COVID-19: Financial and Economic Impacts on the P&C Insurance Industry

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Coronavirus & the Recession of 2020: Outline

- **P/C Insurers: Overcoming Uncertainty With Strength**
  - Financial Overview: The Industry's Financial Position Amid the COVID-19 Pandemic
- **COVID-19: Potential Coronavirus Impacts on Key Lines**
- **Investment Market Issues: Volatility Rules, Low Interest Rates are Back**
- **The Economy and COVID-19: Overview & Outlook**
- **Commercial Lines Rate Trends**
- **Federal & State COVID-19 Initiatives Impacting Commercial Insurers**
- **Summary and Conclusions**

P/C Insurance Industry: Financial Overview Amid the COVID-19 Pandemic

The P/C Insurance Industry Entered the COVID-19 Pandemic from a Position of Financial Strength

Economic, Financial Market, Regulatory and Tort Risks Are Major Challenges Going Forward

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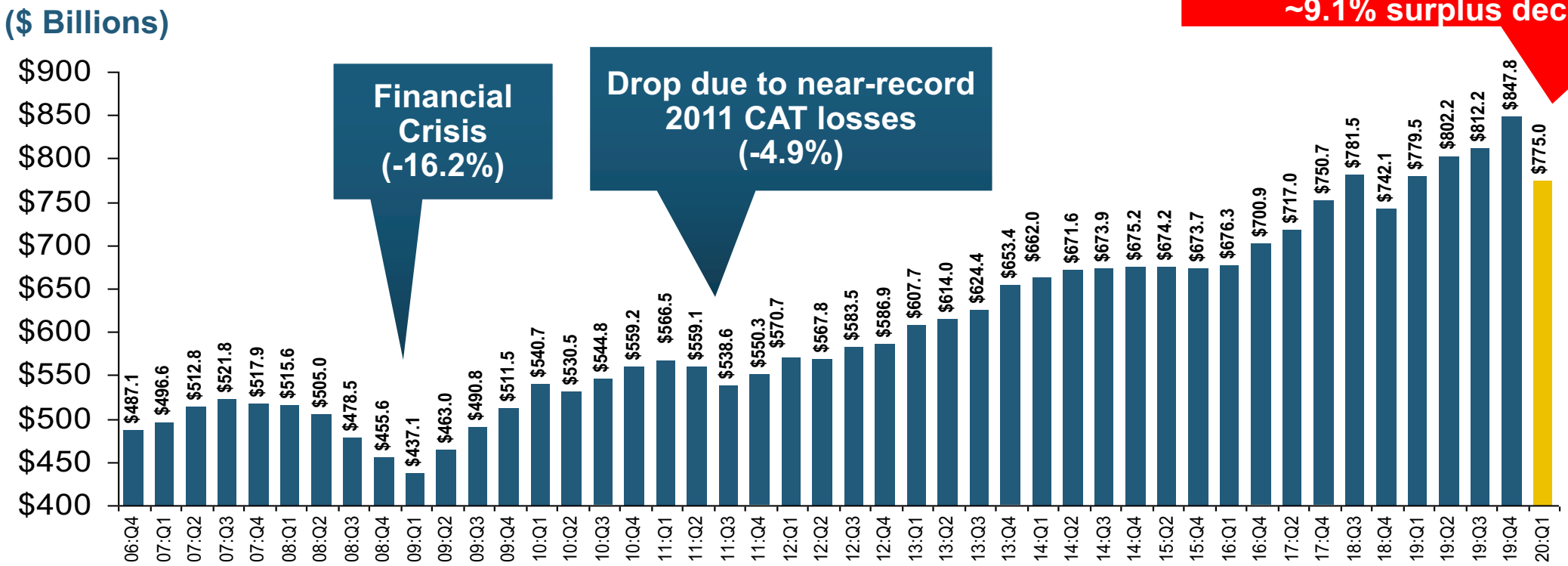
Policyholder Surplus (Capacity), 2006:Q4–2020:Q1E

The P/C insurance industry entered the COVID-19 pandemic from a position strength and can easily withstand the estimated ~9.1% surplus decline

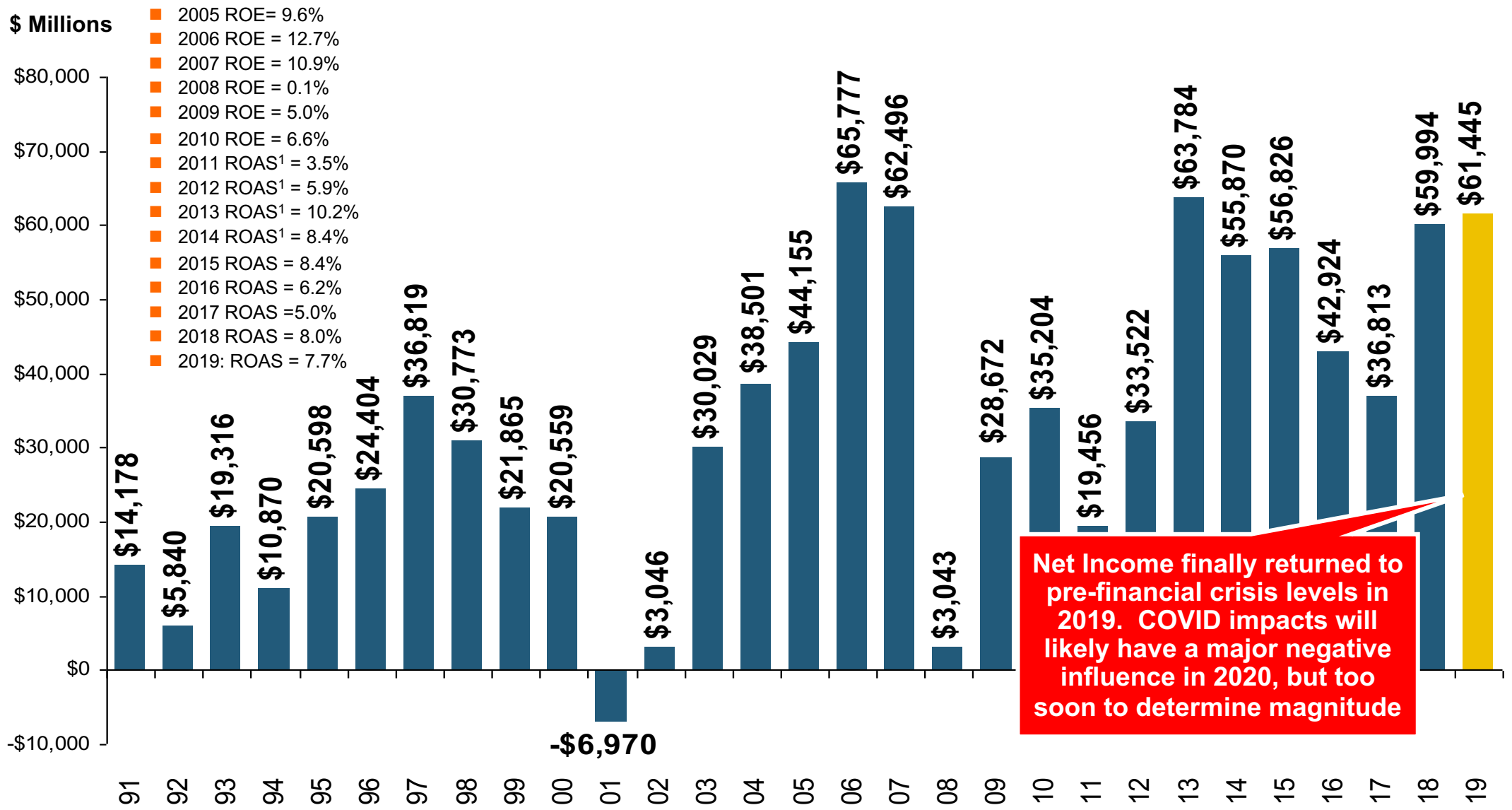


2010:Q1 data includes $22.5B of paid-in capital from a holding company parent for one insurer's investment in a non-insurance business.

Policyholder Surplus is the industry's financial cushion against large insured events, periods of economic stress and financial market volatility. It is also a source of capital to underwrite new risks.

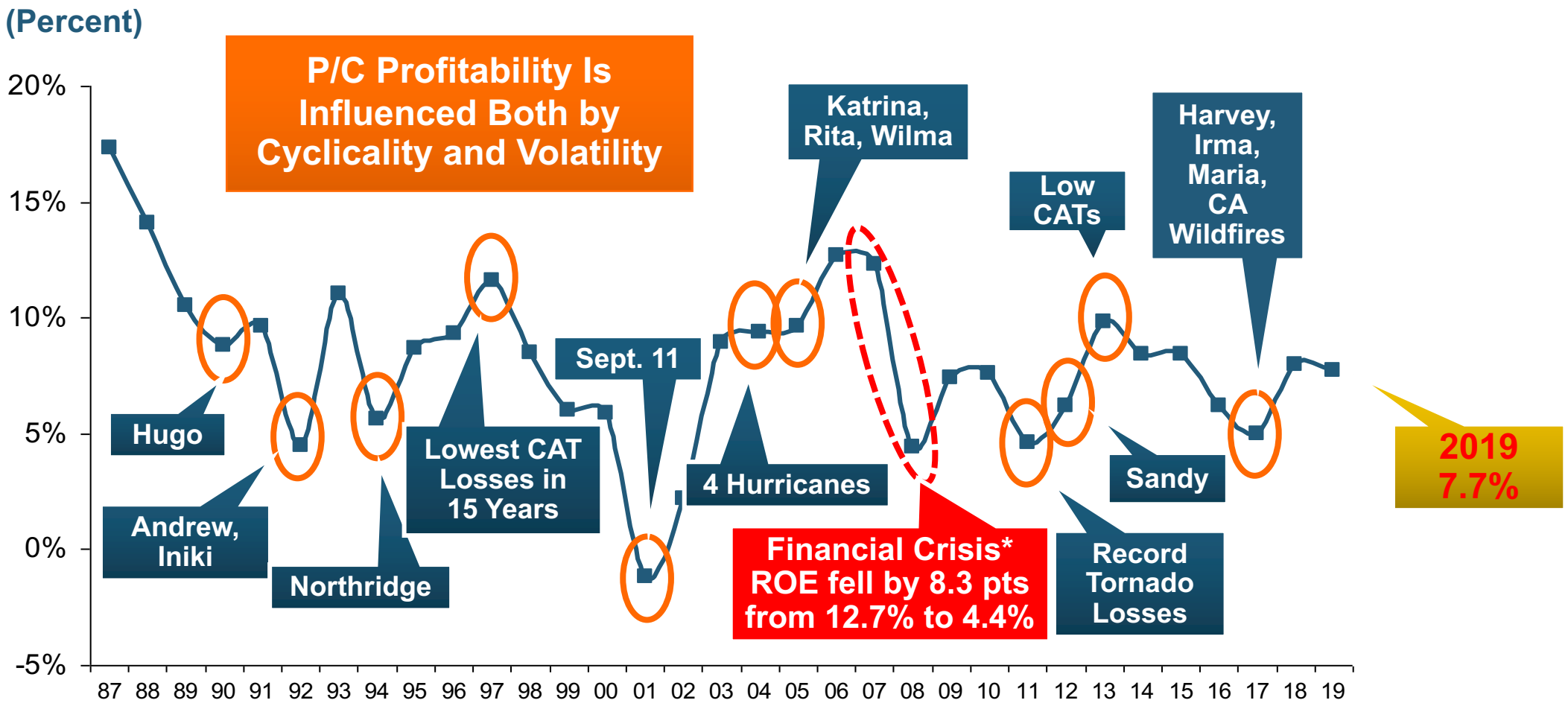
Sources: ISO, A.M .Best; 2020E from Risk and Uncertainty Management Center, University of South Carolina.

