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SEPTEMBER 11, TEN MONTHS LATER

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Article abstract

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In the insurance field, the terrorist acts of September 11 actually caused the most catastrophic losses ever experienced by property and casualty insurers. Add in the impact of strong rate increases and it is easy to see why insurers and reinsurers have been forced to go back to basic rules in underwriting for large risks.

The fateful date also has many lessons to teach us about new approaches to risk management; building codes; and the need for governments and industry to cooperate in finding financial solutions to cover mega-terrorist losses.

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SEPTEMBER 11, TEN MONTHS LATER

by Rémi Moreau

ABSTRACT

In the months just following September 11, 2001, it was too soon to make an accurate evaluation of insurance claims, whether for human or financial losses. Ten months later, the author tries to outline the overall dimensions of the tragedy. Since last September, our lives have been irreversibly changed. In our personal life, we have had to confront a spectrum of emotions, from horror to admiration for heroic efforts. In the business milieu, many firms have been forced to return to basics in their techniques and procedures.

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RÉSUMÉ

Dans les quelques mois qui ont suivi le drame du 11 septembre 2001, il était encore trop tôt pour en mesurer précisément les conséquences en termes de réclamation d'assurance et de pertes humaines et financières. Dix mois après la catastrophe, l'auteur tente de faire le point sur cette tragédie. Depuis septembre dernier, nos habitudes de vie ont changé inexorablement. Nous avons été confrontés au spectre des émotions, partant des gestes d'horreur jusqu'aux actes de courage. Sur le plan commercial, plusieurs entreprises ont dû revenir à des règles de base, tant dans leurs opérations que dans leurs procédures.

Dans le champ de l'assurance, la catastrophe du 11 septembre 2001, qualifiée comme le plus grand sinistre dans l'histoire de l'industrie de l'assurance, fut accompagnée d'une forte hausse des tarifs et d'une profonde remise en question des principes de souscription des grands risques.

Nous pouvons aussi tirer des enseignements de cette journée fatidique, en termes de nouvelles approches en matière de gestion des risques, en matière de réglementation ayant trait aux grands édifices et enfin sur le plan d'une coopération plus forte entre les gouvernements et l'industrie concernant le financement des méga-sinistres découlant du terrorisme.

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INTRODUCTION

September 11 has become a red letter day, not only for the insurance industry but for all sectors of the economy. The date is cited as a temporal watershed in every article, report or analysis one reads. It has become emblematic of the new world (dis)order of terrorism and the geopolitical instability it has ushered in. The media and other sources have submerged us with the facts surrounding the tragedy. We shall not repeat them in this article, but just footnote two articles on the subject written for this Journal[1] by the author.

Ten months later, we are publishing this article to underscore some issues of key interest (written at the end of April 2002):

- The Insured Damages
- The Property & Casualty Market in 2002
- The 2002 Reinsurance Market
- The 2001-2002 Aviation Insurance Market
- The Insurability of Terrorist Risks
- The Painful Lessons from September 11
- The Importance of Risk Management

THE INSURED DAMAGES

As concerns loss of life, there were, fortunately, fewer fatalities than originally anticipated. With some 50,000 people routinely working or circulating in the Twin Towers, the death toll could have been staggering. According to the most recent figures, 3,125 people died in the WTC and Pentagon disasters, including the New York firefighters and police officers called to the scene. Some 2,250 people also suffered injuries in the two disasters. And the four plane crashes took the lives of 266 passengers and crew members.

It is still too soon to make a precise evaluation of the size of the insurance bill for the financial and property losses generated by the terrorist attacks against the U.S. in that day of infamy. The bill could go up to the $US60 billion mark or even higher. The gross economic loss estimated for New York alone is about $US85 million. The attack had a significant impact on the global economy because of the World Trade Centre's strategic location in downtown New

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York. Directly affected as well were airline traffic, travel services, hotel industries, and, of course, the insurance industry—to mention only these.

These extremely costly claims coincided with turbulent trends in capital markets: a highly volatile bond market and substantial slides in stock prices. In the wake of September 11, financial markets dropped 5% in one week. But as disruptions of financial markets go, the impact of the catastrophes marked no dramatic departure from the history of the last century. In 2002, the world was hit by the largest bankruptcy ever (collapse of Enron) and the largest sovereign default ever (Argentina), with barely a ripple through financial markets. The immediate cost was actually less than that of the Kobe earthquake in 1995 which killed 6,300 people and rung up economic costs of around $US120 billion (Jorion, 2002[2]).

