

8. (3.25 points)

In 2014, a certified terrorism event occurred which caused \$50 billion of insurance industry losses.

An insurance company experienced \$200 million of losses due to this event before any recoveries from the federal government.

The following table provides 2013 earned premium for this insurance company:

Line of Business	Earned Premium (\$000 omitted)	
	Direct	Assumed
Commercial Property	50,000	5,000
Homeowners	25,000	1,000
Personal Auto	25,000	1,000
Workers' Compensation	100,000	0

a. (2.25 points)

Determine the amount of the \$200 million terrorism loss that is paid by the insurance company and the amount that is paid by the federal government under the Terrorism Risk Insurance Program Reauthorization Act of 2007.

b. (0.5 point)

Identify two criteria necessary for an event to be certified as an act of terrorism under the Terrorism Risk Insurance Program Reauthorization Act of 2007.

c. (0.5 point)

Briefly describe two characteristics of terrorism risk that may make it uninsurable by the private insurance market.

SAMPLE ANSWERS AND EXAMINER'S REPORT

QUESTION 8	
TOTAL POINT VALUE: 3.25	LEARNING OBJECTIVE: B
SAMPLE ANSWERS	
Part a: 2.25 points	
<p>Personal Auto/HO excluded from TRIA (commercial lines only) Coverage deductible = 20% of <u>Direct</u> Earned Premium that company wrote last year =(\$50M + \$100M) * 20% = \$30M</p> <p>Federal government pays 85% of \$170M (\$200M – \$30M Deductible) = \$144.5M Company pays 15% x \$170M + \$30M (Deductible) = \$55.5M</p>	
Part b: 0.5 point	
<ul style="list-style-type: none"> • Industry losses must be greater than \$5M • Certified (or declared an act of terror) by Secretary of Treasury, Secretary of State, and Attorney General 	
Part c: 0.5 point	
<p>Any two of the following:</p> <ul style="list-style-type: none"> • Catastrophic – high severity affecting many people at once • Lack of credible data from which to base accurate premium rates (or the risk can't be effectively modeled, making adequate pricing impossible) • There are not a sufficient # of historical events to accurately anticipate potential claims • Not fortuitous (i.e., it is an intentional act) 	
EXAMINER'S REPORT	
<p>Candidates generally struggled with parts a and b of this question, but performed better on part c. Some candidates did not understand the level of federal involvement, and how coinsurance and deductibles function within the program.</p>	
Part a	
<p>Common errors:</p> <ul style="list-style-type: none"> • Not calculating deductible based on direct commercial line premium only – either the candidate included personal lines, or included assumed amounts • Not understanding the order of calculation between deductible and coinsurance • Using an incorrect deductible amount or coinsurance percentage • Confusing the \$100M minimum loss for federal involvement, and considering it part of an insured's deductible 	
Part b	
<p>Common errors:</p> <ul style="list-style-type: none"> • Confusing \$5M total loss of the event, and \$5M loss of an individual insured • Using other figures as requisite threshold of federal involvement • Listing other government parties as responsible for declaring an act as a terrorist act 	
Part c	
<p>Common error:</p> <ul style="list-style-type: none"> • Confusing two different requirements of insurability into a single, incorrect requirement 	