P/C Industry Net Income After Taxes, 1991–2019F*



*2019 estimate based on annualized actual Q3:19 figure of $48.075B. ROE figures are GAAP; [1]Return on avg. surplus. Excludes Mortgage & Financial Guaranty insurers for years (2009-2014).
Sources: A.M. Best, ISO.

ROE: Property/Casualty Insurance by Major Event, 1987–2019



*Excludes Mortgage & Financial Guarantee in 2008 – 2014.
Sources: ISO, *Fortune*; A.M. Best (2018E-2019F); USC RUM Center.

Percentage Point Change in P/C ROEs During Past Economic Downturns: 1971 - Present

Change in P/C ROE During Past Economic Downturns

Avg.: -4.5% (-4.0% ex. 2000-01)

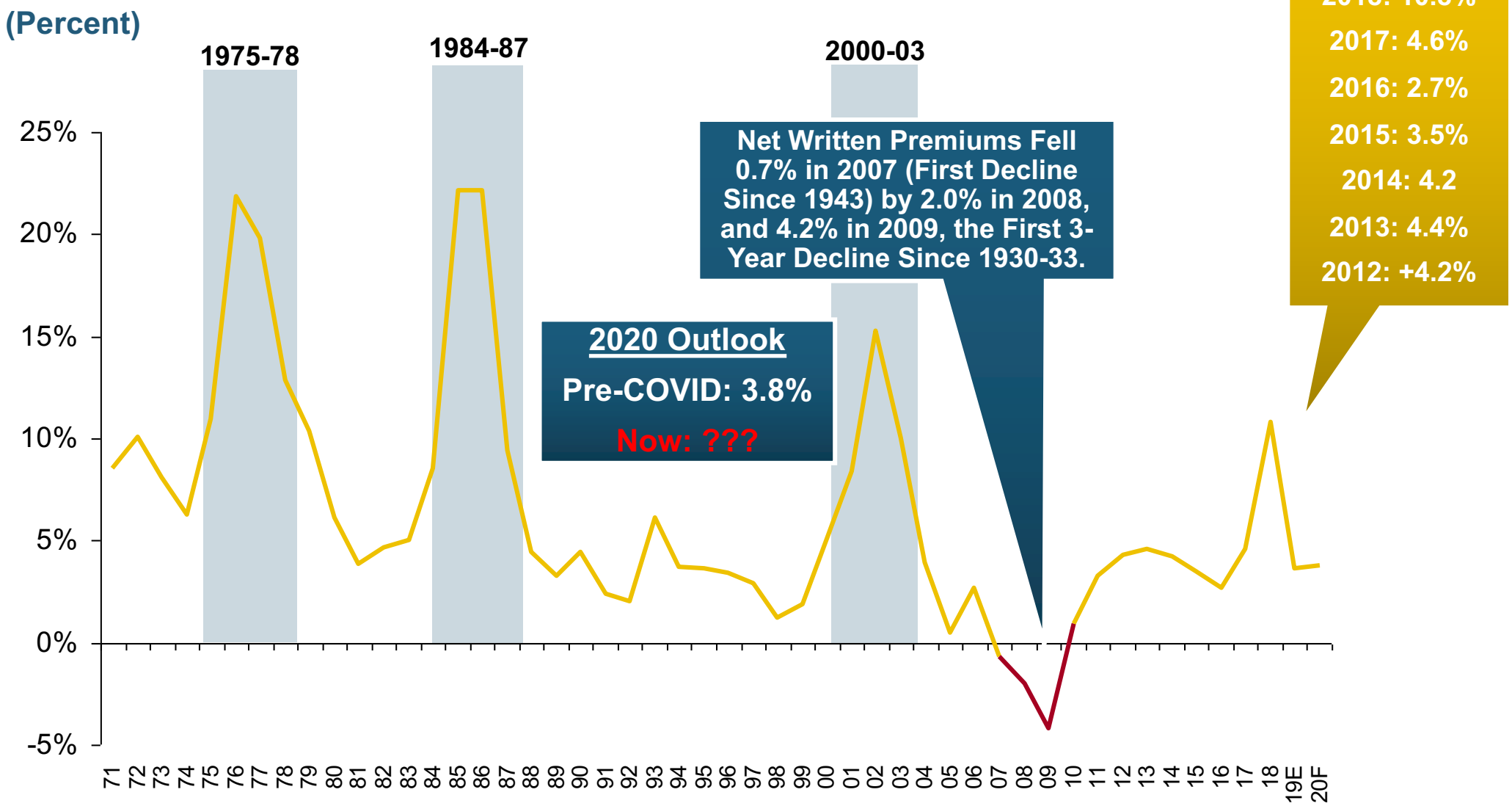
Median: -5.0% (-3.0% ex. 2000-01)

Although the COVID-19 economic downturn will be sharp, it's expected to be brief with a rapid "V-Shaped" recovery

*2000-2001 decline impacted by 9/11 losses.

Source: USC Center for Risk and Uncertainty Management.

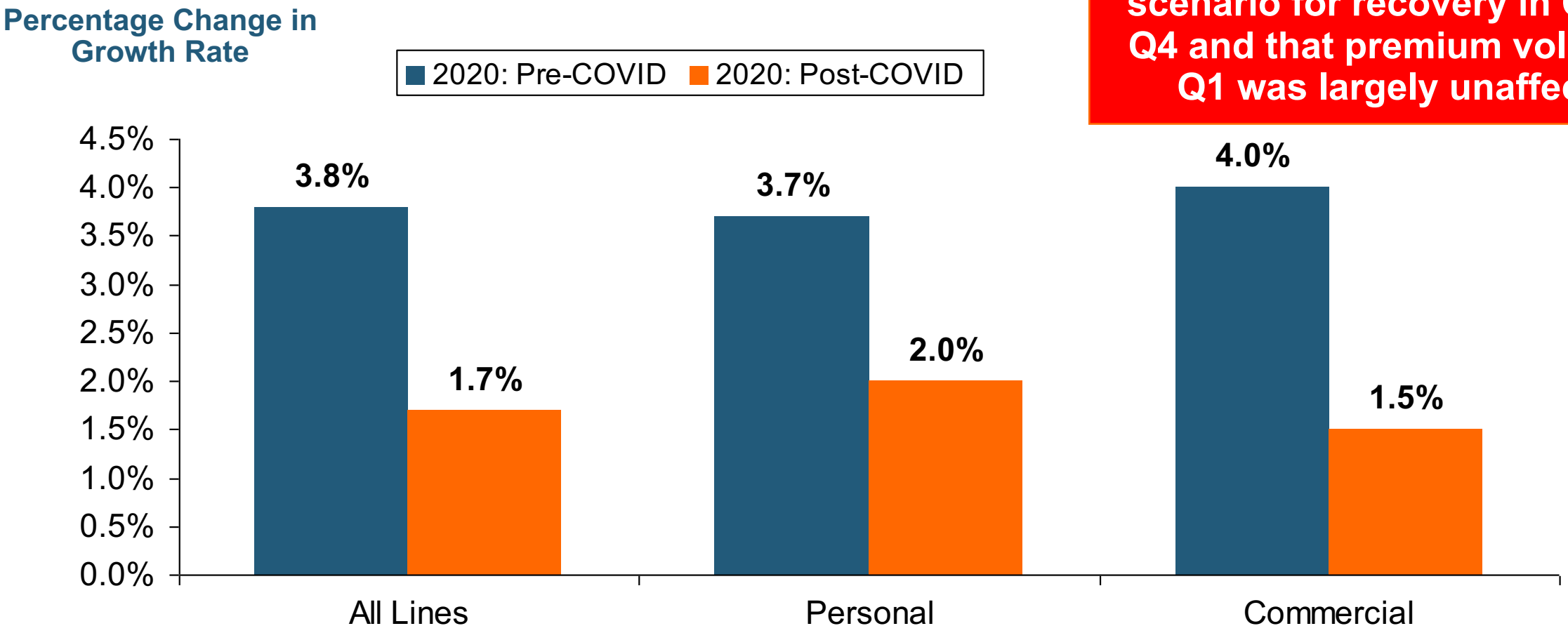
Net Premium Growth (All P/C Lines): Annual Change, 1971—2020F (Pre-COVID)



*Pre-COVID-19 forecast from A.M. Best Review & Preview (Feb. 2020). NOTE: Shaded areas denote "hard market" periods
Sources: A.M. Best (1971-2013, 2020F), ISO (2014-19); Risk & Uncertainty Management Center, Univ. of South Carolina .

2020 Pre- vs. Post-COVID Growth Expectations for P/C Insurance: From Modest to Miserly

Note: 2020 expectations are based on a modestly optimistic scenario for recovery in Q3 and Q4 and that premium volume in Q1 was largely unaffected



Source: 2020 Pre-COVID-19 figures from Best's Review & Preview (Feb. 2020); Post-COVID estimates from USC Center for Risk and Uncertainty Management.