The cost of the insured losses incurred by the September 11 events is nonetheless exceptional both in nature and in scale. Estimates of the insured losses (all types of insurance) stemming from those events are given below:

Lines of business	**Range in $US billions**
Property insurance	$10.0 - 12.0
Business interruption	3.5 - 7.0
Workers' compensation	3.0 - 5.0
Aviation insurance	3.0 - 6.0
Liability insurance	5.0 - 20.0
Life and health insurance	4.5 - 6.0
Other non-life insurance	1.0 - 2.0
Total	**$ 30.0 - 58.0**

With losses estimated at around $US60 billion (two-thirds of which will be borne by reinsurers), the terrorist acts of September 11 now rank as the most expensive disaster the property & casualty insurance industry has ever faced, far exceeding the previous record of $US19.6 billion set by Hurricane Andrew in 1992.

Still under dispute is the number of insured occurrences involved in the collapse of the Twin Towers. One of the policy holders—also the holder of the long-lease on the WTC— has been claiming that coverage should take into account at least two occur-

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rences, one for each tower. But insurers are insisting that there was in fact just one event and that the coverage limit must apply to this single event. The "per occurrence" coverage on the WTC was $US 3.5 billion. As things now stand, there have been settlements with insurers whose policies contain a clear definition of the term "occurrence," but the dispute continues with other insurers whose definition of the term is less precise.

Included in the tens of billions of dollars of losses arising from the terrorist attacks on the WTC is $US100 million worth of fine art, according to the estimate of one insurer. Certainly, for many tenants, filing claims related to the death of some employees and the relocation of others will take priority over filing for lost artwork.

Many firms have already been paid substantial claims for business interruption, but many others have policies that will not cover the full cost for the disruption of businesses, whether for those based directly in the WTC and its vicinity or for affiliates located elsewhere.

Cooperation between government authorities and insurers has been crucial. Insurance adjusters were given early access to the site after the attacks and were kept informed about changes in the perimeter restricting public access to the area.

The bioterror, not related to the September 11 attacks, that followed in the wake of the catastrophe should also be kept in mind. The handful of anthrax-tainted letters that contaminated a congressional office building, several post offices, and two media offices had a huge impact on the insurance industry. Coverage of these incidents depended on whether the anthrax contamination was considered vandalism, which is covered, or pollution, which is not.

THE PROPERTY & CASUALTY INSURANCE MARKET IN 2002

Paul Kovacs—executive V.P. and senior economist with the Insurance Bureau of Canada (IBC)—has described 2001 as the worst year ever for financial results in the P&C insurance sector:

> Canada's P&C insurance industry has hit a collective all-time low, with year-end numbers showing a return on equity of just 3% and a combined ratio topping 110%. In the 25 years for which the IBC has complete data, the

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return on equity has never been lower. And prior to that companies were used to achieving underwriting profits, so it's unlikely it was ever lower.

These unfavourable Canadian results were not limited to any one line of insurance, but were evident in all four of that industry's major lines: personal property insurance, commercial property insurance, automobile insurance, and liability insurance. When these negative results were mixed with a skittish climate of economic downturn, the scene was set for major improvements in underwriting performance and profitability. Some IBC observers saw 2001 as characterized by plummeting stock values, falling interest rates, and record low profits. These simultaneous trends coalesced with skyrocketing costs for claims. Unless major adjustments are made, the solvency of insurance companies is bound to be affected.

In the U.S.A., the 25 largest property & casualty insurers (based on net premiums written) posted a 118.2% combined ratio. The industry's net after-tax losses climbed to $US7.92 million in 2001, as compared with a net income of $US20.56 billion in 2000. The Insurance Services Offices Inc. (ISO) has reported that the 2001 combined ratio (the percentage of each premium dollar spent on claims and expenses) deteriorated by almost 10 points in comparison to last year's 110.1% figure. The losses reflected the huge claims stemming from the September 11 terrorist attacks. Other factors contributed to this deterioration, factors such as sharply lower returns on investments, the failure of Enron, and increased toxic mold claims in Texas.

Insurance Bureau of Canada (IBC) experts think that the industry's 2001 financial results confirm the return of the hard market. The stage may now be set for new rate hikes in 2002. The industry will surely continue to raise its prices over at least the next two years and perhaps even into 2004 or 2005. But, well before the dramatic collapse of the Twin Towers, reinsurers were having trouble covering their capital costs and rate hikes were already on the horizon. The casualty insurance industry's reserves to cover asbestos and environmental liabilities lagged as much as 50% behind premium increases.

