One Year Later:
The Effects of 9/11 on Commercial Insurance Rates and Availability in New York City

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November 13, 2002

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My Fellow New Yorkers:

Just 14 months ago, our City suffered a terrible tragedy. The attack on the World Trade Center was, and remains, an immense human catastrophe that caused an unprecedented loss of life.

The attack also had a profound impact on New York City's economy. My office estimated the cost of the World Trade Center attack to New York City's economy at between $83 and $95 billion, depending on the total number of jobs that relocate to other areas. The City's ability to recover will rely to a large degree on the vitality of its business sector, which is directly affected by the price and availability of commercial insurance.

For this reason, I directed my staff to investigate the effects of September 11th on the cost and supply of commercial property and casualty insurance available to the City's businesses and to make recommendations concerning ways to mitigate those effects. The results of that study are presented in this report: "One Year Later: The Effects of 9/11 on Commercial Insurance Rates and Availability in New York City."

My staff conducted a survey of insurance agents and brokers serving businesses located throughout the five boroughs and asked them to report rate increases and availability for nine lines of property and casualty coverage in the year before September 11th and the year following the attack.

The results of the survey are striking. The survey respondents reported a dramatic increase in premiums for businesses of all sizes and in all lines of insurance in New York City after the terrorist attack. Premiums for large accounts following September 11th increased by an average of 73.3% per policy compared with 11.4% the previous year. Medium-sized accounts experienced an average 49.5% increase after the attack, compared with 9.4% in 2000-2001, and premiums for small accounts went up by 39.0%, compared with 9.7% during the previous year. The agents and brokers consistently reported that the greatest increase in premiums were for businesses located in high-rise buildings in Manhattan, particularly those in, or even near, landmark or "trophy" properties considered by insurers to be at risk of becoming terrorist targets.

By way of comparison, the Insurance Information Institute recently estimated that premiums across the country rose by 30% in 2002, and stated that approximately half of that increase was related to the terrorist attack.

My staff's investigation also showed a decline in availability for accounts of all sizes following the attack. The percentage of respondents who reported that coverage was either "readily available" or "somewhat available" for large accounts fell from 84.1% for the year before September 11th to 20.2% for the following year. Medium-sized accounts also became significantly harder to insure, with 87.1% of respondents finding coverage "readily available" or "somewhat available" before September 11th and only 28.0% making that assessment afterward. Similarly, the number of respondents reporting that coverage for small accounts was "readily" or "somewhat available" decreased from 85.2% for the year before September 11th to 34.3% for the period after the attack.

To better understand the impact on large policyholders, my staff also spoke with members of the Real Estate Board of New York, which includes many of the largest policyholders in New York City. The survey considered all policies over $1 million in the same category of "large accounts" and my staff believed that the responses might not have reflected the experience of the accounts having premiums in the multiple millions of dollars. REBNY members reported premium increases in excess of 700% and severe limitations on the coverage available, particularly for well-known or "trophy" properties.

The tightening of the insurance market shown by the report threatens to hold back the economic performance of New York City for years. Financial resources, which otherwise could be used for economically beneficial purposes, such as improving productivity, expanding businesses or improving wages and benefits, instead are being diverted to pay increased premiums. Moreover, maintenance of adequate insurance coverage is, among other things, a prerequisite for businesses to secure financing to establish new companies, to expand existing business and to accommodate seasonal variations in cash flow. The continued availability of reasonably priced insurance also will be a factor in corporate location decisions as New York City competes for businesses with other communities where insurance is less expensive and easier to obtain.

There are a number of actions available to both government and the private sector that would help to ameliorate the effects of September 11th on the insurance market:

- <u>Federal Terrorism Insurance</u>. The federal government should establish a temporary terrorism insurance program that would provide loans or governmental reinsurance for insurance companies writing terrorism coverage. Such a program would go far in increasing the confidence of the insurance industry in writing coverage in New York City and elsewhere, which would result in lower premiums and greater availability.

- Expansion of Risk Financing Options. As an alternative to purchasing insurance in the commercial market, large companies, groups of companies or industry associations should consider establishing alternative financing strategies, including purchasing groups, reciprocals, other self insurance arrangements, and captive insurance companies. The State Insurance Department should encourage expansion of these alternatives, which will allow businesses to mitigate the effects of price increases and supply shortages in the retail market.

- New Insurance Companies. States that believe that insurance premiums are too high or insufficiently available can encourage the creation of new insurance companies. This has happened in many states for the sale of workers' compensation and medical malpractice insurance and should be considered in New York State in order to create more capacity in the commercial insurance market.

- Risk Reduction. Companies and local governments, including New York City, are investing in physical improvements and in increased coverage by security personnel to improve security and to reduce risks. This effort should continue in the City so that local businesses will become more attractive to insurers, which presumably will result in lower premiums and greater availability.

This report sheds light on a serious secondary effect of the terrorist attack that requires immediate and aggressive intervention. New York City's political and business leadership must immediately seek the legislative and regulatory relief necessary to ensure the well being of the City and its businesses.

Very truly yours,

William C. Thompson, Jr.

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One Year Later: The Effects of 9/11 on Commercial Insurance Rates and Availability in New York City

Introduction and Background

Objective of the Study

In the aftermath of September 11th, the media reported dramatic increases in the cost of insurance and decreasing availability of coverage nationally. The Comptroller's Office began receiving anecdotal reports suggesting that the increases were even more severe in New York City, where businesses were already struggling as a result of the local economic downturn caused by the attack and the general dip in both the local and national economies that began earlier in 2001.

In view of these reports, the Comptroller set out to measure the effects of the World Trade Center attack on the rates and availability of commercial property and casualty insurance in the City.

After contacting several sources in the insurance industry, staff from the Comptroller's Office of Policy Management determined that statistics that would permit conclusions to be drawn about the costs and availability of commercial insurance in New York City were not readily obtainable. The Council of Insurance Agents and Brokers (CIAB) publishes a quarterly rate survey of its membership to estimate the increase in premiums nationwide and regionally, but does not separately calculate statistics for New York City and does not seek to measure availability. After discussing with CIAB and others the possibility of a reasonable estimate of these data for New York City, it was determined that the most practical way to obtain this information was to conduct a survey of agents and brokers serving businesses in the five boroughs. Accordingly, the Comptroller's Office designed and issued a survey to agents and brokers serving businesses in New York City seeking information about changes in price and availability of nine lines of property and casualty coverage since September 11, 2001 as compared with the previous year.[1] (See Appendix A for a copy of the survey document.)

[1]The Comptroller's Office contacted the major membership organizations representing agents and brokers in the metropolitan area. Five organizations agreed to cooperate in the distribution of the survey to their membership, including CIAB, The Independent Brokers Association of New York (IBANY), The Independent Insurance Agents Association of New York (IIAANY), The Professional Insurance Agents of New York (PIANY), and The Professional Insurance Wholesalers Association (PIWA). Each organization provided the Comptroller with access to its membership in New York City and the surrounding counties by e-mail and/or surface mail.