Potential Impacts of COVID-19 on *Written Premium* in 2020, by Key Line

Line	Estimated Premium Impact
Workers Compensation	12.5% to 25% reduction in premium written in 2020 ***(equates to $5.9B to $11.75B DWP)***
Business Interruption & Contingency	7% to 13% reduction in premium volume (US & UK)
General Liability*	$1.5B to $6.3B premium reduction in US
Personal Auto	~$10B in refunds, rebates (equates to ~4% of DWP)
Personal Travel Insurance	29% to 78% reduction in premium written (US & UK)
Personal/Comm. Motor	~10% reduction in US; 0% to 11% reduction in UK
Marine/Aviation/Transport	$0.7B-$1.5B (US); $0.6 - $1.2B (UK)

*Includes nursing home professional liability.

Source: Derived from Willis Towers Watson, *Scenario Analysis of COVID-19 Pandemic* (Fig.11, 14), May 2020. and other sources; Risk and Uncertainty Management Center, University of South Carolina.

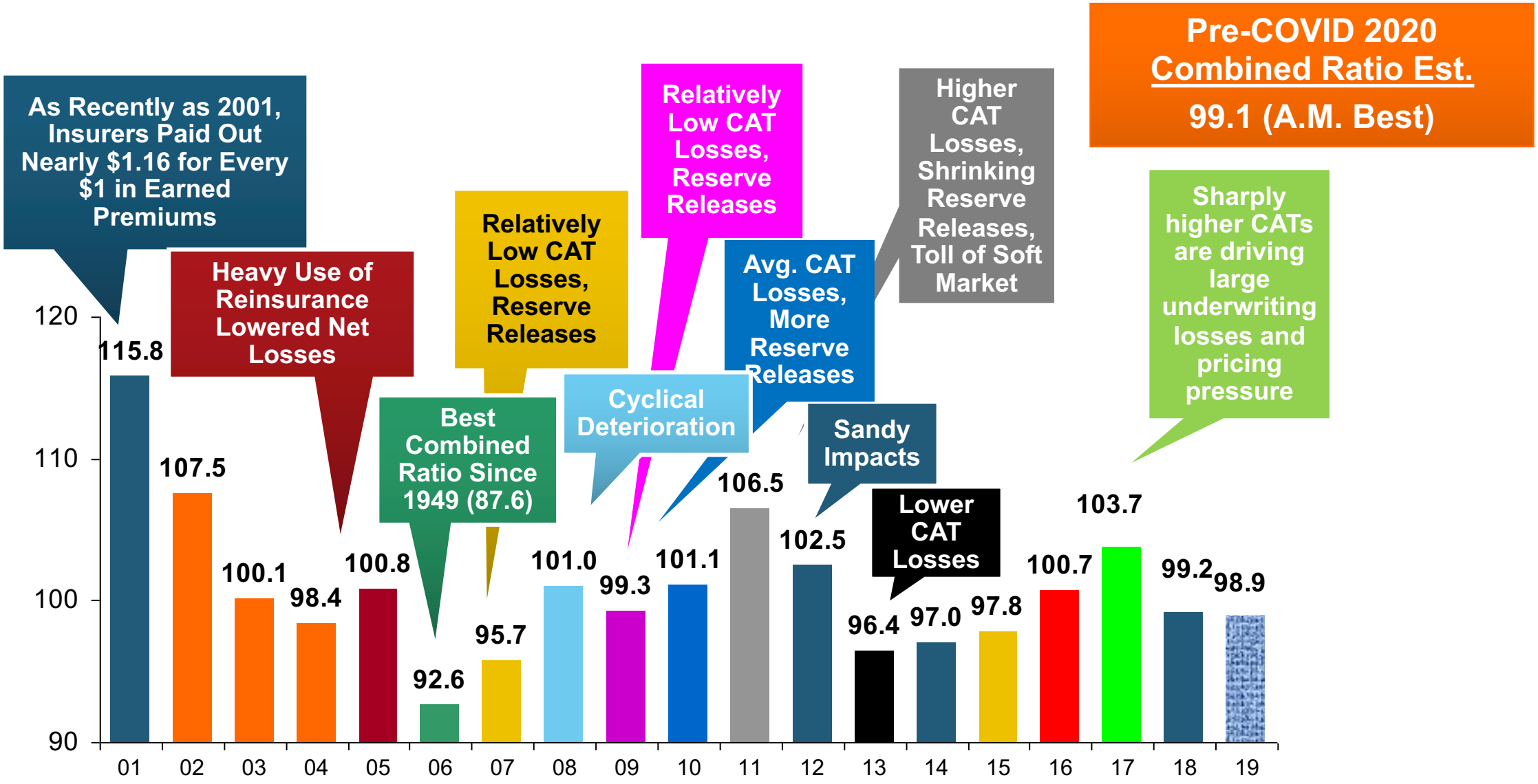
Potential Impacts of COVID-19 on *LOSSES* in 2020, by Key Line

Line	Estimated Loss Impact
Workers Compensation	$0.2B - $92B ***(depends on severity of pandemic and "presumption" determination)***
Business Interruption & Contingency	$2B - $22B (US); $1.1B - $13.9B (UK)
General Liability*	$0.7B to $27B loss across US & Bermuda markets
Personal/Comm. Motor	$26B - $57B reduction in personal auto and $4.2B - $9.4B commercial (US); $1 - $7B overall reduction in UK
Mortgage	$0 - $1.7B loss across US & Bermuda markets
D&O	$0.6 - $4.0 loss across US & Bermuda markets
Marine/Aviation/Transport	$0.3B-$1.3B reduction (US); $0.6 - $1.1B (UK)

*Includes nursing home professional liability.

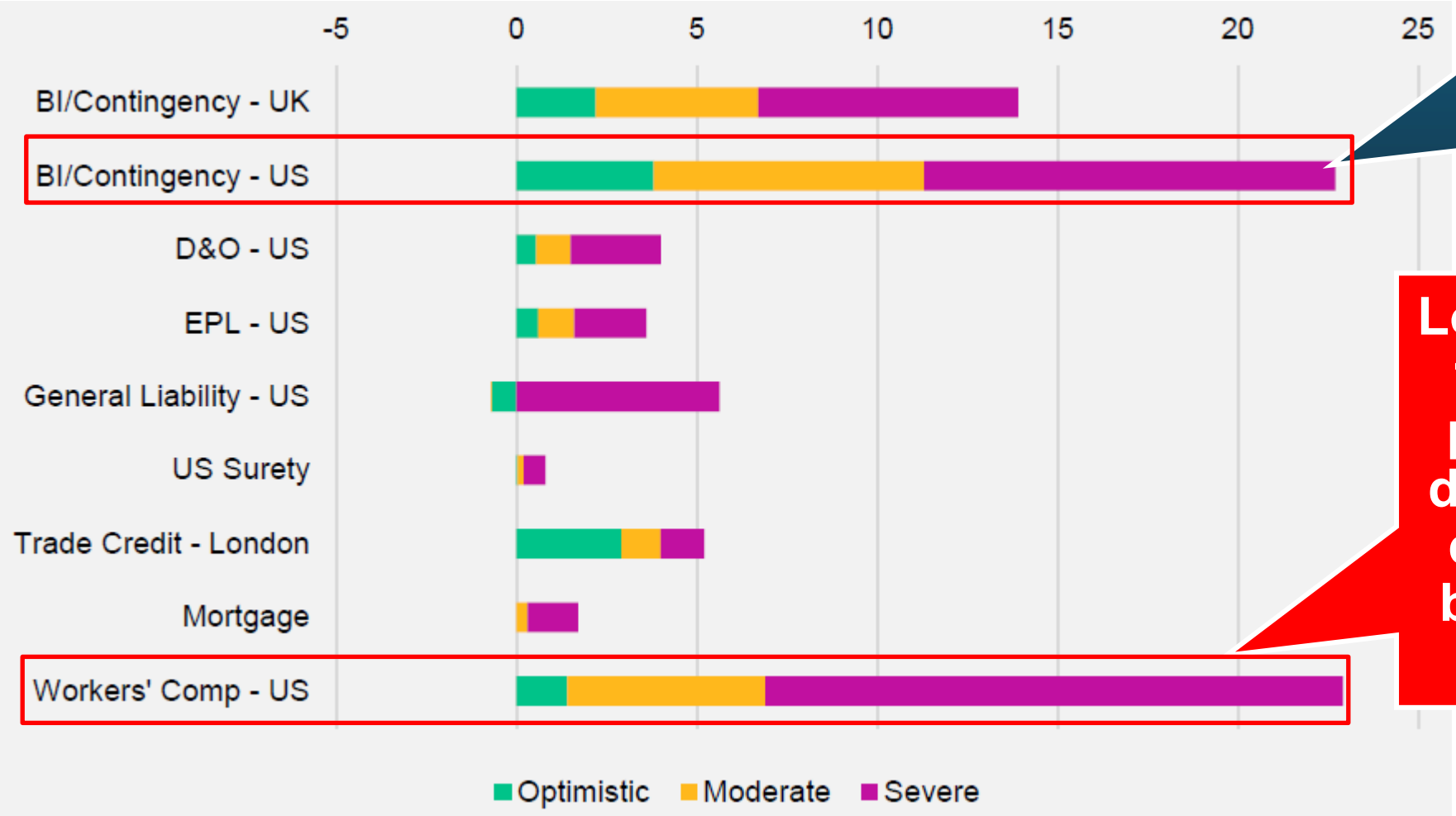
Source: Derived from Willis Towers Watson, *Scenario Analysis of COVID-19 Pandemic* (Fig.11, 14), May 2020. and other sources; Risk and Uncertainty Management Center, University of South Carolina.

P/C Insurance Industry Combined Ratio, 2001–2019E*



* Excludes Mortgage & Financial Guaranty insurers 2008--2014.
Sources: A.M. Best, ISO (2014-2019).

