



The Rippling Effects of Insurance Uncertainty on Commercial Real Estate

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In late 2002, the Bush Administration came galloping to the rescue of a besieged insurance industry. The issue? The terrorist attacks of September 11 had thrown a wrench into the very foundation of how risk was priced. The arbitrary nature of terrorism made it very difficult to predict the magnitude or the likelihood of future attacks, as there was no probabilistic model that could effectively determine a particular level of risk. Enter TRIA. On November 26, 2002, President Bush signed the Terrorism Risk Insurance Act of 2002 (TRIA), legislation that would effectively provide insurers with a needed backstop in the event future catastrophic events were to occur. As much as people might hope this measure permanently eliminates the problem, think again – this legislation has been put in place for only three years, the time estimated it will take for the insurance industry to figure out longer-term solutions.

In our fourth paper, Gill explores the emerging insurance quandary that impacts commercial real estate finance. It describes the strong link between the insurance and real estate finance industry (the latter is one of the biggest drivers of GDP, ranking fourth in the US, and as of 2002 the commercial mortgage debt in the US equaled \$1.7 trillion). In a pre-September 11th world, the insurance industry was accustomed to writing “all-risk” policies that routinely made provisions for events of mass disruption. The policies written in the industry at that time could have been likened to a quilt that provided broad coverage. In the two years that have passed, however, that quilt has been separated into a large number of individual patches that are each subject to a far greater degree of scrutiny. Securing terrorism insurance especially on assets that are centrally located in first tier cities had been an almost cost-prohibitive exercise prior to the unveiling of TRIA. This legislation has effectively placed a cap on insurance industry exposure, and in the process, made it possible to include terrorism in the bunch with other covered perils. A good measure of relief no doubt, but non-sustainable in the long run.

Even as the industry puts out the fires of uncertainty associated with property insurance, the next hurdle is dealing with the issues associated with liability and casualty insurance. The paper will present the issues and find out how they are currently being managed. It also touches on the insurance nuances of business continuity planning, and how this area is being embraced by the industry and being used as the foundation to come up with new insurance products. The rate of escalation of facility insurance is directly proportional to the proximity that facility is to a central city core; therefore insurance uncertainty becomes one of the many potential drivers of decentralization.

Industry Vertical	Principal Learning Benefits
Corporate Real Estate Executives	<ul style="list-style-type: none">• What are the principle limitations of TRIA? How do the nuances of a changing insurance landscape affect my operations? What are the main contentious issues in real estate insurance going forward? How can adequate protection be secured through innovative lease clauses?
Business Continuity Planners and Strategists	<ul style="list-style-type: none">• What are the business continuity related issued associated with property insurance for large facilities? How do insurance issues impact the manner in which BCP strategies are executed?
Institutional Owners, Landlords and Managers	<ul style="list-style-type: none">• Might changes in insurance policy alter the fundamentals of my portfolio? Will changes in the insurance industry going forward affect my ability to attract and retain tenants? Beyond property insurance, what are the other major areas that I need to know about?
Industry Analysts	<ul style="list-style-type: none">• How carefully do I need to monitor developments of TRIA or amendments to it? As the insurance industry becomes even more complex, how will this directly and indirectly affect real estate? What institutional owners are changing the composition of their portfolios – is it related to insurance?
CEOs, CFOs, CIOs	<ul style="list-style-type: none">• What are the particulars of our insurance coverage today? How do current changes in the industry affect our bottom line? Can better efficiencies be attained in different locations?
Commercial Brokerage	<ul style="list-style-type: none">• Learn the nuances of insurance and how it directly and indirectly impacts the real estate industry; how can tenants or new investors be protected by lease clauses that specifically address insurance?

REAL ESTATE CONTINUITY