Property and Casualty Overview

Most lines of property and casualty insurance are highly cyclical, with rates and profits increasing for a time and then decreasing, usually over several years. During the 1990s, the property and casualty insurance industry experienced a "soft market," meaning that many companies were writing insurance (strong capacity and competition), and premiums were low because of reduced losses and/or a strong return on investment.[2] During this period, the stock market rose sharply, interest rates were high and property and casualty insurance companies were able to obtain a good return on the short-term investments into which they placed client premiums. As a result, premiums did not rise as much as they would have in a lower-return environment. In fact, in many cases premiums fell significantly to the point where most experts agree that they were artificially low. This was both a profitable time for property and casualty insurers and a good market for businesses purchasing insurance.[3]

An increase in commercial premiums and a reduction in availability began in 2000 as a result of reduced returns from investments. The lower return on investment also meant that less capital was available to be invested in property and casualty insurance. Premiums continued to increase steadily in 2001.[4] As certain lines of insurance suffered severe losses, property and casualty companies reduced the amount of insurance they were writing and others went out of business entirely. The result was a transition to a "hard market," which brought with it an increase in premiums even before September 11th. Premiums rose sharply after the September 11 terrorist attacks as an additional factor came into play, namely a sense that risk exposures were higher than previously estimated.[5]

Some have argued that this phenomenon has been particularly acute after September 11th in New York State, where the State Insurance Department has refused to allow insurance carriers authorized to write primary insurance business in the State, known as "admitted carriers," to exclude terrorism coverage from property and casualty policies. This policy leaves admitted carriers with few options. If they write policies with coverage for terrorist acts, reinsurers, who are not regulated by the State Insurance Department, refuse to cover those losses, leaving the primary insurers liable for the entire loss. If the admitted carriers cannot accept this potential loss exposure, they cannot renew existing policies or write new ones, resulting in constraints on supply and increased prices for coverage.

Survey Findings

The survey responses demonstrated a dramatic increase in premiums for new and renewal accounts for businesses of all sizes and in all lines of insurance in New York City after the September 11th terrorist attack. Premiums for large accounts following September 11th increased by an average of 73.3% per policy, while medium-sized accounts experienced an

[2] C. Loomis, "Insurance After 9/11: In the property and casualty business, terrorism is an evolving crisis -- and an opportunity," *Fortune*, June 10, 2002.
[3] Robert P. Hartwig, Ph.D., "Industry Financials and Outlook" Reports, The Insurance Information Institute, 1999 - 2000.
[4] S. Sclafane, "Industry Still Strong but Prices Soar," *National Underwriter*, September 9, 2002, 12.
[5] Silvana Vlacich, "Prognosis on Risk Management and Insurance," *The CPA Journal*, 72:5 (May 2002).

average 49.5% increase and premiums for small accounts went up by 39.0% during the same period. (See Graph A and Appendix B).

The agents and brokers responding to the survey consistently reported that they saw the greatest increase in premiums for businesses located in high-rise buildings in Manhattan, particularly those in, or even near, landmark or "trophy" properties considered by insurers to be at risk of becoming terrorist targets. Discussions with members of New York City's real estate community confirmed this information; indeed, in a meeting with the Comptroller's staff, property owners, managers and insurance brokers belonging to the Real Estate Board of New York (REBNY) described in detail the serious problems many commercial tenants were having in obtaining affordable coverage.[6]

For comparison purposes, it is useful to consider current estimates of cost increases for premiums across the country. Robert P. Hartwig, Ph. D., the Chief Economist for the Insurance Information Institute (I.I.I.), recently estimated that the cost of risk rose nationally by 15% in 2001 and 30% in 2002, and asserted that roughly half of the 2002 increase was related to the terrorist attack.[7] Based on these figures, New York City experienced premium increases following September 11th that were markedly higher than the rest of the country.

In addition to the increase in premiums, there was a corresponding decline in availability for accounts of all sizes following the attack, which many respondents reported as more troubling. Agents and brokers consistently described difficulty in finding coverage for companies at rates comparable to the previous year, or, in many cases, coverage at any price. For large accounts, the percentage of respondents who reported that coverage was either "readily available" or "somewhat available" fell from 84.1% for the year before September 11th to 20.2% for the year following the attack.[8] Medium-sized accounts also showed a significant rise in scarcity, with 87.1% of respondents finding coverage "readily available" or "somewhat available" before September 11th and only 28.0% making that assessment afterward. Similarly, the number of respondents reporting that coverage for small accounts was "readily" or "somewhat

[6] In order to encourage as many agents and brokers to respond as possible, the survey instrument was divided into questions on only three categories of accounts: small, medium and large. Small accounts were defined as those with less than $50,000 in premium, medium-sized accounts as having $50,000 to $1,000,000 in premium, and large accounts as having more than $1,000,000 in premium. Some respondents expressed concern that the broad categories used did not represent the extremes of the market (e.g., policies with premiums in the multiple millions of dollars and those with premiums in the hundreds of dollars). In an effort to ascertain the limitations of the data, on October 17, 2002, the Comptroller's staff met with real estate owners, managers and insurance brokers associated with REBNY, which includes many of the largest policy-holders in New York City, and collected anecdotal information concerning their experience obtaining and renewing insurance after September 11th. In all cases, the reported premium increases were markedly higher than even the greatest increases reflected in the survey, and the REBNY members described significantly greater difficulty obtaining coverage than reported by survey respondents. However, the information obtained from these discussions was not tabulated as part of the survey data and is not included in the final survey results.

[7] Robert P. Hartwig, "September 11, 2001: The First Year; One Hundred Minutes of Terror that Changed the Global Insurance Industry Forever," Insurance Information Institute, September 5, 2002, p. 24. His estimates were based in part on CIAB data.

[8] Survey participants were asked to rate availability of coverage on a five-point scale, with 1 indicating "readily available," 2 indicating "somewhat available," 3 indicating "limited availability," 4 indicating "very limited availability," and 5 indicating "not available."

available" decreased from 85.2% for the year before September 11th to 34.3% for the period after the attack. (See Graph B and Appendix B.)

Respondents cited the decline in the number of insurance companies willing to write additional business or renew existing business in New York City, especially Manhattan, because of September 11th. The greatest difficulty, according to the agents and brokers who commented, was in placing large commercial accounts and large residential property risks. However, there was no line of insurance or size of policy for which availability improved.