Starting with post-WTC renewals in 2002, commercial insurance rates were expected to shoot up as much as 25% to 35%, while remaining low in personal lines. Property rate increases of 100% to 200% have not been unusual. Pricing tightened significantly for special risks: anywhere from 300% to 500% for aviation liability and hull insurance.

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The trend in rate increases combined with restrictions in contractual terms and conditions, particularly as concerns insurance against terrorist acts. Insurers and reinsurers adopted a back-to-basics approach to their underwriting rules. For example, since September 11, travel accident coverage has become a great deal more complex and expensive, owing to the limited capacity of reinsurers and to the war-risk exclusions underwriters have placed on travel to many countries. Before September 11, travel accident policies covering acts of war for all countries were readily available. Now, such policies cannot be routinely purchased.

One of the major causes of rate increases was the huge drop in capital in the United States insurance industry. Some $US50 billion in September 11-related losses have combined with about $US50 billion in investment losses to slice insurers' capital by $US100 billion or more. About $US20 billion in new capital has flowed into the industry since September 11, and a further $US10 billion is expected in 2002.

THE 2002 REINSURANCE MARKET

As of December 2001, $US estimates of pre-tax WTC losses for first-world reinsurers were in the stratospheric range: Munich Reinsurance–Germany ($1.9 billion); Swiss Reinsurance –Switzerland ($1.5 billion); Berkshire Hathaway Reinsurance–U.S. ($2.2 billion); Employers Reinsurance–U.S. ($600 million); Hanover Reinsurance–Germany ($365 million); Gerling Global Reinsurance–Germany ($246 million); Lloyd's–U.K. ($2.8 billion); Allianz Reinsurance ($1.3 billion); SCOR Reinsurance–France ($200 million); Converium, formally Zurich Reinsurance–Switzerland ($900 million); Transatlantic Holdings–U.S. ($307 million); AXA Reinsurance–France ($550 million); PartnerRe Ltd.–Bermuda ($400 million); St. Paul Reinsurance–U.S. ($941 million); Everest Reinsurance Ltd.–Barbados ($93 million); XL Capital–Bermuda ($750 million); CNA Reinsurance–U.S. ($468 million); Hartford Reinsurance–U.S. ($676 million); Odyssey Reinsurance–U.S. ($80 million); ACE-Bermuda ($636 million).

And here are the 2001 results obtained by some reinsurers : (1) Lloyd's of London has reported (in its first ever report of an annual result) a loss of $4.53 billion in 2001 (a loss largely owing to claims arising from the terrorist attacks. (2) Munich Re, the world's leading reinsurer, saw its net 2001 income reduced to $222 million, down

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more than 85% from 2000 results. This drop in earnings stemmed mainly from the $1.96 billion in claims owing to the September 11 terrorist attacks; moves to strengthen reserves; and poorer returns on investments. Premium growth in the Munich Re Group was even stronger in 2001 than in the previous year. Gross premium income rose 16.1% to $32.1 billion. (3) Swiss Re, the world's second largest reinsurer, posted a $966 million loss for 2001, its first since 1868. This huge loss can be attributed to a post-tax loss of $1.77 billion from September 11 and a $966 million reduction in capital gains. (4) Gerling Global Reinsurance Corp. of America had such poor 2001 results that it was forced to cut 70 jobs in the U.S so as to restructure its casualty operations. (5) Zurich Financial Services Group, hit by claims for $706 million in September 11 losses, reported a net 2001 loss of $387 million, in contrast with a net income of $2.3 million the previous year. (6) American International Group, fielding $533 million in WTC losses and $57.2 million in Enron-related surety losses, saw its 2001 net income take a 19.2% drop to $5.36 billion. (7) At Allianz there was a $1.52 billion drop in net income for 2001, largely due to net September 11-related claims of $1.34 billion. (8) Bermuda's ACE Ltd. reported a $146.4 million loss for 2001 as compared with a profit of $543 million for the previous year. (9) Chicago-based CNA posted a net loss of $1.6 billion in 2001, compared with a net income of $1.2 billion in 2000. (10) Finally, AXA Corporation Solutions, AXA's reinsurance and large commercial insurance unit, estimated its net loss from September 11 claims at 350 million euros ($312 million), equivalent to about three years of reinsurance profits.