Potential Impact of COVID-19 on Insured Losses by Line



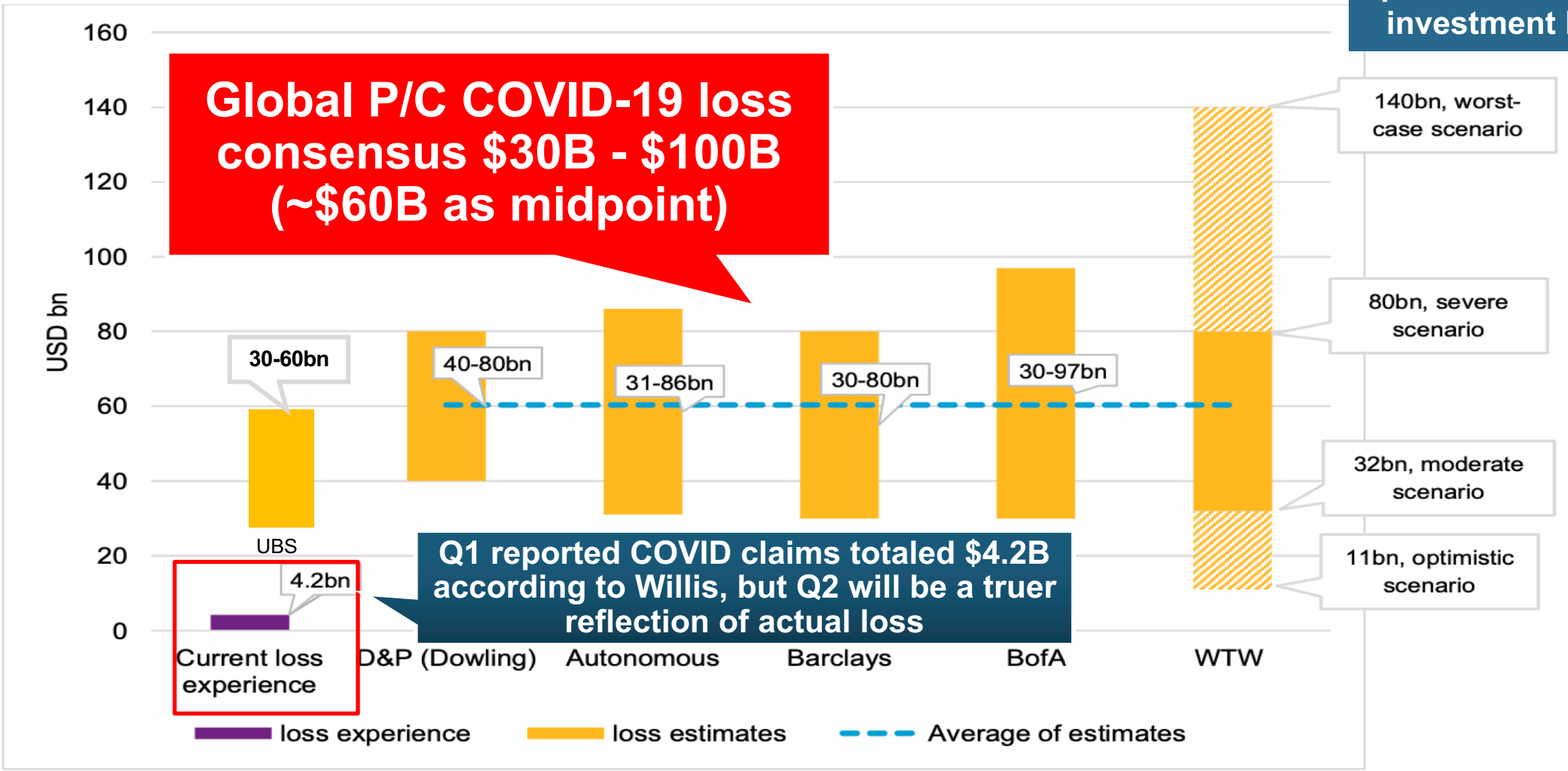
Business Interruption losses are potentially material even under the moderate severity scenario

Loss impacts of COVID-19 on the WC line are potentially severe but depend not only on the course of the disease but state decisions on presumption

Source: Willis Towers Watson, *Scenario Analysis of COVID-19 Pandemic* (Fig.10), May 2020; Risk and Uncertainty Management Center, University of South Carolina.

COVID-19 Announced Losses vs. Top-Down Industry Estimates (as of May 12, 2020)

Lloyd's: Says its own p/c claims could reach $4.3B by June 30. Estimates global p/c losses at $107B; Global investment losses = $96B*



*Lloyd's CEO John Neil appearance on CNBC, May 14, 2020: https://www.cnbc.com/2020/05/14/lloyds-of-london-coronavirus-will-be-largest-loss-on-record-for-insurers.html

Sources: Company disclosures, Dowling & Partners, Barclays Research, Autonomous Research, BofA Global Research, UBS Securities, Willis Towers Watson from Artemis.bm accessed at https://www.artemis.bm/news/consensus-emerging-on-30bn-to-100bn-covid-19-industry-loss-willis-re/; Risk and Uncertainty Management Center, University of South Carolina.

Viral Outbreaks Are Not An Insurable Risk

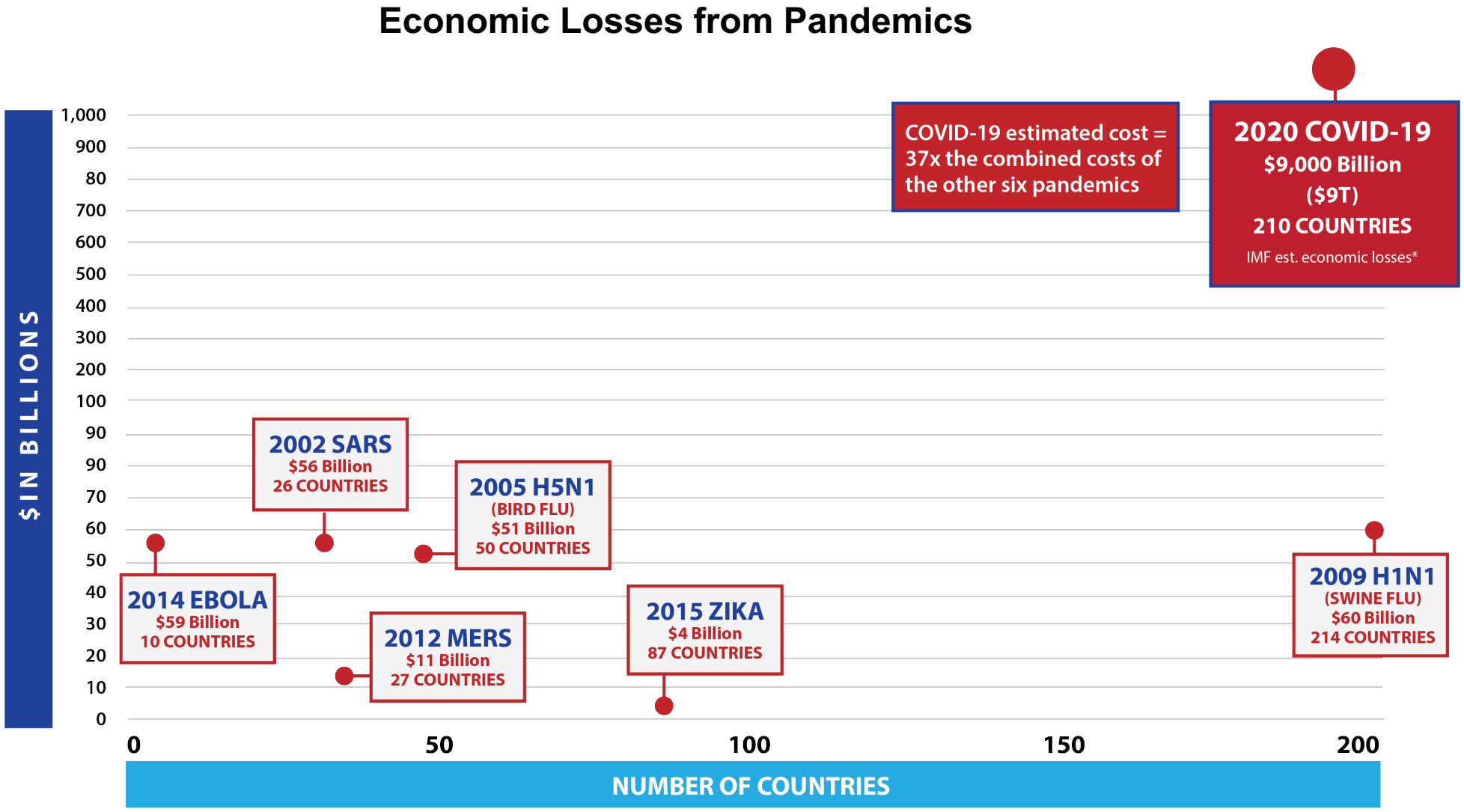
Pandemics are frequent, severe, and widespread (7 pandemics with multi-billion$ economic losses in just the last 18 years)

For Reference

2005 Katrina $58 Billion

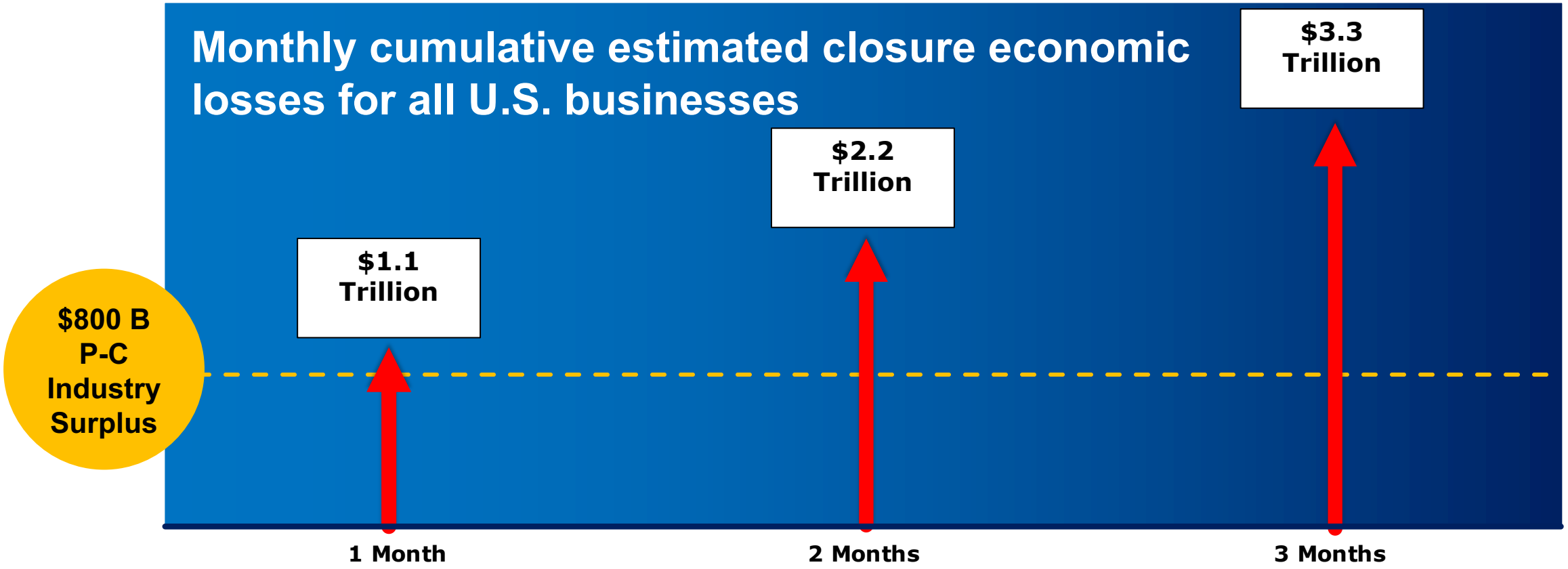
2001 9/11 $48 Billion

(insured losses)