I. Differences in Premiums and Availability by Account Size

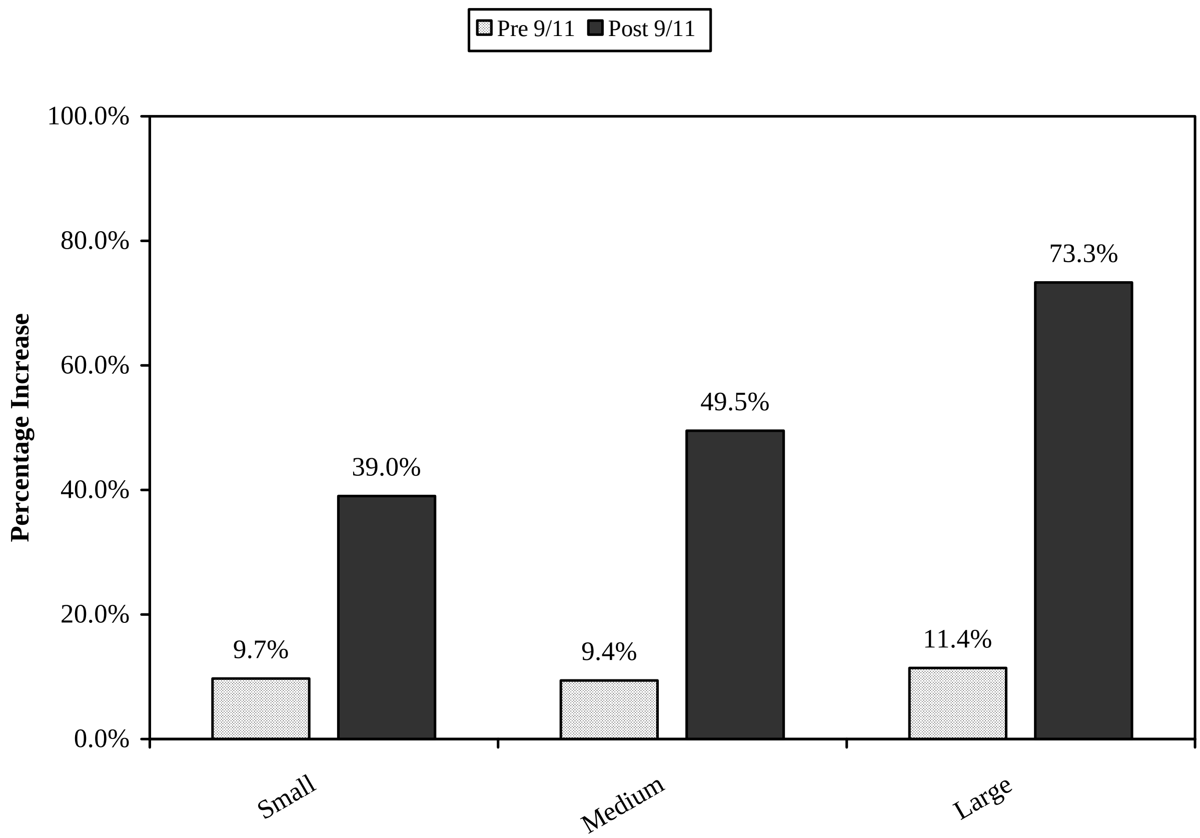
The survey showed that large-sized accounts, having premiums over $1,000,000, experienced the greatest increase in premiums following the terrorist attack, although they also had experienced the greatest increase in premiums the previous year (11.4%). These businesses had an average increase of 73.3% since September 11, 2001, which was significantly greater than the increases experienced by medium and small businesses. (See Graph A.)

The large accounts also showed a significant decline in availability, with the percentage of respondents reporting coverage as being either "readily available" or "somewhat available" falling from 84.1% before September 11, 2001 to only 20.2% afterward – a difference of 63.9%. According to the survey respondents, insurers are reevaluating each risk, increasing their estimate of exposures, and reducing the amount of insurance they will write (i.e., the policy limits) for a particular company, or within particular geographic locations (a building or even a zip code). (See Graph B.)

The agents and brokers reported that medium-sized businesses, those paying premiums between $50,000 and $1,000,000, experienced an average increase in premiums of 49.5% since September 11, 2001, compared with an average increase of 9.4% in the previous year. They also reported a pronounced decline in availability, with the percentage of respondents stating that coverage was either "readily available" or "somewhat available" decreasing from 87.1% to 28.0% after September 11, 2001 – a difference of 59.1%.

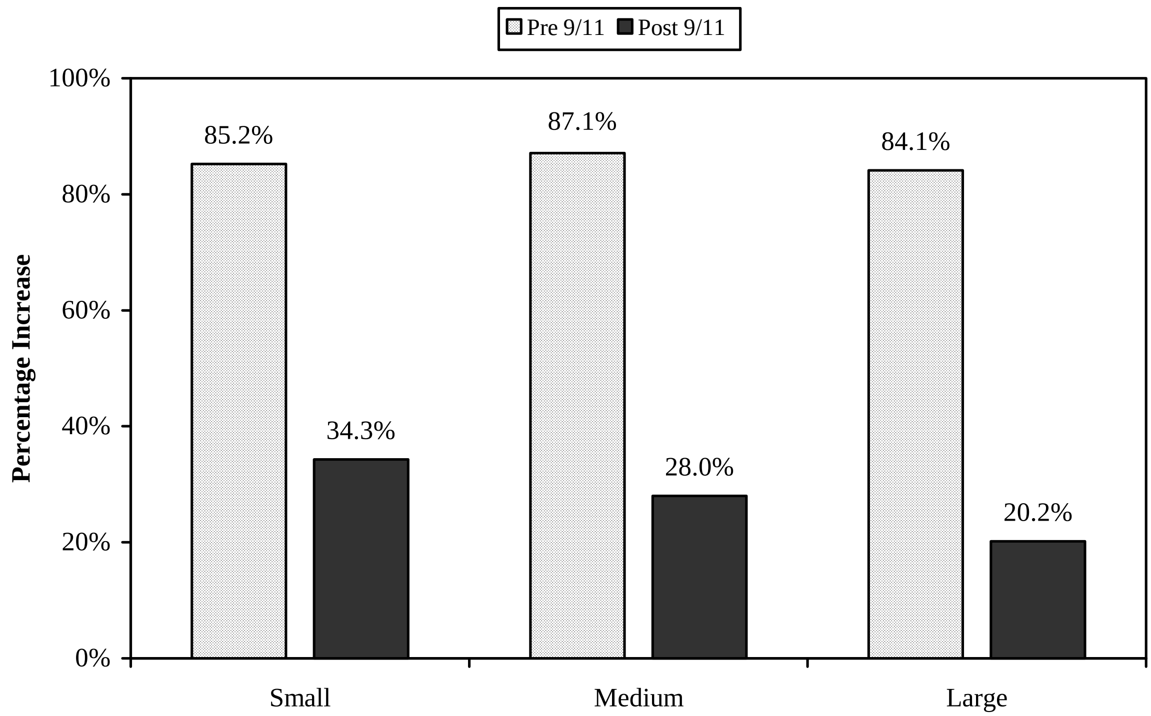
The survey showed that since September 11, 2001, small accounts experienced the lowest average increase in premiums (39.0%) and the least decline in availability. The premium increase represents more than four times the rate of increase from the previous renewal period (9.7%). The number of respondents reporting coverage as being either "readily available" or "somewhat available" dropped from 85.2% to 34.3% -- a difference of 50.9%. Although the small accounts have lower premiums and therefore a smaller dollar increase than the larger accounts, many of these businesses may be at greater peril from rate increases since they are least likely to have the resources to tolerate significantly increased costs. Indeed, one agent commented that one small manufacturing client in Queens with 80 employees had a 300% increase in premium and was relocating his business to Florida, and noted that another "manufacturer in Queens can't get insurance at all. He may have to go out of business."

Graph A: Average Premium Increases, by Account Size



Source: Responses to Comptroller's survey from 93 independent insurance agents and brokers representing more than 63,000 new and renewal commercial accounts written in New York City during each of the relevant time periods. Results are given as unweighted averages and rounded to the nearest tenth of a point. Small accounts are defined as those with less than $50,000 in premium, medium-sized accounts as having $50,000 to $1,000,000 in premium, and large accounts as having more than $1,000,000 in premium.

Graph B: Availability of Insurance, by Account Size: Percentage of Respondents Rating Insurance as Being "Readily Available" or "Somewhat Available"



Source: Responses to Comptroller's survey from 93 independent insurance agents and brokers representing more than 63,000 new and renewal commercial accounts written in New York City during each of the relevant time periods. Survey participants rated availability as follows: 1= readily available, 2= somewhat available, 3= limited availability, 4= very limited availability, and 5= not available. This graph illustrates the percentage of respondents who rated insurance as either "readily available" or "somewhat available" and provides results rounded to the tenth of a point.

