FINANCIAL SUPPORT FOR THE PRIVATE SECTOR AFTER AN ANTHRAX BIOTERRORISM INCIDENT

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Through the Interagency Biological Restoration Demonstration (IBRD) project, a set of private sector stakeholders has been engaged in discussions about recovery from a potential bioterrorism incident involving a wide-area release of anthrax. A primary concern identified by the private sector is the availability of financial support for restoration and long-term recovery of businesses and their physical assets. This document briefly summarizes the two primary mechanisms for providing financial support following a catastrophic event — the Stafford Act and the Terrorism Risk Insurance Act (TRIA) — and describes how they would apply to the private sector in an anthrax terrorism incident.

WHAT IS THE STAFFORD ACT?

The Robert T. Stafford Disaster Relief and Emergency Assistance Act (the Stafford Act) is the primary legislation directing the Federal Government's response to disasters within the United States. It defines how disasters are declared, determines the types of assistance to be provided by the federal government and establishes cost sharing arrangements among federal, state, and local governments.[1] The Stafford Act gives Federal Emergency Management Agency (FEMA) responsibility for coordinating government-wide relief efforts and distributing much of the assistance.

An *emergency* is defined as "any occasion or instance for which, in the determination of the President, Federal assistance is needed to supplement State and local efforts."[2] An emergency declaration allows up to $5 million in federal assistance to be delivered to states and local communities. A *major disaster* is defined as any natural catastrophe (e.g., hurricane, tornado, tsunami, earthquake, volcanic eruption, snowstorm, drought, etc.), or any fire, flood, or explosion, regardless of cause, that the President determines "causes damage of sufficient severity and magnitude to warrant major disaster assistance."[3] A major disaster declaration allows for more extensive and specific provisions from the Federal Government.

[1] Moss, M, C Schellhamer, D Berman. "The Stafford Act and Priorities for Reform." *Journal of Homeland Security and Emergency Management*. 2009;6(1).

[2] 42 U.S.C.5122

[3] 42 U.S.C.5122

WHAT ASSISTANCE IS AVAILABLE TO THE PRIVATE SECTOR UNDER THE STAFFORD ACT?

Federal assistance under the Stafford Act is directed primarily to state and local governments. The Act does not grant the Federal Government the authority to provide assistance to private entities with two exceptions.

First, private nonprofit (PNP) facilities that provide critical services to the general public (e.g., water, power, sewer, wastewater treatment, communications, emergency medical care, etc.) may be eligible to receive grants directly from FEMA. Other "non-critical" PNPs (e.g., educational facilities) that provide essential emergency services can apply to FEMA for emergency work assistance. However, for permanent work costs they must first apply for a disaster loan from the Small Business Administration (SBA); if declined, they may apply for FEMA assistance.[4]

Second, the SBA Economic Injury Disaster Loan Program provides loans to small businesses in areas where a major disaster is declared by the Federal Government. Economic Injury Disaster Loans cover both economic injury and physical damage assistance such as replacing real estate and inventory as well as covering payroll, rent, and utility bills.[5] The assistance is available only to entities that cannot provide for their own recovery from nongovernment sources. Loan amount is based on actual economic injury and financial needs and are capped at $1.5 million in assistance to each business.

WHAT ARE LIMITATIONS OF THE STAFFORD ACT FOR THE PRIVATE SECTOR?

There are several limitations of the Stafford Act that relate to both the private sector and a wide-area bioterrorism related incident. Several of these are identified in the report, *The Stafford Act: Priorities for Reform*. These include:

- The definition of a major disaster does *not* cover chemical, biological, radiological, or nuclear attacks or accidents.
- While two incident levels are defined by the Stafford Act — emergencies and major disasters — no special response is provided following *catastrophes* of a much larger scale.
- Because the Stafford Act only provides coverage to public or nonprofit utility providers, private for-profit utilities cannot access loans to help restore their utilities. Because they are not recognized as "emergency responders," they are not able to receive security escorts and priority access to food, fuel, water, and shelter. Nor do private, for-profit utilities receive reimbursement for the replacement of damaged equipment and facilities and for emergency work performed following a catastrophe, as is provided to public and nonprofit utilities.
- Delays in receiving Economic Injury Disaster Loans are common and as a result loans may not be available to help small businesses defer immediate costs.

WHAT IS THE TRIA?

While the Stafford Act provides disaster financing for the public sector and does not explicitly grant authority to provide assistance to for-profit entities, the private sector is able to receive terrorism disaster assistance through insurance. Prior to the September 11, 2001 terrorist attacks in the United States, insurers did not typically exclude or charge separately for coverage of terrorist incidents. However, as insurers realized costs

[4] Private Nonprofit (PNP) Facility Eligibility, Disaster Assistance Policy 9521.3. FEMA. Available at: http://www.fema.gov/government/grant/pa/9521_3.shtm. Accessed 9/18/09.