*Sources: APCIA using published reports, including IMF, World Bank, Learnbonds.com; APCIA adjustment to 2020 USD

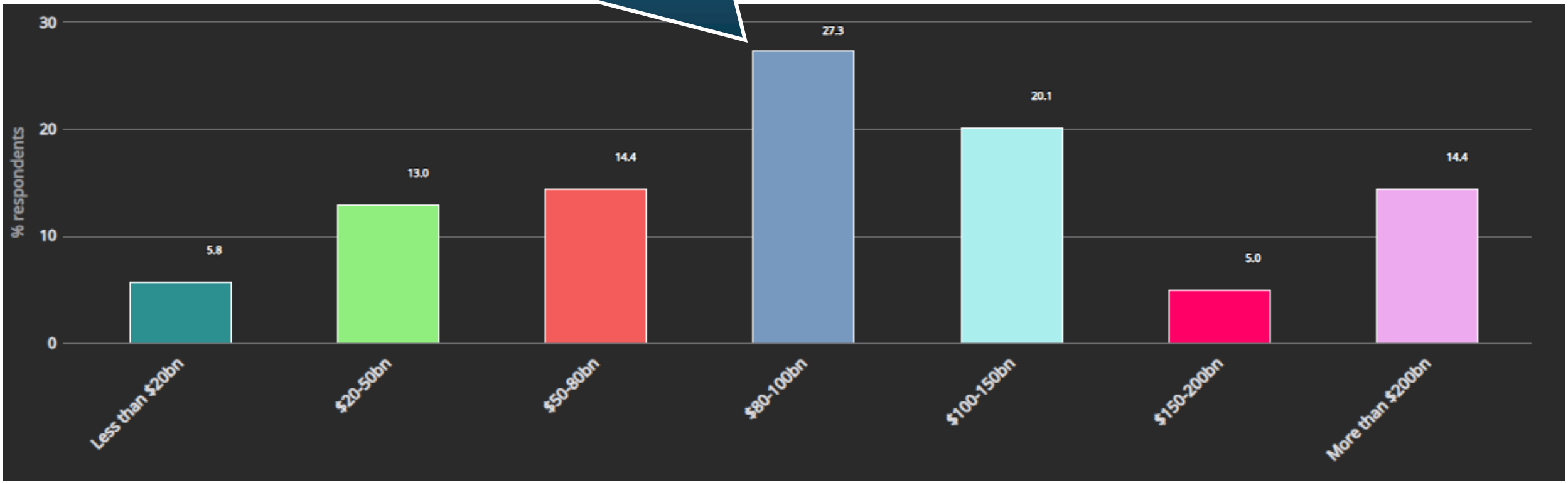
Private Insurance Cannot Close the Gap



Source: APCIA estimates using publicly available data sources, including Bureau of Labor Statistics, Insurance Services Office (Verisk Analytics, Inc.), Houston Chronicle, S&P Global Market Intelligence, and other published reports.

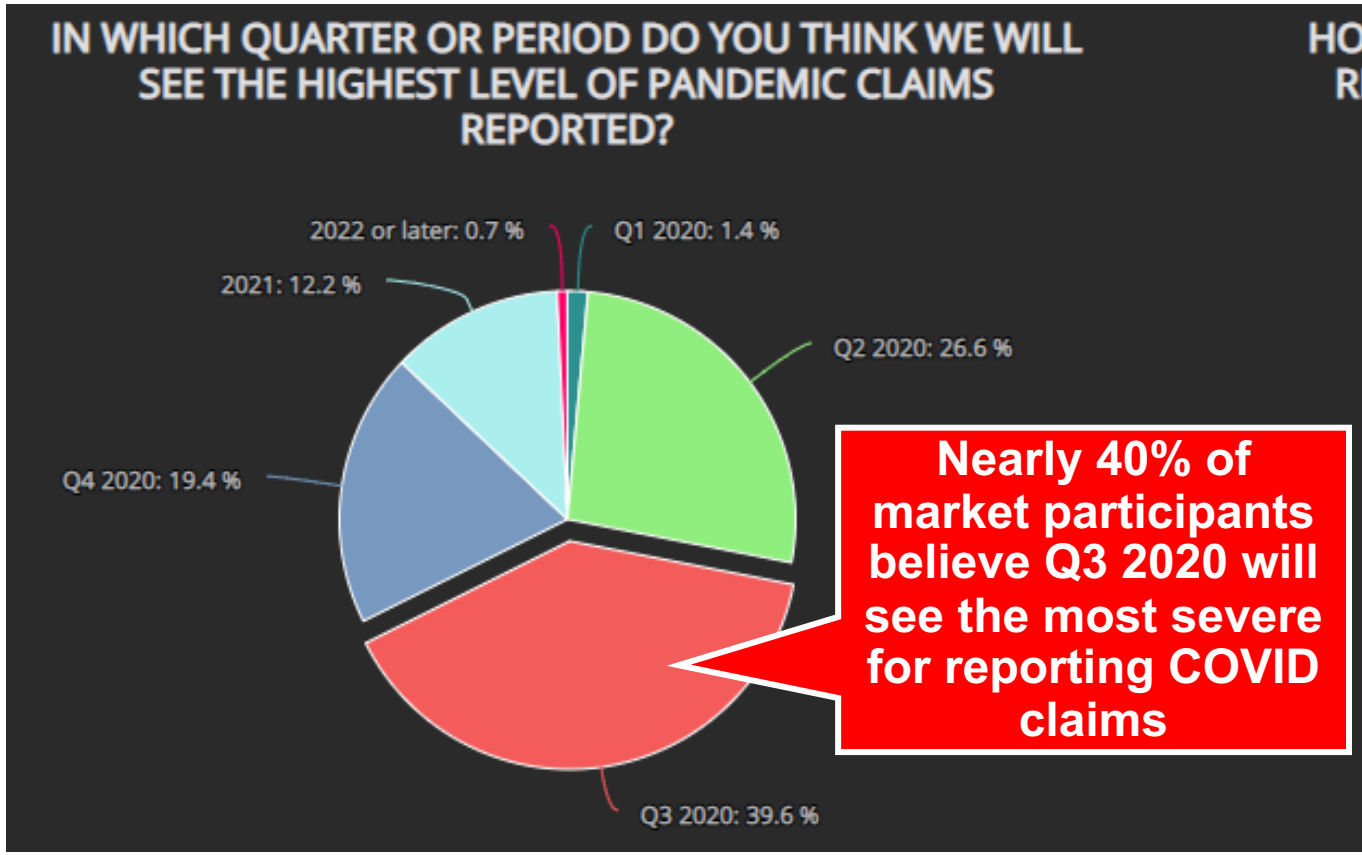
Market Survey: Estimated Global Non-Life COVID-19 Losses

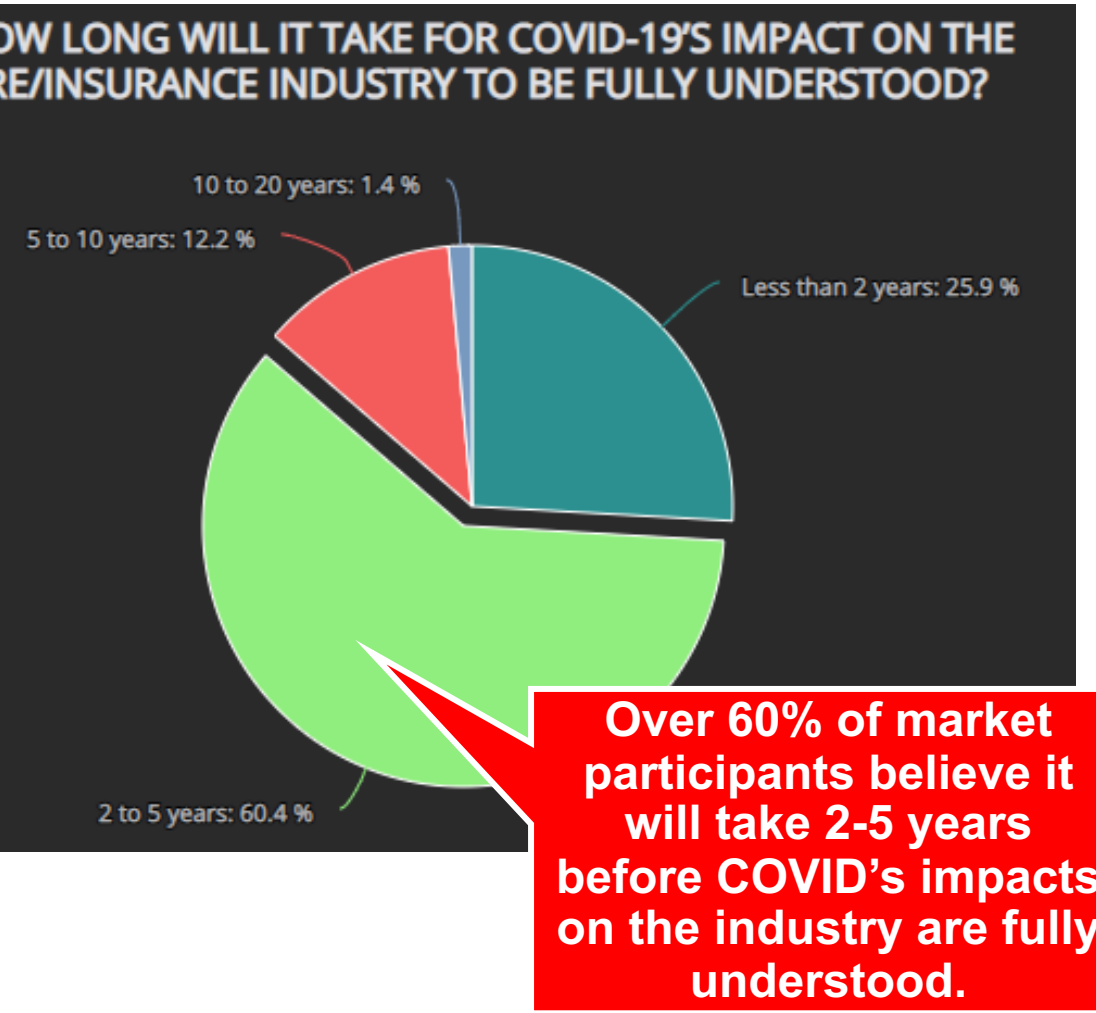
The plurality (27.3%) of market participants believe insured losses will range between $80B and $100B; 60.5% believe losses will be less than $100B while 39.5% believe losses will exceed $100B.



