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# News for Our Clients

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A monthly news bulletin provided by PIA and your insurance agent

## Disaster Insurance

On September 11, 2001, many of us heard the statement, "Our lives will never be the same again." Little did we know!

Sure, many things in our lives have not changed, but the vulnerability of the U. S. economy was exposed, and it has a wide range effect. The insurance industry is no exception.

The insurance industry estimates it sustained about \$40 billion in losses on September 11, more than from any previous single event. In fact, the cost is about double the next highest loss - Hurricane Andrew in 1992.

Because everyone thought this country was immune to acts of terrorism, insurance companies threw in terrorism insurance for free on property and casualty insurance policies. But, suddenly on September 11, terrorism insurance became a complex problem that had to be addressed - especially with the threat of future attacks.

As you likely know, insurance companies are required to have funds in reserve to cover large losses, and the industry has frequently been commended for the way it handled the claims that occurred because of the September 11 events.

But, most insurance companies say they won't have the reserves to pay claims of this magnitude again in the near future. So, many of them added a terrorism exclusion to commercial insurance policies and raised the rates of all lines of insurance.

However, one of the problems companies have is that it is almost impossible to determine how to assess the risks of terrorism. No one has yet been able to predict the potential harm terrorists can inflict.

However, there was no doubt that something had to be done to stabilize the insurance industry as the lack of

terrorism coverage began affecting not just the insurance industry and its commercial clients, but the total economy as well.

So, the insurance industry and others asked the U. S. Congress to establish a temporary backstop program. President Bush and a number of members of the U. S. Congress agreed this was a critical component of homeland security.

Legislation was introduced in the House of Representatives and Senate with input from members of The Professional Insurance Agents Association and others in the insurance industry as well as other business people, attorneys, and citizens. Months of negotiations began.

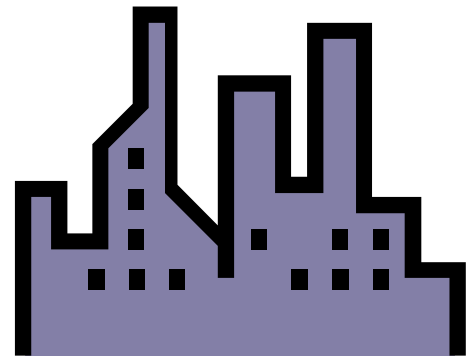
Finally, in November of 2002, both houses of Congress approved legislation called the Terrorism Risk Insurance Act of 2002, and the President signed it into law on November 26. It went into effect that day.

### What Is The Law?

The Terrorism Risk Insurance Act of 2002 will provide a federal government insurance backstop in the event of international terrorism. The Secretary of the Treasury is responsible for issuing regulations to administer the program. We now have interim rules.

The Treasury Secretary, Secretary of State, and Attorney General are to determine if the attack caused at least \$5 million in damages, involves violence and property destruction, and is perpetrated by someone acting on behalf of a foreign entity or interest. (It is interesting to note that the law says if such act "is committed in the course of a war declared by Congress, it is not terrorism. Then, it would not be covered by insurance.)

If an attack meets the definition, our government pays 90 percent of an



insurer's property-casualty losses after the company has paid a sizeable amount. The law is in effect for a little more than three years, expiring on December 31, 2005. It also stipulates how the insurance industry later repays the government.

The law does away with the terrorism exclusions. It requires insurance companies to offer terrorism coverage to commercial clients, but they can reinstate the exclusions if policyholders decline the coverage or do not pay the premium.

### What's Happening Now?

Insurance companies are sending notices to policyholders with pricing information for various coverages. Policyholders and companies then have 30 days to agree on the coverage. Examples include getting higher deductibles or less coverage for terrorism than for other kinds of claims in order to pay a lower premium.

Now, insurers are working with actuaries and scientific modeling to gauge potential losses and ascertain an accurate premium. No doubt, there will be adjustments in coverages and costs in the future.

The new law doesn't solve all of the problems, but it's a step in the right direction. All of us complain about our lawmakers' actions, but those who voted for the Terrorism Risk Insurance Act of 2002 are to be commended.

