

EXAM 6 – UNITED STATES, SPRING 2016

7. (3 points)

a. (0.5 point)

Briefly describe two reasons why terrorism risk might be considered uninsurable by the private insurance market.

b. (1.5 points)

Identify three goals of the Terrorism Risk Insurance Program and briefly describe how it accomplishes each of its goals.

c. (1 point)

Describe one argument in favor of and one argument against terminating the Terrorism Risk Insurance Program.

CONTINUED ON NEXT PAGE

SAMPLE ANSWERS AND EXAMINER'S REPORT

QUESTION 7	
TOTAL POINT VALUE: 3	LEARNING OBJECTIVE: B1,B3
SAMPLE ANSWERS	
Part a: 0.5 point	
<ul style="list-style-type: none"> • lack of available data • losses are not reasonably predictable • losses are not fortuitous • losses are not accidental • losses are intentional • Terrorism models are still relatively new • there are not a significant large number of insureds • losses are catastrophic • low frequency and high severity • insurers unable to make rates that are affordable from lack of data and experience • terrorism is catastrophic which could lead to solvency concerns 	
Part b: 1.5 points	
<ul style="list-style-type: none"> • provide a program of temporary coverage for terrorism risks while the private market stabilizes after 9/11 through a partnership between government and private insurers • serve the social purpose of avoiding economic disruption in the event of a terrorism event - ensuring the coverage is available and affordable means that more companies will be covered and able to recover quickly if there is a terrorist act • preserves state regulation of insurance as states still regulate terrorism rates • ensure terrorism coverage is available which is accomplished by requiring private insurers to offer the coverage • establish a temporary shared public/private program where the federal government acts as a reinsurance backstop in event of terrorist attack • federal government shares insured losses with private insurers to stabilize market with role of federal government depending on size of loss • prevent economic disruption by government acting as backstop • protect consumers by requiring those insurers that offer the lines of insurance covered by TRIP to make terrorism insurance available • promote availability and affordability of terrorism insurance by requiring coverage • create a temporary federal program of shared public and private compensation for insured terrorism losses to allow the private market to stabilize where role of federal loss sharing depends on size of insured loss • protect consumers by ensuring the availability and affordability of insurance for terrorism risks - required insurers to offer the insurance • preserve the state regulation of insurance - this program does not infringe on states' rights to regulate insurance 	
Part c: 1 points	
In Favor of Termination	
<ul style="list-style-type: none"> • private market's appetite for assuming terrorism risk has expanded since 2001, insurers can now find coverage as needed 	

SAMPLE ANSWERS AND EXAMINER'S REPORT

- the risk can be covered by large reinsurers or by catastrophe bonds
- there has not been a significant terrorist attack recently so market has recovered and is well capitalized to provide coverage

Against Termination

- no proof that private market can truly shoulder losses from a catastrophic terrorist event; failure could lead to insurer insolvencies and negatively impact consumers, broader economy, and insurance market
- losses tend to be catastrophic so TRIP should continue to exist to ensure affordability and availability.
- there has been no attacks since 9/11 so hard to say whether private market can take the financial outcome so government should continue to cover large losses
- losses tend to be uninsurable such as non-accidental aspect so there would be an availability issue without the program

EXAMINER'S REPORT

Part a

Candidates were expected to identify two reasons why terrorism risk is uninsurable. Most performed very well on this question. A common error was stating that terrorism is uninsurable because the risks are not independent.

Part b

Candidates were expected to identify three distinct goals of TRIP and then provide a brief description to elaborate on accomplishment. Candidates struggled with identifying three distinct goals, in particular that TRIP preserves state regulation of terrorism insurance. The most common error was identifying the three goals but not adding a brief description on how TRIP accomplishes it.

Part c

Most candidates were able to at least state an argument in favor of terminating TRIP and against terminating TRIP to receive partial credit but not necessarily go on to receive full credit with a description.

Most common error was identifying an argument but not elaborating with a description as requested. Examples include:

- Against Termination: could lead to unavailable coverage if government did not offer
- Favor for Termination: private market has stabilized