Source: Artemis COVID-19 Market Survey (June 2020) accessed at: https://www.artemis.bm/coronavirus-survey-update/

Market Survey: COVID-19 Claims





Source: Artemis COVID-19 Market Survey (June 2020) accessed at: https://www.artemis.bm/coronavirus-survey-update/

Catastrophe Loss Update: *Major Driver of Rate Pressure*

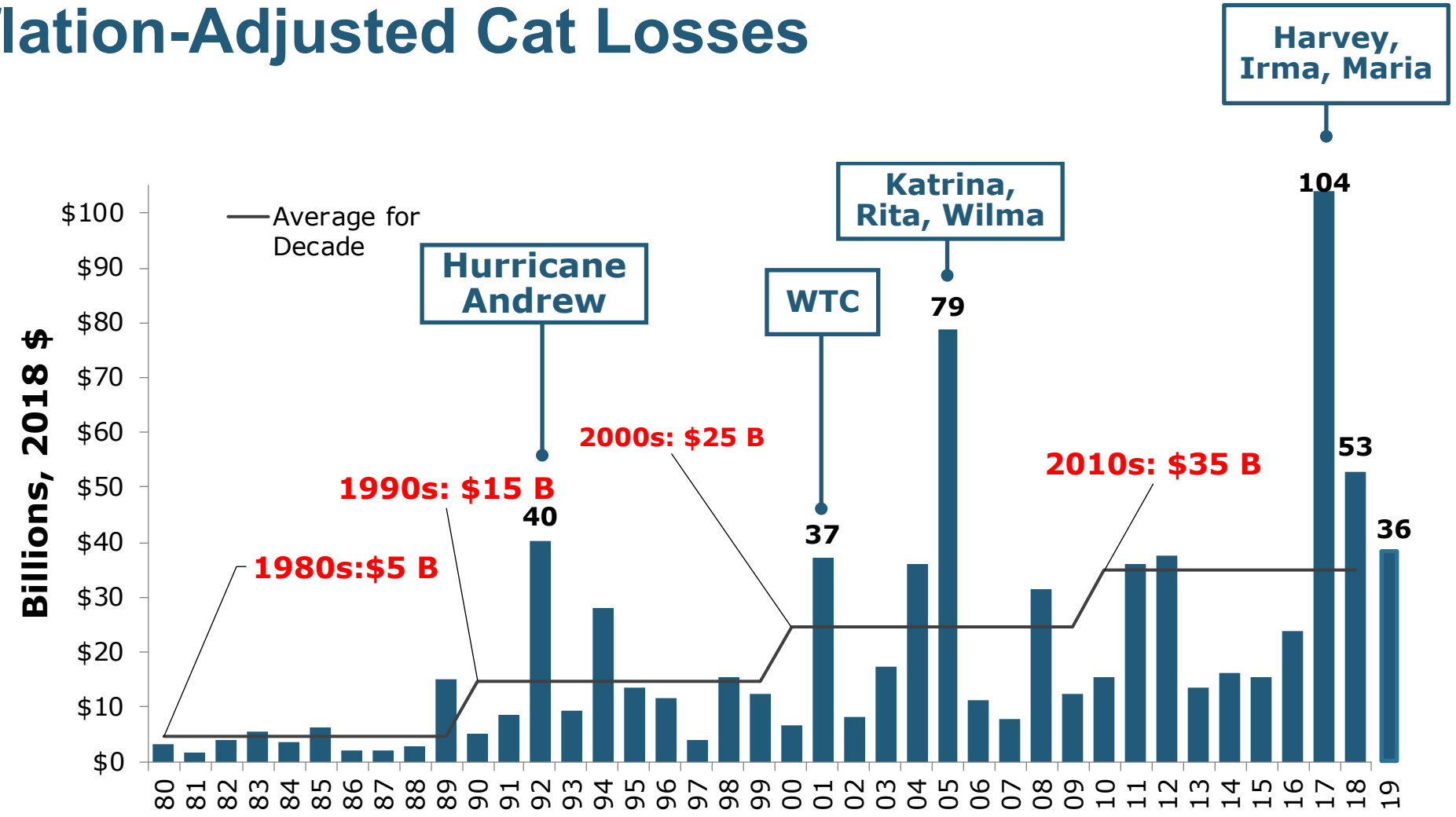
CAT Losses for the Decade Just Ended Were Up Materially—Costliest Ever

Primary, Reinsurance and Retro Markets All Impacted and Are Pressuring Rates

COVID Pressure Kicks Off the New Decade

19

U.S. Inflation-Adjusted Cat Losses



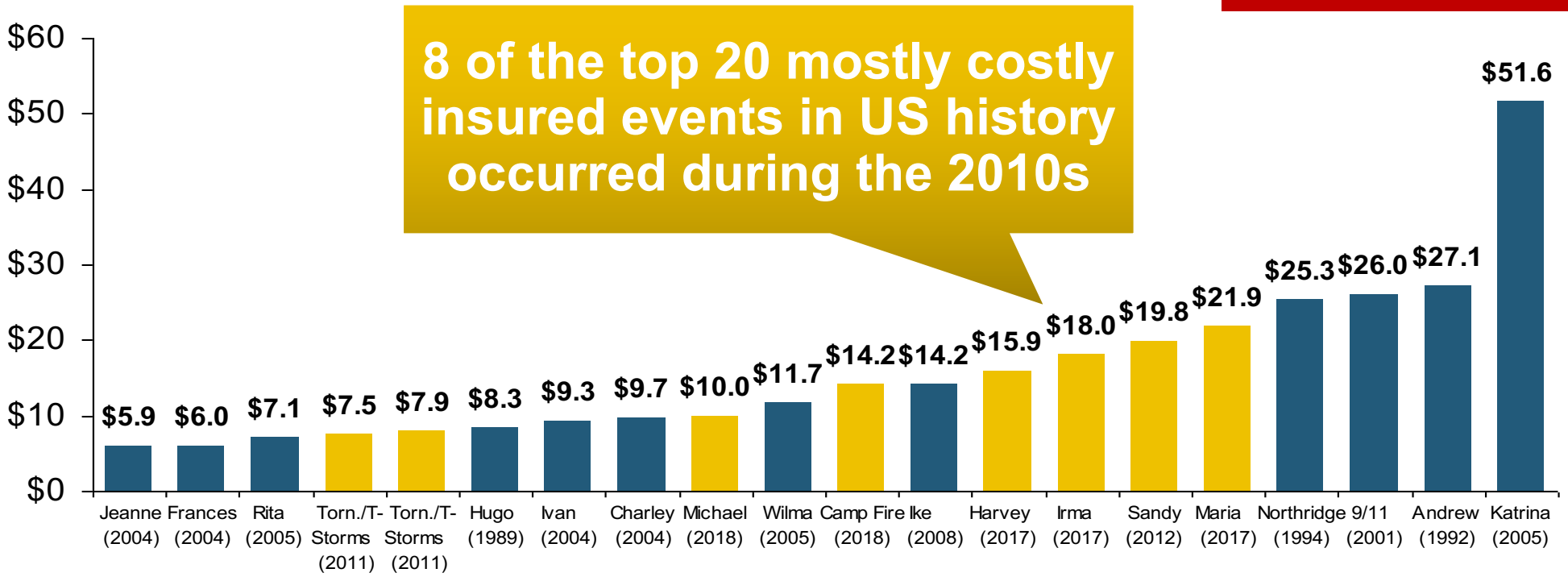
2018 – Third worst year for U.S. Insured Catastrophe Losses.
Average Insured Loss per Year for 1980-2019 is $19.8 B.

Sources: Property Claims Service, a Verisk Analytics business; Insurance Information Institute.