The September 11 attacks wiped out about 25% of the world's overall reinsurance capacity. A massive infusion of capital, including some $25 billion in new Bermuda capacity, was needed.

In the post-September 11 reinsurance marketplace, the better the data, the better the terms and conditions. Reinsurers have been digging deeper for renewal information. They have been requiring more detailed information on exposures from ceding companies and then underwriting coverage accordingly. Consequently, reinsurance brokers say they have been spending much more time with clients in order to accumulate and analyze data for presentation to reinsurers when renewing portfolios of risks or treaties.

The September 11 terrorist attacks were a very rude awakening: They forced reinsurers to change their underwriting approaches and procedures and to develop models more like those already being used in the property damage sector, models capable of assessing exposure to significant aggregate risks in other lines of business as

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well. Reinsurers were also led to modify the terms and conditions of their contracts with cedants to limit losses should other terrorist attacks or major natural disasters occur.

THE 2001-2002 AVIATION INSURANCE MARKET

The aviation industry reported a business loss of $US10.9 billion in 2001, according to the preliminary estimations of OACI (Organisation de l'aviation civile internationale), in the aftermath of the September 11 attacks. In the area of insurance, many companies cancelled or modified their aviation insurance policies. Rate increases were needed to stabilize the aviation insurance market, despite the rate hikes and restrictions which had already been imposed during the previous 10 months. The aviation insurance market faced losses of $5.8 billion in 2001, making it the worst year ever for that market. The losses were so massive that the companies were separating out the impact of September 11 to give a true idea of 2001 business before the terrorist attacks. Prior to 2001, the aviation market's worst year had been 1994, with losses of just under $2.3 billion. Had it not been for the September 11 attacks and, to a lesser extent, the destruction of many Sri Lankan Airlines planes by Tamil Tigers, 2001 losses would have fallen below the expected annual average.

Insurers must show some determination if they want to maintain, in 2002, the annual world premium of from $US 3.5 to $US 4 billion which they earned in 2001 and which far exceeded the average annual premium of $US 1.2 billion. The 2001 premium was mainly generated by terrorism surcharges covering third-party, risk-of-war liabilities. For exemple, underwriters are still charging $US1.25 per passenger for the first $US50 million of third-party war risk liability coverage for any one occurrence and in the aggregate ; this is what most airlines have been paying since the September 11 attacks.

The insurance market for aviation risks has some challenges to face in 2002. The market has maintained the hardened rates for comprehensive aviation coverages which appeared in the final quarter of 2001 and this despite the new capacity coming into the market. Renewals posed difficulties for most of the insurers. Many insurers now operate their reinsurance programmes on a loss-occurring-during (LOD) basis rather than on a risk-attaching basis. So, an underwriter drawing up an airline hull and liability insurance program on

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November 1, 2002 will only have reinsurance protection for about two months—up to December 31, 2002—on that particular insurance program.

But higher prices would not solve all of the aviation insurer's problems. Insurance was needed to provide for the possibility that large lawsuits would be brought by the families of victims. It would take a fundamental review of pricing techniques to stabilize things. Major airlines in Europe and North America were considering the creation of an excess-of-loss pool to cover their third-party, terrorism-risk liabilities, claiming that specialized aviation/commercial rates were too high. But the idea of setting up such global aviation insurance pools met with concerns or objections from a number of countries.

THE INSURABILITY OF TERRORIST RISKS

Last January, the National Association of Insurance Commissioners (NAIC) voted unanimously against excluding terrorism from personal policy lines, judging that such exclusions might violate State law and that they were not needed to maintain a competitive market.

In the wake of the terrorist attacks, most P&C insurers might have been expected to invoke act-of-war exclusions. But it is a mistake to think that such war exclusionary clauses automatically apply to situations involving terrorist attacks. There are at least 3 basic reasons why the war exclusionary clause could not be invoked in the case of September 11: in official contractual terms, the act-of-war exclusion applies only to terrorist attacks carried out during a war officially declared by a State; indemnity is the very soul of insurance, meaning that insurers have to indemnify to ensure their future ability to underwrite new business; and, in service to the public good, insurers are duty bound to pay claims in case of occurrences (unexpected events which, from the standpoint of policy holders or victims, were not intentionally caused).