# Insurance Rates Rising

We mentioned in the article on the other side of this sheet that some insurance premiums have increased because of September 11, but that's not the only reason.

Policyholders are often not aware of the many hidden and subtle factors that find their way into claims costs and then into premiums. Some things cannot be controlled, but it's important that policyholders become more risk conscious and responsible.

Insurance is "funny" in a certain sense. Most businesses you buy from know what the product costs them. But, an insurance company doesn't know what the cost is until the end of the policy period, so it has to look to the past and factor an uncertainty into its current premiums.

When companies get your insurance premium, they have certain immediate costs like any business – salaries, commissions, communications equipment, paper, postage, and the like.

However, part of the money you pay for insurance is put aside to pay future claims. This money is invested in a variety of ways. If the economy is booming, most investments will do well, and the income from them helps hold down the premiums.

Recently, the stock market and the economy in general have not done well, and more of the claims cost is being added to premiums all of us have to pay.

But, let's look at a few other facts:

## Auto Rates

You know your auto insurance premiums depend on your driving record, the vehicle you drive, how much you drive, and your credit rating, but claims costs are raging.

Medical costs run \$15 to \$20 billion a year countrywide; typical costs for treating an auto crash victim are \$6,000 to \$9,000 – many are higher than that.

Auto repair costs significantly affect premiums. The cost of rebuilding a vehicle with parts manufactured by the car company is about 60 percent higher than "generic" parts. Using generic parts helps hold down the premium.

Higher jury awards in liability cases are a factor; awards rose from an average of \$187,000 in 1994 to \$269,000 in 2000 – an increase of 44 percent! Every two seconds, a lawsuit of some type is filed in this country. Insurance companies defend themselves and their policyholders from suits, even when they are frivolous.

Auto theft and fraud account for about 25 percent of all of the comprehensive insurance claims. There were more than a million auto thefts in 2000; that's one every 27 seconds. Fraud includes inflating claims, submitting claims that never occurred, and staging accidents. This activity seems to be growing.

Among the things drivers can do is wear their seatbelts and demand that those riding with them do too. They can install the required seating for their children. They can remember the slogans "none for the road" and "watch out for the other guy."

## Homeowners Insurance

It's our guess that more people have seen their homeowners' premiums increase than their auto premiums. Always premiums have depended on the type of construction, age of the home, and quality of local fire protection services. More recently, your credit rating has also played a part.

Catastrophe losses were much higher than normal during the 1990s. More than \$100 billion has been paid for catastrophe losses since 1990.

Home repair and building costs have a significant impact on insurance rates. Between 1998 and 2000, the cost of household repair increased 17.3 percent.

Mold has become a major factor in recent years. Mold itself is not new, but there has been a sharp increase in mold claims, and there have been multi-million dollar jury awards. In fact, the cost was five times more in 2001 than it was in 2000.

Some mold awards have received such wide publicity that it is thought that many of the claims are not legitimate.

The problem of mold has not been limited to homeowners coverage; it

has affected commercial insurance policies as well. The affordability and availability of property insurance is severely threatened by mold claims. Now, for example, some insurance companies refuse to write insurance on a property that has had water damage.

Among the things homeowners can do to protect themselves against loss is to remember that insurance is not a home-maintenance contract. Your insurance company and insurance agent assume you will make house repairs as they are needed and will use your property insurance coverage for only unusual or catastrophic events.

## Asbestos Claims

Asbestos, once considered a "miracle mineral," was widely used in building products for thousands of homes and industries, but in 1964, a link was established between asbestos dust and various diseases.

Since that time, those who produced asbestos products have been sued by those who were impaired by exposure to it, as well as by thousands who were not.

Most of the asbestos producers are bankrupt, and now compensation is being sought from companies only peripherally connected to asbestos. Insurance companies have paid and continue to pay claims, causing a devastating effect on not just the insurance industry, but also all of the economy.

It is estimated that the cost of asbestos claims to the insurance industry will be more than those paid because of September 11.

If you have questions about your insurance premiums at any time, contact us for an explanation.

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