extend the TRIA program, the Terrorism Risk Insurance Program Reauthorization Act (TRIPRA) of 2007, which passed the committee by a vote of 20-1. This extension legislation was a much narrower extension than that passed by the House in September. The Senate bill extended the federal terrorism backstop for 7 years (as opposed to the 15 years passed by the House) under the same terms as current law (*e.g.* current deductible, co-pay, and trigger levels). In addition, the bill made only a few minor changes to the current program. Specifically, the bill altered the definition of terrorism to include domestic acts of terror, added a number of clarifying provisions regarding the $100 billion annual liability cap, and required reports to Congress with recommendations for NBCR coverage and for addressing capacity constraints in certain geographic areas.

Importantly, prior to the Senate Banking Committee markup, the Treasury Department issued a letter stating that it would not oppose the Senate bill, as currently drafted, but threatening a veto recommendation if amendments are adopted that move the bill further from their key elements (*i.e.*, temporary, no expansion of the program, increased private sector retentions). Treasury's threatened veto recommendation of the House bill was based on the conclusion that it did not meet these elements.

On November 16th, the Senate amended H.R. 2761 by replacing all of the House's legislative language with the language passed by the Senate Banking Committee including

the title of the bill – the Terrorism Risk Insurance Program Reauthorization Act of 2007. This bill was brought to the Senate floor and passed unanimously. The only additions to the Senate Banking Committee language were the recoupment provisions that were included in order to satisfy budget pay-as-you-go requirements. Under the Senate-passed bill, the $27.5 billion recoupment by the federal government of funds paid out under the program would be required to be paid back on an accelerated schedule in order for the impact of the program to be revenue neutral. Solving the budget impact of the extension was the only obstacle to Senate passage and the Big "I", along with other industry and policyholder groups, worked very closely with Senate staff to help craft a solution that would allow the bill to move forward without objection.

Reconciliation of House and Senate Bills

Given the Administration's veto threat of any extension legislation that would go beyond the Senate bill as well as the potential of losing the support of some Senators if the Senate bill were changed, the Senate did not undertake any effort to engage in a formal conference with the House in order to reconcile their competing bills. In response, on December 12th, the House passed new TRIA extension legislation, H.R. 4299, which tracked the TRIA extension legislation recently passed by the Senate with the addition of a number of provisions from the previously-passed House bill. Specifically, H.R. 4299 included four provisions from the House-passed extension: 1) the deductible reset for large terrorist events; 2) lower trigger of $50 million instead of $100 million; 3) coverage for group life insurance; and 4) underwriting restrictions related to foreign travel.

Passage of this bill instead of the Senate-passed bill created a slightly complicated situation. Because both chambers must pass identical versions of extension legislation before it can be sent to the President, Congressional action was still necessary before the program could be extended. One option would have been for the Senate to take up and pass the new House legislation unaltered and send it to the President. However, the Administration indicated that it would recommend a veto of this new House bill and the Senate did not seem inclined to reconsider the issue. The other option was for the House to re-address this issue before Congress recesses and pass H.R. 2761, the extension bill the Senate passed and sent back to the House. (Despite the new House bill, because it was a different bill than the bill the Senate passed and sent over, the House still had the ability to pass the Senate's bill.)

Ultimately, the second option was pursued and on December 18th the House passed (360-53) the TRIA extension bill recently approved by the Senate – H.R. 2761, the Terrorism Risk Insurance Program Reauthorization Act of 2007. Having cleared both chambers of Congress, the extension legislation moved to the President's desk. On December 26, 2007, the President signed the extension bill into law.

The Big "I", along with other industry and policyholder groups, worked very closely with Members of Congress, staff, and the Administration throughout this year to ensure passage of extension legislation prior to the program's expiration. A summary of the final legislation is below.

Terrorism Risk Insurance Program Reauthorization Act of 2007

Duration	This bill extends the TRIA program for seven years, through December 31, 2014.
Triggering Event	The size of an event needed to trigger TRIA is maintained at $100 million.
Lines of Coverage	The extension bill retains all of the lines covered by the current program.
Make Available	The requirement that insurers make coverage available to policyholders in all lines covered by the program is retained.
Individual Retention	The individual insurer retention level – the amount of terrorism losses that an individual insurance company must pay before federal assistance becomes available is maintained at 20% of such premiums.
Co-pays	Insurers must pay a share of losses above their individual retentions, known as co-pays. Current co-pay levels of 85% federal/15% insurer are retained.
Industry Retention / Recoupment	The insurance industry as a whole must cover a certain amount of losses before federal assistance is available. This cost may be spread among policyholders by a policy surcharge not to exceed 3% of premiums annually. This industry-wide retention amount of $27.5 billion is retained, but the timeframe for collecting from industry is accelerated.
Definitions	The term "act of terrorism" is amended to include domestic acts of terrorism
Study	The Comptroller General is required, no later than one year after enactment, to submit a report to Congress with detailed findings and recommendations appropriate to expand the availability and affordability of insurance for NBCR terrorist events. The Comptroller General also is required, within 180 days of enactment, to determine whether there are specific markets in the United States where there are unique capacity constraints on the amount of terrorism risk insurance available. In addition, the President's Working Group on Financial Markets is required to continue with an ongoing study and reports to Congress in 2010 and 2013 on the long-term availability and affordability of terrorism insurance, including the availability and affordability of group life insurance.

The Future of Terrorism Insurance

Terrorism insurance was a top legislative priority for the Big "I" Government Affairs team in 2007 and the extension of the federal backstop is a tremendous victory for our membership and the insurance marketplace. However, the Big "I" remains committed to continuing to work with interested parties in the public and private sectors to develop long term solutions to terrorism insurance. IIABA staff also will continue to work on behalf of our members to ensure that terrorism insurance is available and affordable beyond the 2014 expiration of the Terrorism Risk Insurance Program Reauthorization Act of 2007.