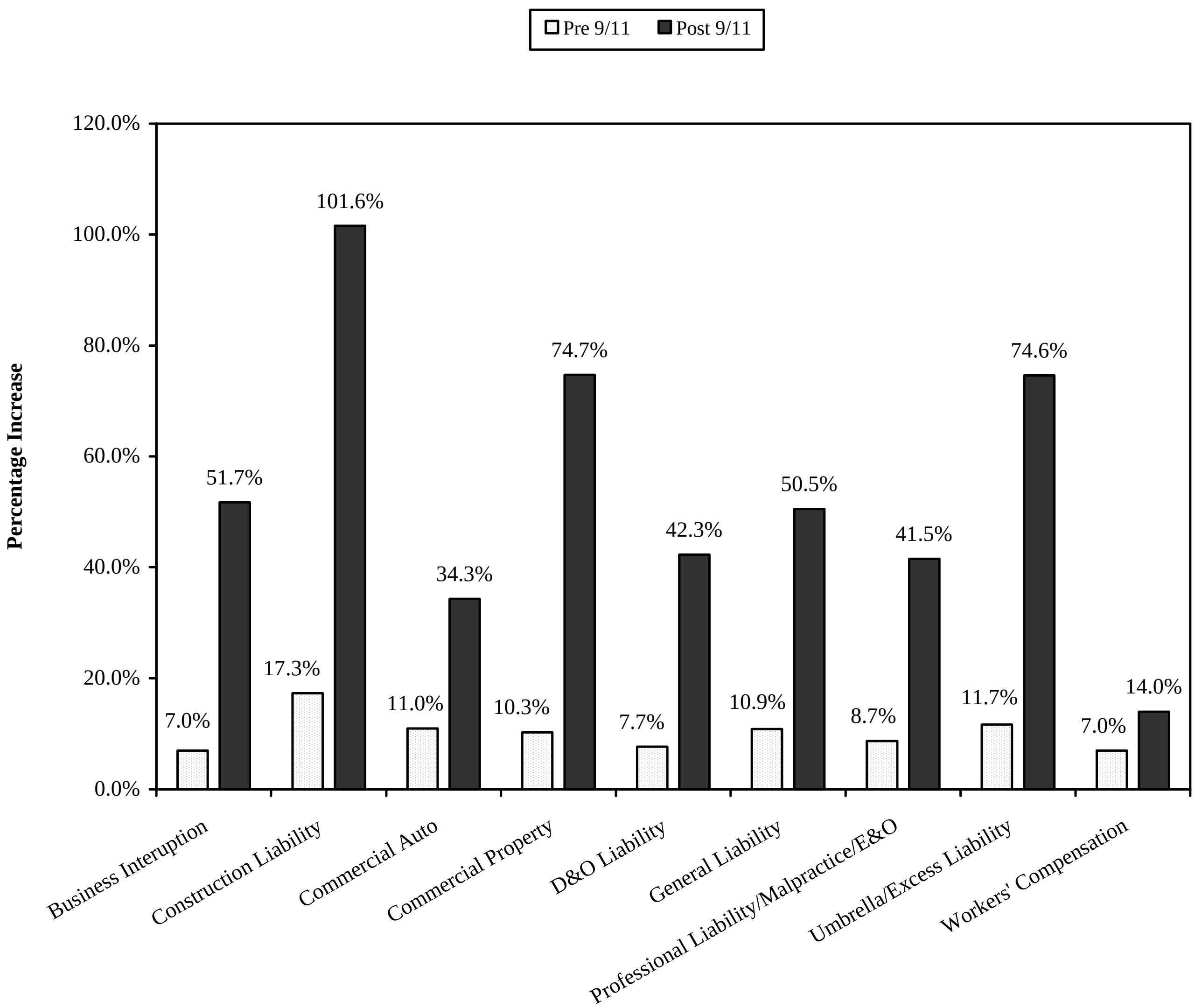
II. Differences in Premiums and Availability by Line

In addition to seeking information concerning the changes in premiums and availability by the size of the account, the survey asked respondents to report changes by the lines or types of insurance sold. Changes in premiums and availability varied widely by insurance line. The agents and brokers reported in their comments that some of these variations had to do with the changes in underwriting evaluation of the risks as a result of the terrorist attack of September 11th and some lines increased for other reasons.

The graphs that follow illustrate the changes in premiums and availability by line of insurance. Graph C illustrates the average percentage increase in premiums for each of the two years in the survey, September 11, 2000 to September 10, 2001 and September 11, 2001 to the present.

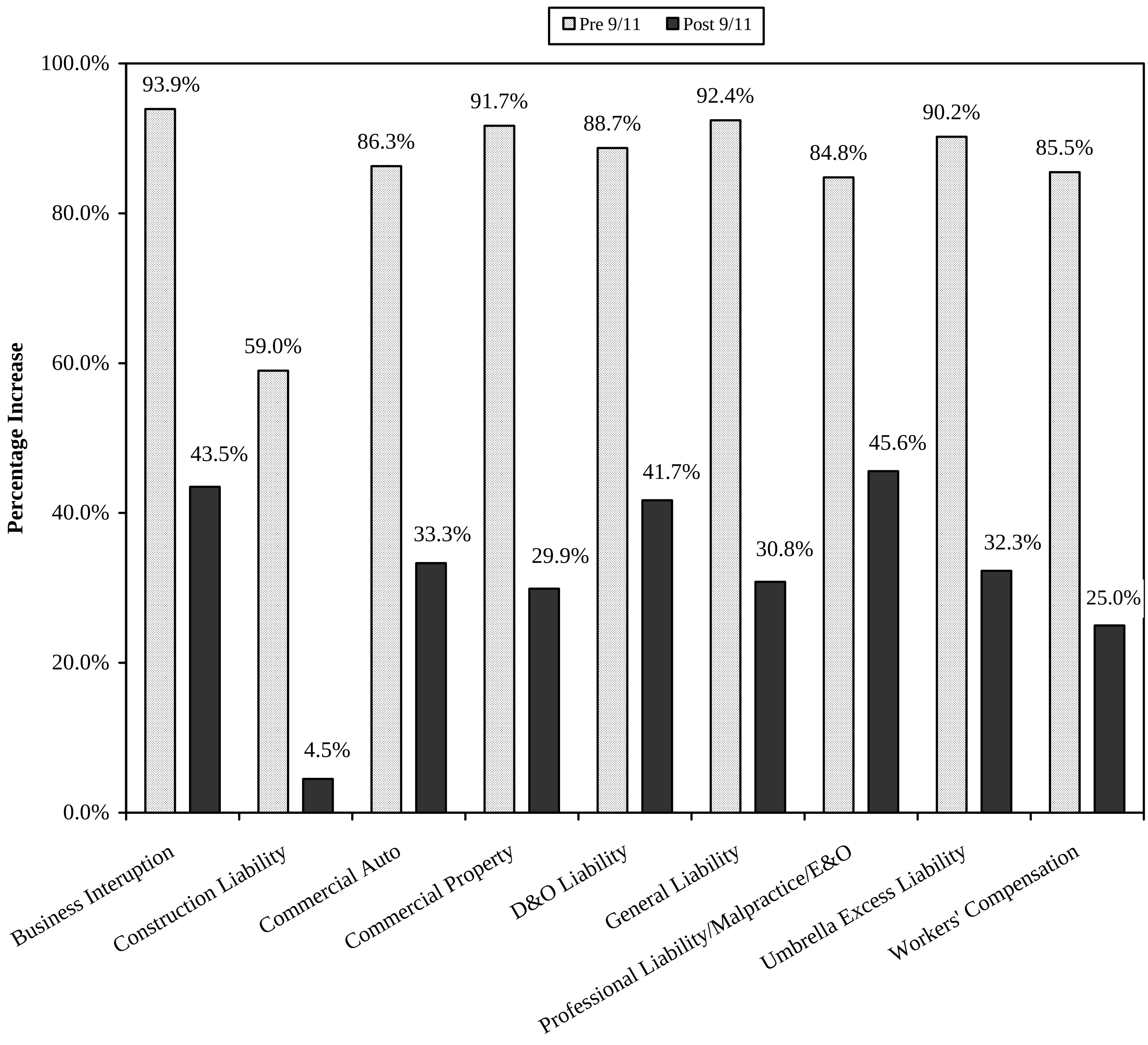
Graph D illustrates the increased difficulty agents and brokers reported in placing commercial insurance for each line of insurance after September 11, 2001, as compared with the year from September 11, 2000 to September 10, 2001. Graph D shows, by line of insurance, the percentage of agents and brokers who characterized coverage during these periods as being either "readily available" or "somewhat available".

