



## CONFERENCE ON TERRORISM RISK INSURANCE

June 1-2, 2010 – Paris – OECD Headquarters

The heads of all the national terrorism insurance programs of OECD member countries gathered early June at the OECD headquarters in Paris in an attempt to begin a dialogue concerning approaches of compensation of losses from terrorist attacks<sup>1</sup>. The conference was organised under the auspices of the OECD Secretary General's High Level Advisory Board on Financial Management of Catastrophes, at the initiative of the Australian terrorism insurance program. More than 120 representatives from government, top decision makers from the (re)insurance market as well as experts of leading research institutions also participated in what was the largest ever gathering of key players in terrorism insurance markets. While the heads of member countries' programs participated, the results of the conference do not necessarily reflect the position or views of the member countries themselves.

There was broad agreement amongst participants on the following areas:

### General framework

1. Terrorism threat is still very real in many countries despite the lack of a major successful attack recently.
2. The terrorism risk is associated with characteristics that render it difficult to assess and insure. The best practice principles and recommendations expressed in the 2005 OECD report to address this risk were recognized as still highly relevant today. In particular, it was emphasized that public-private partnerships have proved to be in various countries an efficient and useful approach to achieve better spread and diversification and to guarantee sustainable terrorism insurance solutions, when appropriately designed<sup>2</sup>. There is governmental responsibility in the prevention and mitigation of terror attacks as well as the definition of a suitable regulatory framework to operate in, whereas the insurance industry

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<sup>1</sup> On top of bilateral contacts, multilateral dialogue between the countries where terrorism insurance schemes were first established was initiated after the 2001 events, under the OECD auspices (the work of the *Task Force on Terrorism Insurance* resulted in the 2005 publication on this issue). The June 2010 conference allowed to resume such dialogue, which now includes other countries that have since established their own terrorism insurance scheme.

<sup>2</sup> Within the EU, projects to establish new terrorism insurance pools should be carefully reviewed against the new bloc exemption regulation in force since 1<sup>st</sup> April, 2010 .

manages risk transfer and financial impact of such attacks. In various countries, it may be reasonable to expect insurers to manage such risk up to certain limits beyond which governments may need to play a role of (re)insurer of last resort.

3. When comparing state run pools to privately managed pools, proper consideration of the effect of tax exemptions may be important.

### **Improving existing solutions**

While there is a great variety of permanent and temporary solutions amongst existing terrorism programs, most of them are based on above principles. 9 out of the 31 OECD countries (Australia, Belgium, Denmark, France, Germany, Netherlands, Spain, the U.S. and the U.K.) have now set up public-private partnerships, either permanent or temporary, most often with a layered structure approach in which various stakeholders can intervene under pre-determined thresholds and where the government acts as the (re)insurer of last resort. Government reinsurance programs would typically be provided for ex ante premiums, except in the US where the federal reinsurance is based on ex post recoupment fees. Belgium and Denmark have established such a public-private mechanism recently – in 2008 and mid 2010 respectively. Some of the specific features of national schemes (e.g. the extent of coverage, the level of government intervention, the voluntary or mandatory nature of the scheme, the pricing mechanism, etc.) reflect various approaches, but also, in certain countries, the political and other circumstances at the time the program was established. Individual countries may therefore consider re-assessing their current set-up and check whether potential alterations to their schemes such as those that could make them more effective in risk spreading between the private and public component, or more comprehensive. Several issues were discussed in this respect:

1. Consideration could be given to introducing compulsory terrorism coverage - where today cover is voluntary - so that anti-selection could be avoided and the size of the risk-sharing community could be maximised. Consideration could be given to whether this would help improve stability, resilience and affordability of these schemes and also ensure a more complete financial coverage in case of an event with caution given to possible negative implications from such an approach.
2. The absolute amount of cover provided by the public/private partnership may be set at a level that can absorb a reasonable worst case event. Some programs provide very limited cover only, while there would probably be sufficient risk appetite and available capacity by the market for larger protections.

Terrorism attacks can affect many lines of business. An expansion of the scope of cover to all relevant lines of business could therefore be considered, as various programs heavily focus on property exposures only. In case of nuclear, biological, chemical or radiological attacks, many claims will be expected to come from workers compensation and life and health, on top of (contingent) business interruption, decontamination costs, etc.



More generally, participants highlighted the need for individual countries or their national schemes to continuously improve risk modeling and the quality of exposure data.

At international level, particularly among European member countries for instance, efforts should be made towards some convergence between national covers/schemes as well as the development of regional cooperation processes in case of a major cross-border event.

Cover for nuclear attacks will most likely remain a niche product due to its heavy correlation with financial market risks. A major nuclear attack would most probably deplete any terrorism insurance scheme absent limits. This risk remains fundamentally uninsurable absent compulsory coverage.

Specific capital market solutions have not yet taken off and any major evolution in this respect is not expected in the near future.

### **Creation of an OECD international platform on terrorism risk insurance**

Very little regulatory and market information is currently available on a comparable basis to monitor the evolution of national schemes, assess market trends, and identify and share best practices to continuously improve current terrorism insurance solutions. Yet, the heads of terrorism insurance programs, who met in a closed session just before the 1-2 June Conference, agreed that those in charge of terrorism risk insurance would benefit from cooperation to better manage their programs in the light of the global terrorism threat. They therefore decided to set up, under the aegis of the OECD High Level Advisory Board, a permanent international platform on the financial coverage of terrorism risk. The creation of this platform was announced at the Conference.

This new OECD platform will monitor the evolution of national systems of terrorism insurance as well as market trends.

It will also foster the development of best practices on financial prevention, mitigation and compensation of terrorism risk. While it will serve the countries where a national terrorism insurance system has been established, it will also benefit those countries that currently have no national scheme (2/3 of OECD countries and nearly all non-member countries) but are considering some form of national response to the terrorism insurance challenge.