Top 20 Most Costly Disasters in U.S. History—Katrina Still Ranks #1

COVID-19 insured property losses remain highly uncertain, but could easily make the top 10

(Insured Losses, 2017 Dollars, $ Billions)*

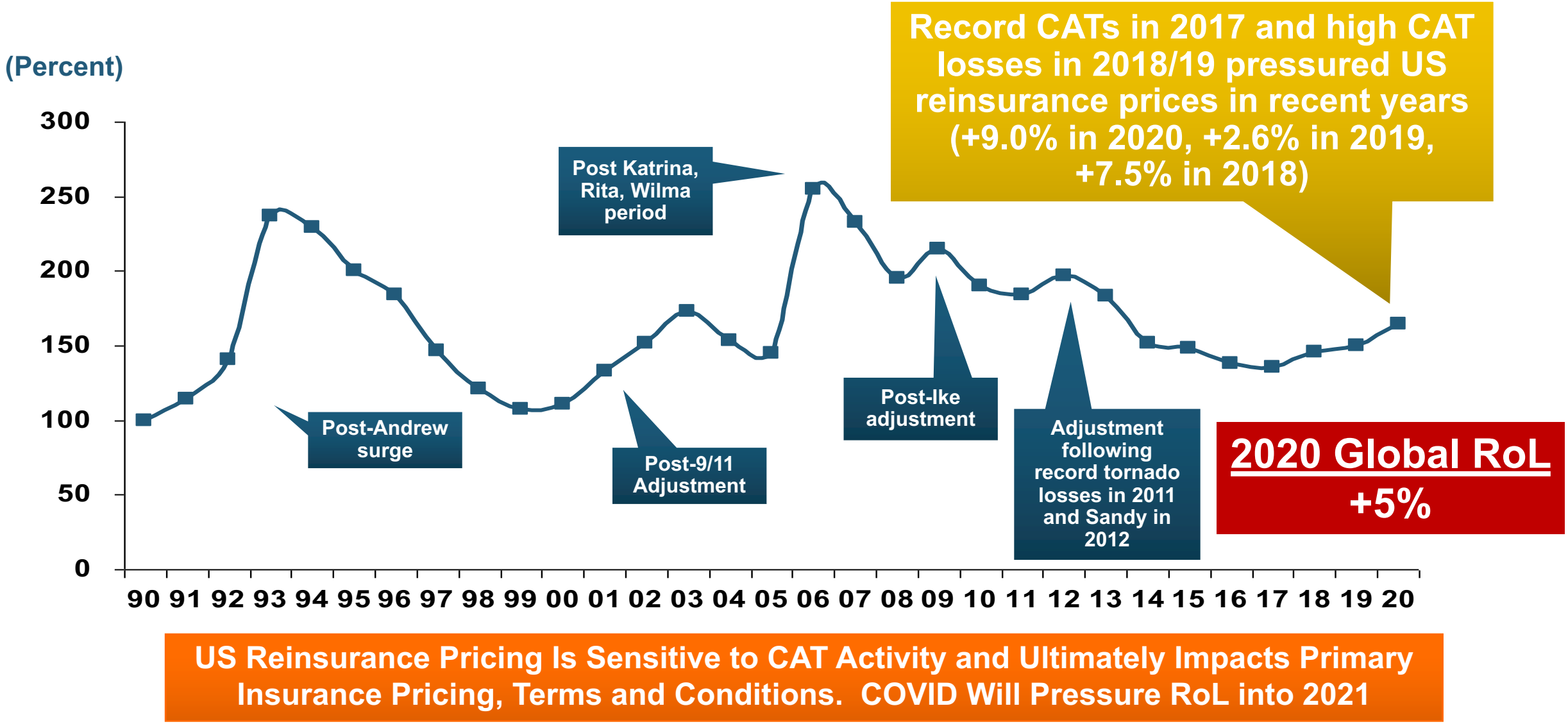


17 of the 20 Most Expensive Insurance Events in US History Have Occurred Since 2004

*Estimated.

Sources: PCS, RMS, Karen Clark & Co; USC Center for Risk and Uncertainty Management adjustments to 2017 dollars using the CPI.

US Property Catastrophe Rate-on-Line Index: 1990 – 2020*



US Reinsurance Pricing Is Sensitive to CAT Activity and Ultimately Impacts Primary Insurance Pricing, Terms and Conditions. COVID Will Pressure RoL into 2021

*As of January 1 each year.

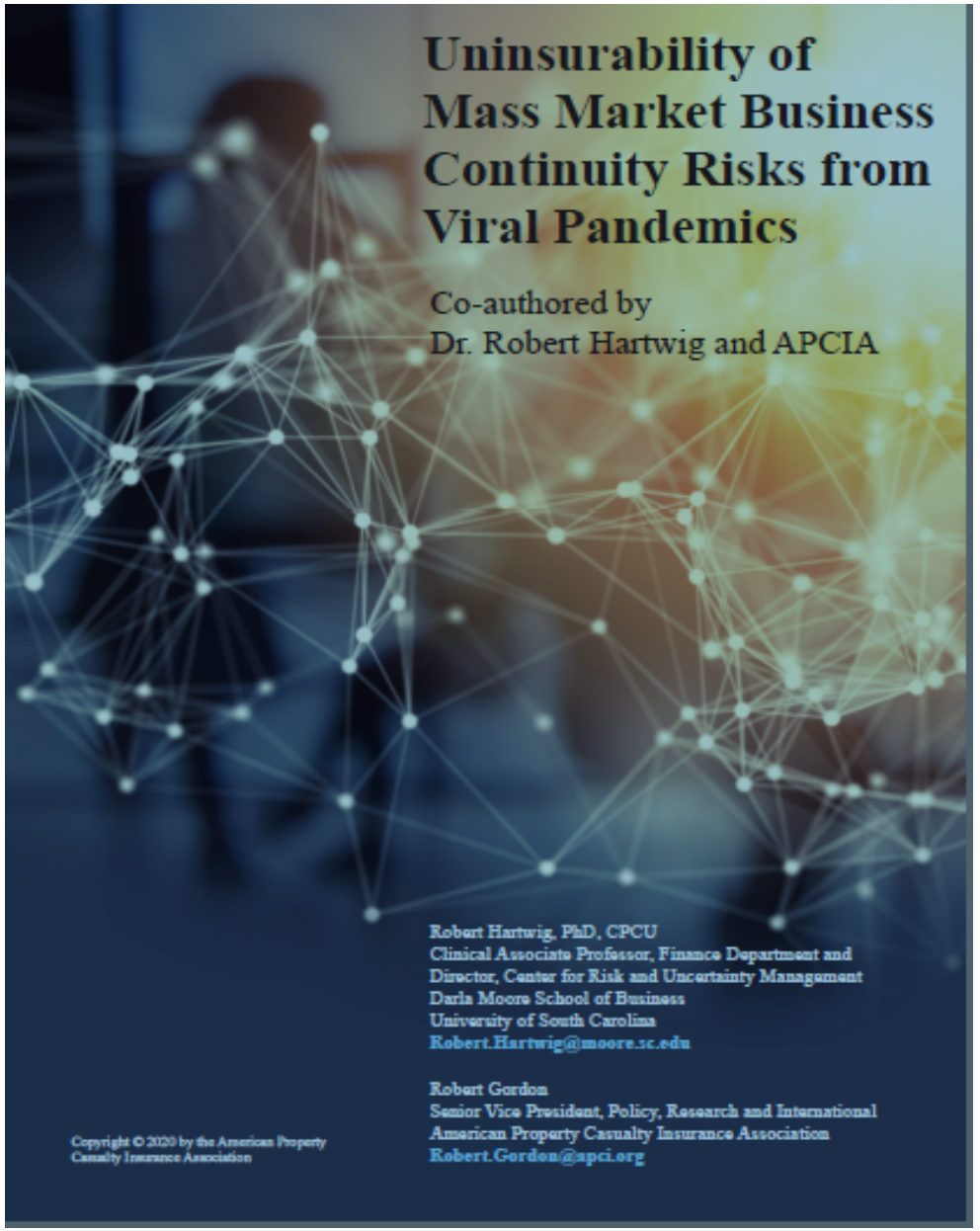
Source: Guy Carpenter; Artimes.bm accessed at: http://www.artemis.bm/us-property-cat-rate-on-line-index

Pandemic - An Insurable Risk?

Requirements of an Insurable Risk	Requirement Met? Yes/No
1. Large number of exposure units	**No.** While millions of individual businesses suffered business continuity losses arising from the COVID-19 pandemic, the pandemic's effects were global in scale and nearly simultaneous in scope, effectively reducing the number of exposure units to one—the business sector collectively.
2. Accidental/Random and unintentional loss	**No.** Pandemics are natural phenomena but the decisions by thousands of policymakers at all levels of government to close millions of businesses and restrict the movement of people was intentional.
3. Determinable and measurable loss	**No.** For insurers to determine losses, the scale and scope of losses for any given risk must be estimable. Business continuity losses from COVID-19, estimates for which remain highly uncertain and range into the trillions of dollars, are indeterminable due to their dependence on decisions made by thousands of policymakers at all levels of government, the pace at which consumers and businesses reengage in the economy and epidemiological developments.
4. No (ruinous) catastrophic loss	**No.** Unlike traditional catastrophe risks, pandemics by definition threaten all or most or the members of the risk pool simultaneously. The rapid aggregation of losses is destabilizing and potentially ruinous, threatening the solvency of individual insurers and the industry as a whole.
5. Calculable chance of loss	**No.** Pandemics have occurred throughout history but the policy response to COVID-19 is without precedent. Insurers traditionally rely on historical loss information and trends to estimate the frequency and severity (cost) for risks they insure. No such historical data exists for the policy response associated with the COVID-19 pandemic, hence premiums cannot be determined.
6. Economically feasible premium	**No.** Because pandemics by definition threaten all or most or the members of the risk pool simultaneously, the probability of loss is close to certainty. The high probability of loss combined with high claim severities necessarily lead to premiums that can approach or even exceed the cost of the claim itself.