Graph C: Average Premium Increases, by Line, for All Accounts



Source: Responses to Comptroller's survey from 93 independent insurance agents and brokers representing more than 63,000 new and renewal commercial accounts written in New York City during each of the relevant time periods. Results are given as unweighted averages and rounded to the nearest tenth of a point. Small accounts are defined as those with less than $50,000 in premium, medium-sized accounts as having $50,000 to $1,000,000 in premium, and large accounts as having more than $1,000,000 in premium.

Graph D: Availability of Insurance, by Line, for All Accounts: Percentage of Respondents Rating Insurance as Being "Readily Available" or "Somewhat Available"



Source: Responses to Comptroller's survey from 93 independent insurance agents and brokers representing more than 63,000 new and renewal commercial accounts written in New York City during each of the relevant time periods. Survey participants rated availability as follows: 1= readily available, 2= somewhat available, 3= limited availability, 4= very limited availability, and 5= not available. This graph illustrates the percent of respondents who rated insurance as either “readily available” or “somewhat available” and provides results rounded to the tenth of a point.

A. Lines Most Affected by the September 11th Terrorist Attack: Business Interruption, Commercial Property, General Liability, Umbrella and Excess Liability and Workers' Compensation

Survey respondents reported that, although some lines of insurance showed unprecedented increases in premiums after September 11th, some of these increases were not a result of the terrorist attack but had other explanations. The lines that experienced increases that were most clearly attributed by the respondents to the terrorist attack were business interruption, commercial property, general liability, umbrella and excess liability and workers' compensation insurance.

Survey respondents reported that these five lines have been very difficult to place in New York City since September 11th, particularly for large accounts and businesses located in or near "trophy" properties. In the aftermath of the attack, the media have reported on numerous cases in which insurance companies have reduced their exposure through non-renewal of policies where their exposure no longer meets the company's new criteria. For instance, the Fireman's Fund Insurance Company recently refused to renew the property and automobile liability coverage for the Uniformed Firefighters Association of New York City, the firefighters' union, due to "increased hazard and exposures to loss." [9]

Considering these five lines of insurance separately, the average increase in premiums after the attack was 53.1% compared with a 9.4% increase in 2000-2001, and the number of respondents reporting coverage as being either "readily available" or "somewhat available" declined following September 11th from 90.8% to 32.0%, a net difference of 58.8%. Without workers' compensation, which had lower premium increases because of the availability of a state fund (see Point 3 below), the rate increase for the remaining four lines since September 11th was 62.9%, compared with 9.9% the previous year.

1. Commercial Property and Business Interruption

Rates for commercial property and business interruption coverage, which are sometimes included in the same policy, were clearly affected by the terrorist attack. The I.I.I. recently estimated that more than 50% of the $40.2 billion in insured losses from September 11th will be on business interruption and property policies, including $11 billion (27%) in business interruption and $9.5 billion (24%) in property claims.[10] Survey respondents reported that premiums for business interruption increased 51.7% and commercial property premiums increased a notable 74.7% after September 11, 2001 as compared with 7.0% and 10.3% respectively in the previous year. Indeed, following the attack, large accounts showed an average 108.8% increase in premiums for commercial property coverage in the City. Even this large increase is significantly below reported increases of between 800% and 1700% on insurance for some of the City's largest buildings, however, particularly for "trophy" or

[9] "A Slap to the Bravest," *New York Daily News*, August 15, 2002.
[10] "9/11 and Insurance, One Year Later -- Terror Attacks Most Complex Disaster in History", Insurance Information Institute Press Release, September 5, 2002.

landmark properties.[11] The difference can be explained by the fact that the survey considered all policies over $1 million in the same category, so the responses may not have reflected the experience of the largest accounts having premiums in the multiple millions of dollars. Moreover, the survey received the fewest responses in the "large accounts" category, which also might have resulted in under-representation of the largest customers in New York City's insurance market.

The decline in availability for commercial property and business interruption coverage following the attack also was significant: the number of respondents reporting commercial property coverage as being either "readily available" or "somewhat available" fell from 91.7% to 29.9% – a difference of 61.8%. Business interruption insurance also became markedly more scarce, with a decline from 93.9% to 43.5% of respondents rating it as "readily available" or "somewhat available" after September 11, 2001 – a difference of 50.4%. However, in both cases, large accounts experienced the most difficulty obtaining coverage, with a net decrease in the percentage of respondents rating coverage as "readily" or "somewhat available" of 78.6% for commercial property and 76.9% for business interruption.

It should be noted that before September 11th, terrorism coverage had been included in the property and business interruption policies, although it was not a separately rated (charged) exposure. The insurance companies did not charge for this coverage because they had insufficient experience to estimate the frequency and severity of potential losses, which means that on September 11, 2001 they incurred losses for which they had not collected sufficient premiums in the past. The insurance companies are now working to develop estimates of potential losses in the event of future terrorist attacks, which will eventually become part of the rating process, although in the interim insurers are hesitant to insure exposures they cannot fully quantify. This uncertainty is reflected in the significant increases in premiums and decrease in availability for these lines since the terrorist attack.

Anecdotal reports indicate that non-admitted carriers, which are not subject to the same regulations as the admitted carriers, are providing some terrorism coverage at tremendously increased premiums, although reports persist that some properties have become extremely difficult to adequately insure.[12] For instance, in discussions with the Comptroller's staff, the representative of one landmark property said that its property insurance premium had increased almost 700% without terrorism coverage for one-third of the property's value. He could only get terrorism coverage for 10% of the previous limits and the rate for this reduced terrorism coverage was so high he would not even discuss it. Another property owner reported that he approached 25 insurers in the domestic and foreign market, none of whom was interested in insuring his portfolio of properties at any price. Owners and managers of large properties who received competitive bids from several insurers in the past said that they had difficulty finding complete coverage even through combining coverage from several different insurers. According to one insurance broker, many real estate companies have had to leave large gaps in their coverage, essentially self-insuring for millions of dollars. This

[11] Comptroller's staff meeting with members of the Real Estate Board of New York (REBNY) on October 17, 2002. The information obtained from discussions with members of REBNY was not tabulated as part of the survey data and is not included in the final survey results.

[12] Meeting with REBNY members, October 17, 2002.

practice places the real estate industry in a precarious position in the event of another large-scale catastrophe.