According to the terms used by many insurers, what distinguishes an insurable terrorist attack from an act of hyper-terrorism, which is excluded in many countries, is the scale of the resulting damage. In France, the goal of that definition was to shift the coverage of such acts to the government. In the United States, the National Association of Insurance Commissioners, as well as regulators in 46

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jurisdictions, have given the green light to the terrorism exclusion language proposed by the Insurance Services Office Inc. Among other thresholds it sets, this language limits coverage for insured damages from terrorism to $25 million. The ISO proposal also provided for an exclusion if more than 50 people were killed or injured in a terrorist event.

Prior to September 11, it was assumed that maximum potential losses from terrorist acts would not exceed those comparable to the property losses resulting from fires or explosions. Working on this assumption, terrorism was not explicitly excluded from property policies. However, the magnitude of the 2001 losses incurred in the United States has revealed an entirely new dimension of the terrorist threat and has forced insurers to reconsider these assumptions and the whole notion of the insurability of terrorist risks. The Swiss Re report finds that risks associated with terrorism meet fewer and fewer of the important criteria of insurability, in particular the possibility of accurately assessing the probability and severity of terrorist attacks. As a result, terrorism is now insurable only on a very limited basis. In other words, the new definition has rendered terrorism uninsurable, unless the industry can determine its frequency and severity.

In the new environment, the solution is to have both governments and the insurance industry providing the funds to finance and to cover terrorist losses.

☐ Industry Examples

Six leading insurance and reinsurance companies have formed a new company in Luxembourg to provide property coverage for acts of terrorism in Europe. The new company, Special Risks, Insurance & Reinsurance Luxembourg S.A., has a total committed capital of 500 million euros ($US 438.5 million). Planning to begin underwriting in the second quarter of 2002, the insurer will cover property damage resulting from an act of terrorism. To prevent the aggregation of losses, the coverage is limited to 275 million euros within a given 600-meter area. The new group will not insure losses due to either business interruptions or liability.

ACE USA is now also offering up to $100 million in coverage for property losses stemming from acts of terrorism. The coverage is being offered to U.S. and Canadian utilities, telecommunications companies, manufacturers, entertainment industries, financial institutions, and real estate businesses. Coverage for terrorism-related business interruption is available up to unspecified limits.

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Governmental Examples

In the United States, the House did manage to pass a bill related to the insurance industry in 2001. Under its plan, the federal government would establish a loan program to help insurers cover losses from another terrorist event. But this loan program has been refused by the insurance industry. In the Senate, a bill to establish a quota-share reinsurance plan (far more effective in making insurance available) was stalled over tort reform disputes. Under this Senate bill, which never reached the floor, insurers would have had to pay out an industry aggregate of $10 billion before receiving any federal assistance, but they would not have had to repay the funds as in the House bill. It seemed, nevertheless, that creating a federal role in the market for terrorism insurance would remain a top priority for President Bush and Congress in 2002.

The French government has agreed to have its state-owned reinsurer *Caisse centrale de réassurance* (CCR) bear the cost of any terrorism insurance losses exceeding 1.5 billion euros per year. Reinsurers have decided to form a pool to pay for insurable terrorist losses up to that maximum amount. This pool is to be supported by property insurers and backed by the government. It will cover property and business-interruption losses up to an insured value of 6 million euros. The first 250 euros in aggregate annual losses is to be covered by insurers writing property insurance. Capacity to cover annual aggregate losses totaling 750 million euros over and above the first 250 million euros will be provided by a group of reinsurers. If aggregate annual losses exceed 1 billion euros, the pool's participants will cover a further 500 million euros through a government-backed financial agreement. Above the 1.5 million mark, the French government will provide unlimited stop-loss coverage through its CCR.

Spain and the United Kingdom, which set up government-backed terrorism pools years ago, have been giving some consideration to expanding the coverage of their existing pools. The U.K.'s Pool Re provides reinsurance for property and business interruption losses caused by fire and explosion. The coverage has now been broadened to include all such losses resulting from terrorism. And the new set of circumstances at large in the world have brought Pool Re's definition of terrorism into question. Under the law creating Pool Re, "terrorism" was defined as "acts of persons acting on behalf of, or in connection with, any organization which carries out activities directed towards the overthrowing or influencing, by force or by violence, of Her Majesty's government in the United Kingdom or any other government de jure or de facto." Revising that definition

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would require new legislation. Finally, the UK government outlined changes to its terrorism reinsurer Pool Re in response to perceived changes in risk.

