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As Expiration of TRIPRA Approaches, Rating Pressure Increases

Material changes would raise rating concerns.

As the U.S. House of Representatives introduces legislation to extend the Terrorism Risk Insurance Program Reauthorization Act (TRIPRA), uncertainty remains as to whether Congress will allow the program to lapse in December 2014, or if it is renewed, what the backstop will encompass. Amid partisan debate over fiscal issues, little movement is anticipated on any terrorism legislation in the near future. Although a federal backstop helps reduce the impact terrorism has on an organization's risk-adjusted capitalization, overreliance on such a mechanism isn't a substitute for sound risk management.

A.M. Best continues to request that insurers, especially those that are heavily reliant on TRIPRA, present detailed plans to be implemented in the event TRIPRA isn't renewed or its protection is materially altered. Although private terrorism reinsurance is currently available, a rating concern will be future availability and affordability if the federal backstop changes significantly.

A.M. Best believes a comprehensive risk management process is crucial to the financial strength rating of any insurer with a material exposure to terrorism risk. A.M. Best has been assessing the impact of terrorism risk on insurers' balance sheets using confidential information gathered during rating discussions, as well as information submitted in companies' Supplemental Rating Questionnaires (SRQs). This information is used to complete a stress test designed to gauge the impact a large, insured terrorism loss could have on a primary insurer's capitalization if TRIPRA were not available. Key concerns for A.M. Best continue to be insurers' net loss exposures to terrorism (excluding the benefit of TRIPRA) exceeding 20% of capital and surplus; high aggregate exposures of risks within certain geographic areas; the locations of exposures within those areas; and the impact on capitalization.

As insurers anticipate writing policies that are exposed to terrorism after TRIPRA expires, A.M. Best will increase its emphasis on analyzing risk management processes of those affected. Insurers that currently would be materially affected by the absence of TRIPRA, and that cannot provide a sufficient action plan to reduce exposures to terrorism risks, likely will face rating pressure as the expiration date approaches. Initially, this pressure may result in the assignment of a negative outlook during the latter part of 2013.

For more information on how A.M. Best views terrorism risk, please see the criteria report *The Treatment of Terrorism Risk in the Rating Evaluation*.

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