2. General Liability, Umbrella and Excess Liability

The massive losses from the terrorist attack also had a profound effect on rates for liability insurance. According to the I.I.I., $10 billion or 25% of all insured losses from September 11th will take the form of liability claims. Following the September 11th attack, premiums for general liability coverage increased by 50.5%, compared with a 10.9% increase in the previous year and the percentage of respondents rating coverage as "readily" or "somewhat available" declined from 92.4% to 30.8%, a difference of 61.6%. The greatest decline in availability was reported for medium-sized accounts, where the number of respondents rating the coverage as "readily" or "somewhat available" fell from 90.2% to 25.5% – a difference of 64.7%.

Even more dramatic, umbrella and excess liability premiums increased by 74.6% after September 11, 2001 compared with 11.7% the previous year. The greatest change in premiums was reported for large accounts, which experienced a 104% increase, in contrast with a 13.2% increase in 2001-2002. The number of respondents rating this coverage as "readily" or "somewhat available" for accounts of all sizes declined from 90.2% to 32.3% – a difference of 57.9%.

3. Workers' Compensation

Survey results indicate that workers' compensation premiums increased by 14% after September 11, 2001, which is a much lower rate than for any of the other lines of insurance studied. This may be the result of the availability of the New York State Insurance Fund, which historically has charged premiums that are lower than those charged by the retail market. The State Insurance Fund insured 35% of the workers' compensation risk in the State for the year ending December 31, 2000.[13] In fact, the State Insurance Fund experienced a substantial increase in applications for coverage since September 11th as well as a 20% increase in business.[14] However, the State Fund, like the retail carriers, has reduced certain rate credits it offers, resulting in higher premiums for businesses it insures. Another possible explanation for the lower rate of increase in premiums for this line of insurance, cited by some sources (including a representative of the New York State Builder's Association),[15] is that the rate structure currently in place is inadequate to cover losses and expenses.

The percentage of respondents who ranked workers' compensation coverage as being "readily" or "somewhat available" declined from 85.5% in the year before September 11th to 25.0% afterward – a 60.5% difference. One agent reported that an insurer he worked with

[13] The most recent data available. "2000 Market Share, Individual Property/ Casualty Lines," New York State Insurance Department, October 31, 2001, p. 60.
[14] Telephone interview with Vincent Trainolo, Director of Underwriting, New York State Insurance Fund, September 10, 2002.
[15] Telephone interview with Philip La Rocque, Executive Vice President, New York State Builders Association, September 16, 2002.

raised the minimum premium for workers' compensation from $1,000 to $5,000, which made it impossible for him to renew small business policies with this company.

Workers' compensation policies also have been non-renewed by the private insurance market as a result of changed guidelines instituted in response to the September 11th attack. *The Wall Street Journal* reported that workers' compensation coverage is becoming increasingly hard to find as “insurers reach their maximum tolerance for coverage in certain locations.”[16] Consistent with this account, one broker commented that the insurance companies are no longer willing to cover large numbers of people within a geographic area, whether that is a zip code, a city block, or even a large office building. This means that if an insurer has a policy with one large employer in a particular area, other employers in the same location will not be able to obtain workers' compensation coverage from that company.[17]

B. Lines Affected by Factors other than the Terrorist Attack

1. Construction Liability

Construction liability premiums showed an increase of 101.6% since September 11, 2001, which was the highest average premium increase reported in the survey, although its 2002-2001 increase of 17.3% was also the highest during that period. In addition, there was a pronounced reduction in supply, with the number of agents and brokers reporting coverage as being “readily” or “somewhat available” declining from 59.0% before September 11, 2001 to 4.5% afterward (a 54.5% difference). This line of insurance was the topic of comments by many of the responding agents and brokers, who attributed most of the significant increase in premiums for this line to NYS Labor Law §§ 240 and 241, known as the “Safe Place to Work” laws, and not the terrorist attack. This legislation imposes greatly enhanced liability on owners and general contractors for workplace injuries. According to the agents and brokers, this legislation has made it increasingly difficult for insurers to effectively project future claims.

Although the "Safe Place to Work" statutes do increase potential liability for general contractors and property owners, this does not explain the extent of the increase in premiums reflected in our survey. The CIAB quarterly rate survey, published July 18, 2002, showed that construction liability premiums across the nation increased dramatically, with 57% of the brokers reporting increases of over 30%, and 19% of the brokers reporting increases over 50%. Indeed, construction liability insurance showed the second highest rate of increase of all the lines CIAB studied. Further review of the responses to our survey and discussions with several experts in the construction and insurance field indicates that the increase in this line of insurance is most likely a result of a combination of factors, including increased losses, changing legal climate (including an increase in mold claims), withdrawal of several insurers from the market, and the impact of the terrorist attack.

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[16] "Workers' Comp Insurers Shy from Businesses in Big Cities", *The Wall Street Journal*, July 22, 2002.

[17] Members of REBNY, in their October 17, 2002 meeting with the Comptroller’s staff, also made this observation.

2. Commercial Auto

The agents and brokers responding to the survey reported an average increase in premiums for commercial automobile coverage of 34.3% since September 11, 2001 as compared with 11.0% in the prior year. Many respondents attributed this increase not to the losses the insurance companies suffered as a result of September 11th, but to declining availability of coverage. According to the agents and brokers, several companies have stopped offering this coverage as a result of higher than anticipated losses unrelated to the terrorist attack and the contraction in capital available to underwrite these risks. The number of respondents reporting coverage as being "readily" or "somewhat available" fell by from 86.3% in the year before September 11, 2001 to 33.3% the year after – a 53.0% difference. In his response to the survey, one agent stated that he had only one market left for commercial auto coverage. Another agent commented that "[c]ommercial auto markets are dwindling down to a very few creating substantial premium [increases] for less coverage." This contraction in the market is having a serious impact on many businesses. *Newsday* reported on August 17, 2002 that an operator of school buses in New York City and across Long Island filed for bankruptcy, in part as a result of "skyrocketing costs for automobile liability insurance."[18]

3. Other Lines (D & O, Professional Liability)

The final two lines of insurance studied showed increases that survey responses and media sources all attribute primarily to higher than anticipated loss experience and the general hardening of the insurance market.

Survey responses showed that the cost of Directors and Officers Liability coverage increased by 42.3% in the period after September 11, 2001 in response to stockholder actions in the Enron, WorldCom and other company stock scandals. *The New York Times* reported on September 7, 2002 that, "…the big commercial insurance companies are cutting back sharply on liability coverage for American corporations, their directors, and senior executives." The *Times* quoted one attorney representing directors and officers as saying that "…protection is going to be increasingly difficult to get and companies are going to have to pay through the nose for it." The article states that the insurers expect to pay out $7.5 billion in losses this year under coverage for which they only collected $4.5 billion in premiums.

Professional liability premiums are also increasing in response to increased verdicts and settlements, decreases in investment income, and the rising cost of reinsurance.[19] Indeed, one broker described "a near crisis" in the medical malpractice area.[20]

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[18] "School Bus Corp. Files for Bankruptcy," *Newsday,* August 17, 2002.

[19] Conning Institutional Research Press Release on their study, "Medical Malpractice Insurance: A Prescription for Chaos", May 17, 2001.

[20] Council of Insurance Agents and Brokers News Release, "A Hard Market in Real Distress, The Council's Second Quarter 2002 Rate Survey Shows," July 18, 2002.

Conclusion

The effect of September 11th on the market for property and casualty coverage in New York City has been profound. The survey shows that premiums in the City have increased dramatically since the terrorist attack of September 11th. Large businesses, which represent the smallest number of the three categories of insured companies in the City, have a very large economic impact. They have experienced rate increases of more than 73% in the last year as well as significant limits on availability, which can be thought of as an infinite premium (no premium is viewed by insurance sellers as large enough to buy such insurance). This phenomenon was confirmed by discussions between the Comptroller's staff and members of REBNY, who encountered serious limitations on the coverage available, but who also were confronted with premium increases in excess of 700%. The survey shows that medium–sized and small businesses experienced average increases of close to 50% and 40% respectively, and both also experienced a tightening of supply.