[5] Moss, Mitchell and Charles Shelhamer. 2007. "The Stafford Act: Priorities for Reform." Available at: http://www.nyu.edu/ccpr/pubs/Report_StaffordActReform_MitchellMoss_10.03.07.pdf.

from these attacks amounted to an estimated $32.5 billion,[6] primary insurers either stopped offering coverage for acts of terrorism or provided it at a cost that was not accessible to many businesses.[7] This raised concerns about the insurance industry's ability to provide coverage against the risk of terrorism and led Congress to pass the TRIA in 2002. [8]

TRIA requires insurers to make terrorism coverage (property/casualty insurance) available to commercial property owners and guarantees that the Federal Government will reimburse insurers for a portion of the losses above a particular threshold. Insurance premiums are set by insurers (subject to state regulation), and purchase of the insurance by policyholders is voluntary. TRIA was reauthorized in 2007 with several new provisions and extended through December 31, 2014.

WHAT SPECIFIC ASSISTANCE IS AVAILABLE TO THE PRIVATE SECTOR UNDER TRIA?

Key features of TRIA as reauthorized include:

- TRIA was expanded to cover both acts of foreign and domestic terrorism.
- Federal assistance is triggered following an incident in which aggregate industry losses exceed $100 million.
- Federal assistance is capped at an annual aggregate amount of $100 billion, and TRIA specifies that insurers are not responsible for aggregate industry losses exceeding that amount.
- When the program is triggered, the Federal Government will pay 85% of insured terrorism losses beyond the individual insurer trigger and deductibles.
- Individual insurers pay 20% of the previous year's direct-earned insurance premiums.
- Industry as a whole (industry-wide retention) must cover $27.5 billion in losses before federal assistance is available.
- The Federal Government can recover some of its costs through surcharges (not to exceed 3% of premium) on commercial insurance policies sold after the terrorist attack occurred.

WHAT IS THE COST AND AVAILABILITY OF TERRORISM INSURANCE?

Largely due to the TRIA program, commercial property terrorism insurance is widely available on a nationwide basis at rates viewed by policyholders as reasonable, according to a U.S. Government Accountability Office (GAO) study. Some commercial entities seeking large policies in urban areas viewed as at higher risk of terrorist attack (e.g., Manhattan, Chicago, San Francisco, etc.) may face initial challenges obtaining full coverage for terrorism at reasonable rates. However, they have generally been able to obtain the desired amount of terrorism coverage by increasing the number of carriers.[9]

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[6] Department of the Treasury, Board of Governors of the Federal Reserve System, U.S. Securities and Exchange Commission, and Commodity Futures Trading Commission, Terrorism Risk Insurance: Report of the President's Working Group on Financial Markets (Washington, D.C., September 2006), 8.

[7] Baird, Webel. April 11, 2005. "Terrorism Risk Insurance: An Overview." CRS Report for Congress. Available at: www.fas.org/sgp/crs/terror/RS21979.pdf.

[8] Dixon, L, J Arlington, S Carroll, D Lakdawalla, R Reville, and D Adamson. 2004. Issues and Options for Government Intervention in the Market for Terrorism Insurance.

[9] GAO. Terrorism Insurance: Status of Efforts by Policyholders to Obtain Coverage. GAO-08-1057. Washington, DC: September 2008. Available at: http://www.gao.gov/new.items/d081057.pdf.

Policyholders typically buy property coverage, including terrorism coverage, through one all-risk policy, which insures losses from multiple perils. Premiums for these policies have been relatively stable at around 4% of U.S. commercial property premiums since 2003. Policyholders generally do not purchase terrorism insurance in amounts that would cover the total replacement value of the insured property. Coverage amounts are typically based on either the maximum amount of foreseeable losses that could occur in a terrorism incident or the amount required by a lender providing the mortgage for the property.[10]

An estimated 60% of commercial policyholders nationwide purchase terrorism risk insurance, according to data from two large insurance brokers.[11] Take-up rates by commercial clients appear to be higher in the northeast (which includes New York City), with about 70% having purchased terrorism insurance in 2007. By sector, real estate companies account for the largest percentage (about 80% in 2007) of clients with terrorism insurance, while sectors such as manufacturing and construction have much lower take-up rates (45% and 34%, respectively).[12]

The primary reason why about 40% of commercial policyholders do not purchase terrorism insurance is that they do not perceive themselves at risk (particularly those in nonurban areas). Other reasons may include the absence of lender requirements for coverage and the cost of coverage.[13]

WHAT ARE LIMITATIONS OF TRIA AND CURRENT TERRORISM INSURANCE FOR THE PRIVATE SECTOR?

While TRIA covers attacks involving conventional weapons, insurers' standard exceptions may exclude coverage for terrorist attacks with nuclear, biological, chemical, or radiological (NBCR) weapon. An attack with NBCR materials could result in substantially higher casualties and property damage than an attack with conventional weapons, raising concerns that a lack of coverage could prolong economic recovery from such attacks.[14]

In practice, most property/casualty insurance policies do exclude coverage for terrorist attacks involving NBCR materials because of the uncertainties surrounding such attacks and the potential for generating catastrophic losses. The insurance industry faces the challenge of reliably estimating the severity and frequency of NBCR attacks, making it difficult to set premium rates. Those that do offer NBCR coverage do so at a very high cost and with several restrictions. For example, only losses from the initial force may be covered; long-term effects such as illness or business interruption are excluded.[15]

Workers' compensation, group life, and health insurance companies are generally required by state regulators to cover losses from such attacks. However, when workers' compensation is offered by private

[10] GAO. Terrorism Insurance: Status of Efforts by Policyholders to Obtain Coverage. GAO-08-1057. Washington, DC: September 2008. Available at: http://www.gao.gov/new.items/d081057.pdf.