In Germany, a pool with a capacity of several million euros has been under consideration. The pool would offer coverage similar to that given in the mutual terrorism scheme of the UK's Pool Re.

Yet a terrorism reinsurance pool for the whole of the European Union countries looked unlikely because of the lack of political pressure for such a move, according to European Commission officials and the trade association the Comité Européen des Assurances (CEA).

Terrorism reinsurance pool also opened in Russia. Six leading Russian insurers have set up a reinsurance pool because of their difficulties in finding terrorism cover in Russia and the London market.

And what about Canada? The idea of a reinsurance pool for terrorist acts has also been considered in Canada. The insurance industry was asking the federal government to act as an insurer of last resort, selling coverage to reinsurers on a case-by-case basis for needs above a minimum level. The discussion on a Canadian pool program between IBC and the Federal Finance Department finally failed because the insurance market conditions have changed since last year.

■ THE PAINFUL LESSONS OF SEPTEMBER 11

Ironically, the terrorists who slammed jets into the WTC may inadvertently have helped to ensure that future terrorist targets will have a better chance of standing up to such attacks. The lessons offered by the September 11 disasters raised questions about existing fire safety standards and fire code regulations for high-rise buildings: Do they correspond to real-world situations and issues? Some experts and investigators have expressed their frustration with the obstacles they have met in their attempts to understand exactly why the Twin Towers collapsed.

The obstacles include a lack of coordination among federal agencies involved in the investigation, delays in obtaining documents such as blueprints, and the loss of some potentially key pieces of evidence. A hearing committee, the House Science Committee,

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has been created to learn as much as possible about what happened so as to help ensure that such a catastrophic building failure and resulting loss of life will never again occur.

On March 2002, two studies on natural catastrophes were published respectively by Munich Reinsurance and Swiss Reinsurance. These reports are of great interest, even though natural disasters do not correspond perfectly with man-made ones. Swiss Re reports that, in 2001, worldwide, insured property and business interruption losses from man-made disasters totaled $24.4 billion—by far the worst year on record for man-made disasters and directly linked to 9/11—as compared to an average of $5.9 billion per year from 1987 to 2001.

In its report, Munich Re states that risk managers will have to think the unthinkable in the future. September 11 has demonstrated that they will have to envision maximum loss potentials which, albeit improbable, may nevertheless prove to be possible. For example, the study investigates the risk of strikes by meteorites, of which some 100 were documented last century. The effects of climate change for decades to come are also considered, mainly in the form of more frequent and destructive natural catastrophes.

Over the long term, despite the new dimensions of the terrorist threat, it is mostly natural catastrophes, i.e. storms, floods, and earthquakes, which concern the insurance industry. The trend towards higher losses can be expected to continue in view of the existing risk factors involved: higher population densities and higher concentrations of insured values, especially in endangered areas or high-rise office buildings or towers. It therefore remains crucial that insurers and reinsurers should identify and diversify the risks associated with natural disasters.

The need for counseling services generated by September 11 increased awareness of employee assistance plans. This increased awareness and the ongoing need for counseling on the part of employees traumatized by the September 11 attacks have been driving the demand for additional Employee Assistance Programs (EAPs).

■ THE IMPORTANCE OF RISK MANAGEMENT

The events of 9/11 have once again confirmed the importance of risk management. For a decade now, risk managers have been

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playing a bigger role in studying financial risks and finding alternative ways of financing such risks. They have also been more active in promoting new global approaches, such as enterprise-wide risk management (ERM).

In 2002's hard market, the most commonly cited concern among risk managers seems to be the increasing cost of coverage and the necessity of maintaining strong long-term relations with insurers. The risk management industry is currently confronted with a number of serious challenges such as: managing financial, economic, and political risks; securing fronting insurers for captives; identifying risk exposures; setting priorities; and using loss control techniques to improve risk portfolios or the renewal process.

Moreover, international business exposes risk managers to new forms of risk such as those associated with global coverages. All these may now change in the face of increasing globalization; heightened awareness of terrorism; and destabilization of the international political environment.

While facing these new challenges, risk managers must continue to assume their traditional roles in negotiating insurable risks from conventional exposures, for which there has also been a growing demand since 9/11. Pricing for major property and liability risks is likely to be analyzed more closely and, where feasible, modelled. The fall-out from the 9/11 attacks sent rates skyward and injected chaos into many buyers' renewal negotiations.