However, the events of September 11th do not account for all changes reported by participants in the survey. Higher than anticipated losses and the New York City and national economies, which were already in recession for three quarters before the attacks, have also contributed to rising prices and a tightening insurance market.

Whatever the cause, higher premiums for property and casualty insurance and scarcity of coverage can serve as a drag on economic performance in New York City for years to come. Financial resources, which otherwise could be used for economically beneficial purposes, such as improving productivity, expanding businesses or improving wages and benefits, instead are being diverted to pay increased premiums. Moreover, maintenance of adequate insurance coverage is, among other things, a prerequisite for businesses to secure financing to establish new companies, to expand existing business and to contend with variations in cash flow. If insurance coverage is not available, financial institutions will not make loans, and if the cost of coverage is too high, the pace of economic recovery and expansion will be slowed. The continued availability of reasonably priced insurance also will be a factor in corporate location decisions as New York City competes for businesses with other communities in which insurance is less expensive and easier to obtain or that otherwise have lower costs.

Businesses that cannot purchase insurance at a reasonable price ultimately will be forced to make some difficult choices:

- operate without adequate coverage, which may make it impossible for them to borrow for expansion or even to meet a seasonal cash-flow shortage;
- reduce their exposure to risk through increased security, including physical plant alterations and stricter access procedures;
- reduce their costs through layoffs or other measures;
- increase their prices, becoming less competitive;
- relocate outside New York City; or,
- Close down entirely.

All of these possibilities would be damaging to New York City’s economy.

As insurers seek to recoup their catastrophic losses from the events of September 11th and limit further exposure, the City's businesses will continue to struggle to secure appropriate and affordable coverage. Indeed, reports from the real estate industry suggest property owners are experiencing enormous increases in premiums that they will undoubtedly seek to pass on to their already beleaguered tenants. These high insurance premiums are likely to weaken New York City's competitive position relative to other locations that have seen lower premium hikes or are just lower in cost, such as Northern New Jersey. This trend has dire implications for New York City's efforts to retain businesses during a period when many have already left the City.

From the perspective of the insurance industry itself, the capital appears to be in place to pay the anticipated $30-$58 billion in claims for the terrorist attacks of September 11, 2001.[21] The concern is that further attacks could endanger the solvency of the industry. Some experts have predicted that another incident or series of incidents of similar magnitude, whether they are natural or man-made, would produce insolvencies in the reinsurance market that would produce a ripple effect throughout the industry.[22] This potential crisis has resulted in insurance companies' reluctance to provide coverage where they have a substantial terrorism exposure. For these insurers, New York City, as a center of American culture and world finance, is seen as one of the most likely targets of future terrorist violence. Since New York State does not allow insurers to exclude terrorism, the insurers are restricting the coverage they will write, or drastically increasing rates to protect themselves from potential catastrophic losses. While the insurance industry's capital position ultimately will recover, especially with the higher premiums that are increasingly in place, the industry is being cautious about its exposure.

Recommendations

There are a number of strategies that can be implemented to address the increase in insurance premiums and tightening of supply in New York City, some of which are already underway:

- Federal Terrorism Insurance. On April 8, 2002 President Bush called for federal support of terrorism insurance, saying that skyrocketing premiums and policy cancellations are stifling economic development and costing jobs. Bills have passed in both the House and the Senate and a conference committee was established to reconcile the differences between the two bills. As of October 18th, when Congress recessed for the November

[21] D. Pilla and L. Gorski, "One Year Later," *Best's Review*, September 2002. The $30-$58 billion estimate is from Tillinghast-Towers Perrin, "Implications of the September 11 Terrorist Attack", September 21, 2001. The total losses were expected to "exceed $40 billion," according to Robert P. Hartwig (chief economist of the Insurance Information Institute), in "September 11, 2001: One Hundred Minutes of Terror that Changed the Global Insurance Industry Forever," *John Liner Review*, 15:4 (Winter 2002), p. 7. PriceWaterhouseCoopers in *Americas Insurance Digest*, fourth quarter 2001, p. 5, put the "industry consensus" of insurance losses at $50 billion. A recent estimate put the "net" loss number at $30 billion; *Insurance Advocate*, September 9, 2002, p. 5.

[22] Reinsurance Association of America, "The Reinsurance Market: The Impact of the September 11th Terrorism Catastrophe," April 24, 2002, p. 1.

elections, there were still several issues to be resolved. This legislation includes a backstop proposal that would provide temporary support in the form of loans or governmental reinsurance for insurance companies writing terrorism coverage. Supporters cite the importance of these proposals as increasing the confidence of the insurance industry in writing coverage in New York City and elsewhere, which would result in lower premiums and greater availability than would otherwise prevail.[23]

- Expansion of Risk Financing Options. As an alternative to purchasing insurance in the commercial market, large companies, groups of companies or industry associations should consider establishing alternative financing strategies. These financing options, often referred to as Alternative Risk Transfer arrangements, include reciprocals (a self-insurance program established for an organization or a related group of companies), purchasing groups (organizations or businesses within an industry that band together to purchase insurance), and captives (insurance companies set up by large corporations, or other entities to provide insurance to the corporation or entity). Another alternative is the establishment of a self-insurance program for individual businesses. This requires the allocation of capital to provide for any potential losses. Self-insurance can be used in addition to, or in place of, alternative risk options or commercial insurance. The State Insurance Department should encourage expansion of these alternatives.
- New Insurance Companies. States that believe that insurance premiums are too high or insufficiently available can encourage the creation of new insurance companies. This has happened in many states, including Vermont, Minnesota and Maine, and should be considered in New York State in order to create more capacity in the commercial insurance market.
- Risk Reduction. Companies and local governments, including New York City, are investing in physical improvements and in increased coverage by security personnel to improve security and to reduce risk. This effort should continue in the City so that local businesses will become more attractive to insurers, which presumably will result in lower premiums and greater availability.

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The Real Estate Board of New York and the representative owners, managers and brokers who met with the Comptroller's staff.

[23] Bill Sammon, "Bush Says Senate Should Federalize Terror Insurance," *The Washington Times* April 9, 2002.

Appendices

Appendix A - Survey Instrument

Appendix B – Summary Statistical Tables

Appendix C - Methodology

APPENDIX A: SURVEY INSTRUMENT

APPENDIX B: SUMMARY STATISTICAL TABLES

Average Premium Increases, by Line (%)

Accounts of All Sizes

	Pre 9/11	Post 9/11	Net Difference
Business Interruption	7.0%	51.7%	44.7 %
Construction Liability	17.3%	101.6%	84.3%
Commercial Auto	11.0%	34.3%	23.3%
Commercial Property	10.3%	74.7%	64.4%
Directors & Officers	7.7%	42.3%	34.6%
General Liability	10.9%	50.5%	39.6%
Professional Liability/ Malpractice/E&O	8.7%	41.5%	32.8%
Umbrella, Excess	11.7%	74.6%	62.9%
Worker's Compensation	7.0%	14.0%	7.0%
Average of 5 lines most affected by 9-11	9.4%	53.1%	43.7%
Average of 4 lines most affected by 9-11	9.9%	62.9%	53.0%

Availability of Insurance: Respondents Rating Insurance as "Readily Available" or "Somewhat Available", by Line (%)
Accounts of All Sizes