[11] Ibid.

[12] Ibid.

[13] Ibid.

[14] GAO. Terrorism Insurance: Status of Coverage Availability for Attacks Involving Nuclear, Biological, Chemical, or Radiological Weapons. GAO-09-39. Washington, DC: December 2008. Available at: http://www.gao.gov/new.items/d0939.pdf.

[15] Ibid.

insurers rather than through a state program, there is possibility that insurers would only offer coverage to certain employers and not to others (e.g., those in densely populated high-risk areas).[16]

Some major corporations have established "captive insurers" to self-insure the risk of an NBCR attack and obtain federal reinsurance under TRIA. However, the GAO reports that these captive insurers are not widely used for this purpose, perhaps due to the cost.[17]

[16] Ibid.

[17] GAO. Terrorism Insurance: Status of Coverage Availability for Attacks Involving Nuclear, Biological, Chemical, or Radiological Weapons. GAO-09-39. Washington, DC: December 2008. Available at: http://www.gao.gov/new.items/d0939.pdf.

APPENDIX

HISTORY OF THE STAFFORD ACT

The Stafford Act is a 1988 amended version of the Disaster Relief Act of 1974. Under the 1988 amendment, the Stafford Act gave FEMA greater authority for disaster recovery and mitigation, and it created the single authority for providing disaster assistance with funding appropriated by the U.S. Congress each year. The 1988 amendment also enacted the current definitions of emergencies and major disasters. Prior to that, the definitions for major disasters and emergencies declarations were contained in the Disaster Relief Act of 1974, which was not limited to "natural catastrophes" at that time—it applied to "any hurricane, tornado, storm, flood, high water, wind-driven water, tidal wave, tsunami, earthquake, volcanic eruption, landslide, mudslide, snowstorm, drought, fire, explosion, or other catastrophe."[18] In response to Presidential use of the Disaster Relief Act to support human-caused activities (e.g., FEMA providing temporary housing to Cuban refugees under President Carter) an amendment to the definition was made in 1988 limiting the Stafford Act to apply to "natural catastrophes." The 100thCongress passed the Stafford Act to limit major disaster assistance to "natural" incidents and deny major disaster assistance to incidents that were caused by human activity.

At the conclusion of the 109th Congress, the Senate inserted Stafford Act amendments into the fiscal year 2007 U.S. Department of Homeland Security appropriations legislation. These amendments expand FEMA's authority to expedite emergency assistance to stricken areas, to impose new planning and preparedness requirements on federal administrators, and to increase federal assistance to victims and communities.[19]

Legislation to amend the Stafford Act also received action in the 110th Congress. On July 31, 2008, the House Transportation and Infrastructure Committee ordered to be reported H.R. 6658: Disaster Response, Recovery, and Mitigation Enhancement Act of 2008, which would make significant changes in the Stafford Act regarding, but not limited to, temporary employees, warning systems, pre-disaster hazard mitigation; the bill also would establish new authorities for existing programs and the funding mechanism. The bill was not passed into law. Another bill reported from the same committee on September, 2007, H.R. 2775: To amend the Robert T. Stafford Disaster Relief and Emergency Assistance Act to, would have amended the statute by authorizing the Emergency Management Performance Grant (EMPG) program but was not passed into law.[20]

Also in the 110th Congress, the House approved H.R. 6109: Pre-Disaster Mitigation Act of 2008, which would amend the Stafford Act to: (1) increase the amount guaranteed to each state under the pre-disaster mitigation program; (2) require other financial assistance under the program to be awarded on a competitive basis; and

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[18] P.L. 93-288, 88 Stat. 143, at § 102

[19] Bea, Keith. Federal Stafford Act Disaster Assistance: Presidential Declarations, Eligible Activities, and Funding." Updated August 15, 2008. CRS Report for Congress. Available at: http://assets.opencrs.com/rpts/RL33053_20080815.pdf.

[20] Bea, Keith. Federal Stafford Act Disaster Assistance: Presidential Declarations, Eligible Activities, and Funding." Updated August 15, 2008. CRS Report for Congress. Available at: http://assets.opencrs.com/rpts/RL33053_20080815.pdf.

(3) authorize appropriations for the program through fiscal year 2011. Legislation was passed in 2007 specific to the administration of Stafford Act provisions in the Gulf Coast (cost-share waivers and cancellation of loan repayment requirements), which were folded into P.L. 110-28, the U.S. Troop Readiness, Veterans' Care, Katrina Recovery, and Iraq Accountability Acts.[21]

[21] Bea, Keith. Federal Stafford Act Disaster Assistance: Presidential Declarations, Eligible Activities, and Funding." Updated August 15, 2008. CRS Report for Congress. Available at: http://assets.opencrs.com/rpts/RL33053_20080815.pdf.