The September 11 terrorist attacks forced everyone to be more creative on the risk management side. As risk managers assume more risks as a means of lowering insurance costs, they are experiencing more uninsured losses. They have to use large deductibles to control their cost of risk. But, according to a recent survey, since September 11, risk managers in large corporations are becoming more interested in purchasing terrorism coverage. Safety and engineering programs have also become a necessity. At RIMS's membership meeting in New Orleans this April (RIMS's 40th Annual Conference and Exhibition), Mr. Christopher E. Mandel, the new president, urged risk managers to adopt "world-class risk management." Among the new principles to be adopted post-9/11, we may mention two: ceaseless innovation and widespread use of best practices.

Amid all this turmoil, risk managers have been forced to rethink security concerns and make major changes to keep their companies safe. Since the terrorist attacks, risk managers have been asking many more questions about how to prepare for such events. Many

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enterprises now look more closely at disaster planning. Risk managers are now more concerned about having such plans carefully drawn up and implemented. And risk managers with some experience in handling large claims have gained in status. Knowing what is required to adjust a large claim efficiently, they can do so without feeling they have to waste time reinventing the wheel.

The hard market could give a real boost to new alternative risk financing options such as finite risk products (FRPs). Originally, FRPs were financial reinsurance deals that gave insurers a method of capping their losses when they were unable to obtain reinsurance during a hard market. These original transactions were structured on a post-funded basis and many regulators soon realized that they involved little transfer of risk. One of the most frequently used FRPs is the loss portfolio transfer. Its coverage is designed to provide retroactive coverage for losses arising from a policy holder's claims, losses that have already occurred but have not yet been settled.

The new enterprise-risk-management (ERM) option mentioned above is also worth recalling. This concept is based on a common framework for handling risk throughout the organization. One of the ERM's core concepts is to anticipate and plan for risks on a corporate-wide basis.

CONCLUSION

Although the insurance market was already hardening prior to the September 11, 2001, the events of that day were a catalyst for enormous changes. Since last September, our countries and our lives have been irreversibly changed. We have personally had to confront a spectrum of emotions, from horrified disbelief to admiration for the heroic efforts we witnessed. The whole business milieu has been forced to return to basics in its techniques and procedures.

The WTC losses have alerted insurers and reinsurers to the stark reality that all risks are possible and should be anticipated. Insurers have been raising rates, tightening restrictions, limiting areas of coverage, and demanding comprehensive underwriting information. Underwriters have grown increasingly concerned about exposures, especially where there are large concentrations of people. During the January 2002 renewal period, insurance brokers had to work overtime to place many of their clients' programs in a difficult market.

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Risk managers must revisit cause-and-effect relations in order to make intelligent decisions regarding their improvement plans. They must be more creative in designing their coverage programs. They should be very cautious in choosing which risks they retain and, finally, they should review their selection of insurers and create competition for their business.

In the first months after the attacks, the claims tally escalated rapidly. If 9/11 follows the pattern of previous disasters, about 60% of the total claims will have been handled by the first anniversary of the Twin Towers attack. After that, experts expect to see a long period of insurance litigation stretching far into the future.

We can also learn many lessons from the WTC disaster, for example: lessons promoting better building code regulations, enhanced building design methodologies, improved emergency procedures, and more effective protection against terrorist attacks.

That fateful September day has also clearly demonstrated that the companies or institutions that survived the catastrophe with the least damage are those that had planned ahead. For example: companies such as Merrill Lynch and Morgan Stanley activated their comprehensive disaster plans and were back to business almost immediately after the attacks.

Finally, the events of September 11 show that government and insurance companies must adopt a broader and more integrated approach to contingency planning and risk management. Many organizations have been urging governments all over the world to provide global terrorism insurance to cover amounts in excess of the insurance industry's primary limits, because this industry has neither the capacity nor the willingness to underwrite comprehensive terrorism coverage.

☐ Notes

1. See Rémi Moreau, "Le jour de l'infamie", *Assurances*, October 2001, 335-357; Rémi Moreau, "La plus grande catastrophe dans l'histoire de l'assurance", *Assurances*, January 2002, 511-532.

2. Available in French or in English: "Risk Management in the Aftermath of September 11" or "La gestion des risques après le 11 septembre 2001", Les Conférences Gérard-Parizeau, HEC-Montréal, April 2002 (http://www.hec.ca/fonds.gerard-parizeau).

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