	Pre 9/11	Post 9/11	Net Difference
Business Interruption	93.9%	43.5%	-50.4%
Construction Liability	59.0%	4.5%	-54.5%
Commercial Auto	86.3%	33.3%	-53.0%
Commercial Property	91.7%	29.9%	-61.8%
Directors & Officers	88.7%	41.7%	-47.0%
General Liability	92.4%	30.8%	-61.6%
Professional Liability/ Malpractice/E&O	84.8%	45.6%	-39.2%
Umbrella, Excess	90.2%	32.3%	-57.9%
Worker's Compensation	85.5%	25.0%	-60.5%
Average of 5 Lines Most Affected by 9-11	90.8%	32.0%	-58.8%
Average of 4 Lines Most Affected by 9-11	92.0%	33.6%	-58.4%

Average Premium Increases, by Account Size

	Small Accounts			Medium Accounts			Large Accounts		
	Pre 9/11	Post 9/11	Net Difference	Pre 9/11	Post 9/11	Net Difference	Pre 9/11	Post 9/11	Net Difference
Business Interruption	6.3%	25.9%	19.6%	6.6%	41.7%	35.1%	8.0%	87.5%	79.5%
Construction Liability	18.1%	90.6%	72.5%	16.5%	109.6%	93.1%	17.3%	104.5%	87.2%
Commercial Auto	11.1%	27.5%	16.4%	10.6%	30.0%	19.4%	11.1%	45.6%	34.5%
Commercial Property	10.1%	43.0%	32.9%	9.8%	72.3%	62.5%	10.8%	108.8%	98.0%
Directors & Officers	6.8%	32.2%	25.4%	6.7%	37.7%	31.0%	9.5%	57.2%	47.7%
General Liability	11.5%	39.2%	27.7%	10.9%	46.9%	36.0%	10.3%	65.5%	55.2%
Professional Liability/ Malpractice/ E&O	6.5%	23.0%	16.5%	6.9%	29.5%	22.6%	12.8%	72.2%	59.4%
Umbrella, Excess	10.4%	52.9%	42.5%	11.3%	66.9%	55.6%	13.2%	104.0%	90.8%
Worker's Compensation	6.0%	16.9%	10.9%	5.2%	11.0%	5.8%	9.6%	14.1%	4.5%
Overall Average	**9.7%**	**39.0%**	**29.3%**	**9.4%**	**49.5%**	**40.1%**	**11.4%**	**73.3%**	**61.9%**
Average of 5 lines most affected by 9-11	**8.9%**	**35.6%**	**26.7%**	**8.8%**	**47.8%**	**39.0%**	**10.4%**	**76.0%**	**65.6%**
Average of 4 lines most affected by 9-11	**9.6%**	**40.3%**	**30.7%**	**9.7%**	**57.0%**	**47.3%**	**10.6%**	**91.4%**	**80.8%**

Availability of Insurance: Percentage of Respondents Rating Insurance as Readily or Somewhat Available, by Account Size (%)

	Small Accounts			Medium Accounts			Large Accounts		
	Pre 9/11	Post 9/11	Net Difference	Pre 9/11	Post 9/11	Net Difference	Pre 9/11	Post 9/11	Net Difference
Business Interruption	95.2%	52.4%	-42.8%	92.3%	38.5%	-53.8%	92.3%	15.4%	-76.9%
Construction Liability	57.3%	5.3%	-52.0%	60.0%	2.2%	-57.8%	64.3%	7.1%	-57.2%
Commercial Auto	87.0%	32.9%	-54.1%	89.4%	36.2%	-53.2%	73.3%	26.7%	-46.6%
Commercial Property	90.1%	32.9%	-57.2%	93.9%	29.2%	-64.7%	92.9%	14.3%	-78.6%
Directors & Officers	88.7%	50.9%	-37.8%	90.9%	40.6%	-50.3%	81.8%	0.0%	-81.8%
General Liability	93.8%	33.3%	-60.5%	90.2%	25.5%	-64.7%	92.9%	35.7%	-57.2%
Professional Liability/ Malpractice/ E&O	83.3%	52.4%	-30.9%	86.2%	44.8%	-41.4%	87.5%	12.5%	-75.0
Umbrella, Excess	88.7%	38.0%	-50.7%	91.7%	22.9%	-68.8%	92.3%	35.7%	-56.6%
Worker's Compensation	83.6%	26.0%	-57.6%	90.0%	22.5%	-67.5%	81.8%	27.3%	-54.5%
Overall Average	**85.2%**	**34.3%**	**-50.9%**	**87.1%**	**28.0%**	**-59.1%**	**84.1%**	**20.2%**	**-63.9%**
Average of 5 lines most affected by 9-11	**90.2%**	**35.9%**	**54.3%**	**91.6%**	**27.4%**	**64.2%**	**90.8%**	**25.8%**	**65.0%**
Average of 4 lines most affected by 9-11	**91.9%**	**38.4%**	**53.5%**	**92.0%**	**28.5%**	**63.5%**	**92.6%**	**25.5%**	**67.1%**

APPENDIX C: METHODOLOGY

Methodology

Sampling

The survey instrument was designed with input from representatives of the agent and broker membership organizations. Individual agents and brokers also tested a draft and their comments, as well as those of the membership organizations, were incorporated into the final survey document.

The five membership organizations provided the Comptroller's office with access to more than 1,700 agents and brokers in the New York Metropolitan area. These organizations forwarded the survey questionnaire to their membership by e-mail and the Comptroller's office also sent a paper copy of the survey by regular mail. The mailing was completed on August 1, 2002 and the survey requested a response by August 16, 2002. Because many agents and brokers were on vacation during this period, the deadline was extended and responses were accepted through September 6, 2002.

The Comptroller's office received a total of 152 completed questionnaires. However, this number likely does not reflect the full number of responses to the survey, since respondents were asked to coordinate with their colleagues and submit one completed questionnaire on behalf of the entire firm in which they work, not individually. Since in many cases multiple agents and brokers working for the same company received the survey, and we have confirmed that there was no more than one response for each brokerage or agency that participated, it is reasonable to assume that the questionnaire response rate understates the number of individual agents and brokers who contributed information.

Where information on returned survey questionnaires was incomplete, inconsistent or unreadable, follow-up telephone calls were made. Ninety-three responses could be used in the study and the remaining 59 questionnaires were not usable. Of the unusable responses, some stated that they did not do business in New York City. Other agents and brokers provided incomplete information and either did not include contact information or did not give the Comptroller's Office permission to call for clarification. The 93 completed questionnaires that were used reported results for a total of approximately 63,000 new and renewal accounts for businesses in New York City. The responses were submitted by 89 agents and brokers writing roughly 56,000 small accounts, 61 agents and brokers writing approximately 6,900 medium-sized accounts, and 18 agents and brokers writing 830 large accounts. Account size was defined by premium, with small accounts having premiums under $50,000, medium-sized accounts having premiums between $50,000 to $1 million, and large accounts having premiums over $1 million.

Limitations of the Sample

The usable responses represent 5.5% of the original mailing. However, it was not possible to estimate the portion of the entire universe of agents and brokers serving New York City businesses these responses represent, nor could the participating membership organizations estimate the percentage of the agency and brokerage market in New York City included in their membership. In addition, as there is no reliable and readily available information on the number of commercial property and casualty accounts written in New York City each year, it was not possible to calculate the percentage of that number represented by the 63,000 new and renewal accounts placed by respondents to the survey.

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