New Paper on Insurability of Pandemic Risk

- Large scale business continuity risks from pandemics are generally note insurable in the private sector
- Business continuity risks are largely undiversifiable within private insurance markets and are highly correlated with other risks (e.g., investment risks)
- Large scale business continuity losses pose a potentially systemic risk to the industry and overall economy
- Import role for government



Download at: http://www.pciaa.net/docs/default-source/default-document-library/apcia-white-paper-hartwig-gordon.pdf

INVESTMENTS:
THE NEW REALITY

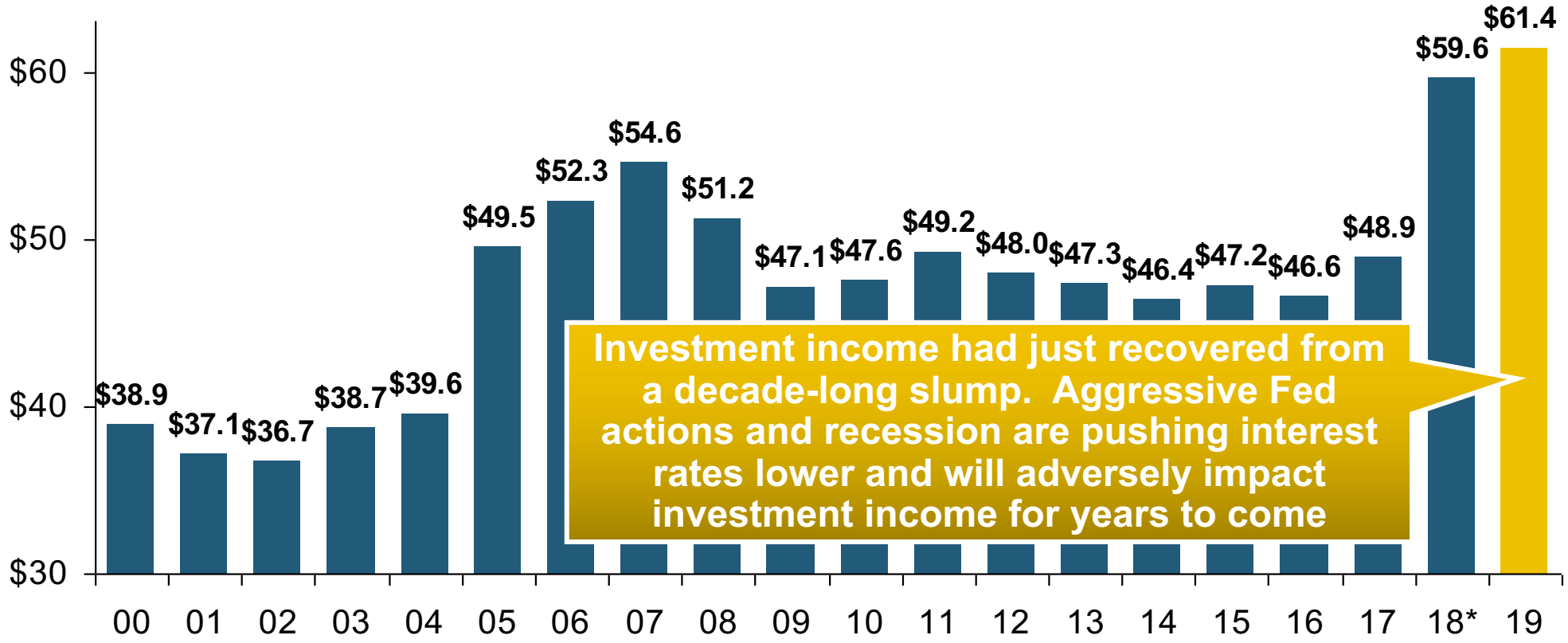
Investment Performance Is a Key Driver of Insurer Profitability

Aggressive Rate Cuts Will Adversely Impact Invest Earnings

Financial Crisis *Déjà Vu*?

Property/Casualty Insurance Industry Investment Income: 2000–2019

($ Billions)

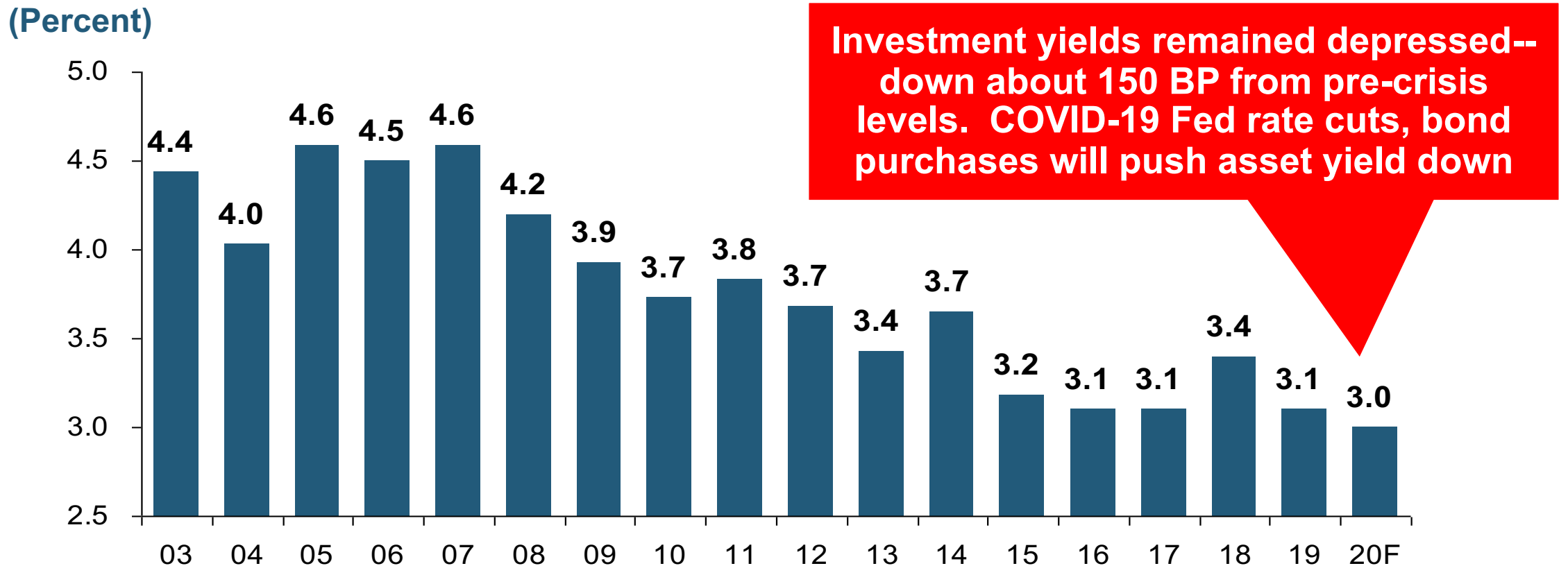


Due to persistently low interest rates, investment income remained below pre-crisis levels for a decade. Lower interest rates post-COVID will drive investment income down once again.

*2018-19 figures are distorted by provisions of the TCJA of 2017. Increase reflects such items as dividends from foreign subsidiaries.

[1] Investment gains consist primarily of interest and stock dividends. Sources: ISO; University of South Carolina, Center for Risk and Uncertainty Management.

Net Investment Yield on Property/Casualty Insurance Invested Assets, 2007–2020F*



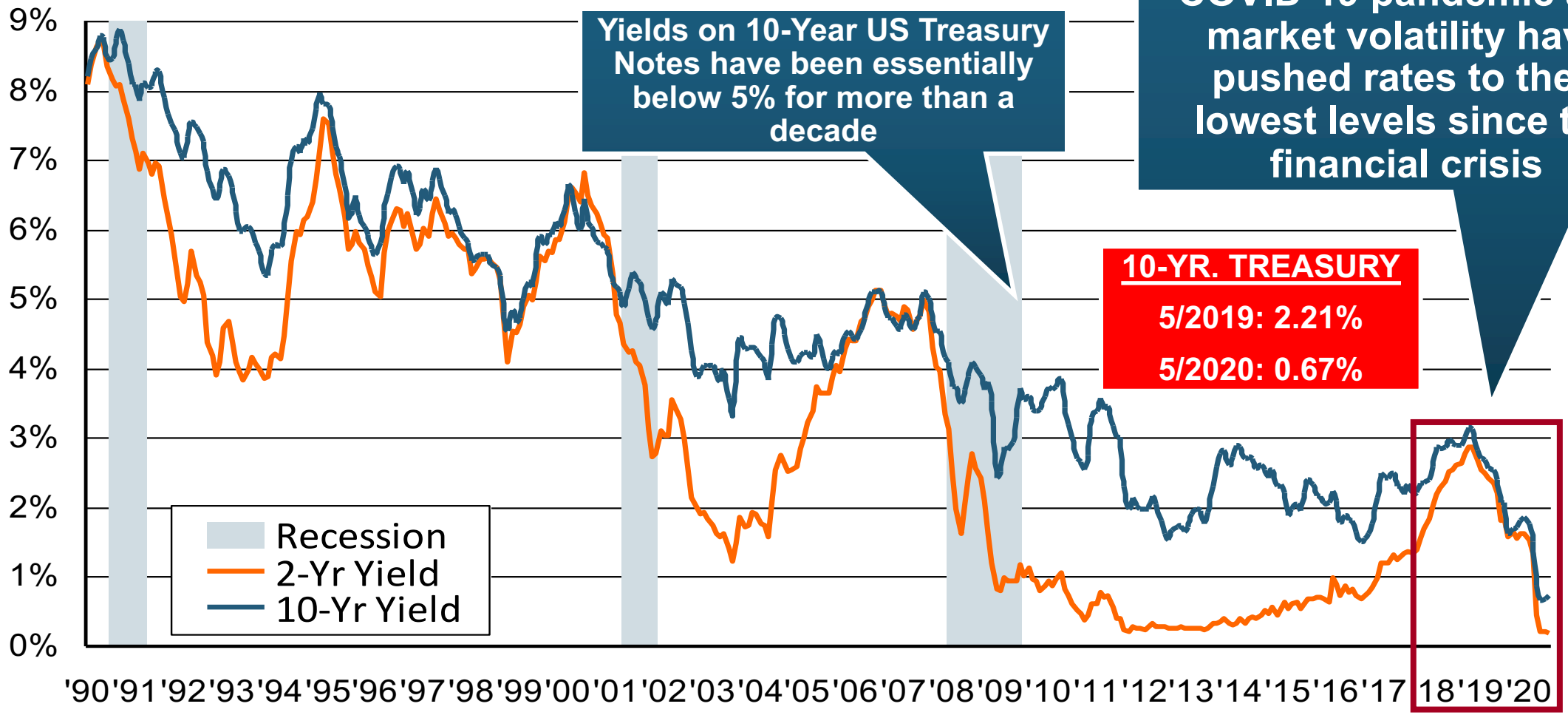
Investment yields remained depressed--down about 150 BP from pre-crisis levels. COVID-19 Fed rate cuts, bond purchases will push asset yield down

The yield on invested assets remains low relative to pre-crisis yields. Fed rate increases beginning in late 2015 through 2018 halted the slide in yields, but rate cuts in 2019/2020 will preclude future gains

Average: 1960-2018 = 5.0%
Low: 2.8% (1961)
High: 8.2% (1984/85)

Sources: NAIC data, sourced from S&P Global Market Intelligence; 2017-19 figures are from ISO. 2020F is from the Risk and Uncertainty Management Center, Univ. of South Carolina.

US Treasury Security Yields: A Long Downward Trend, 1990–2020*

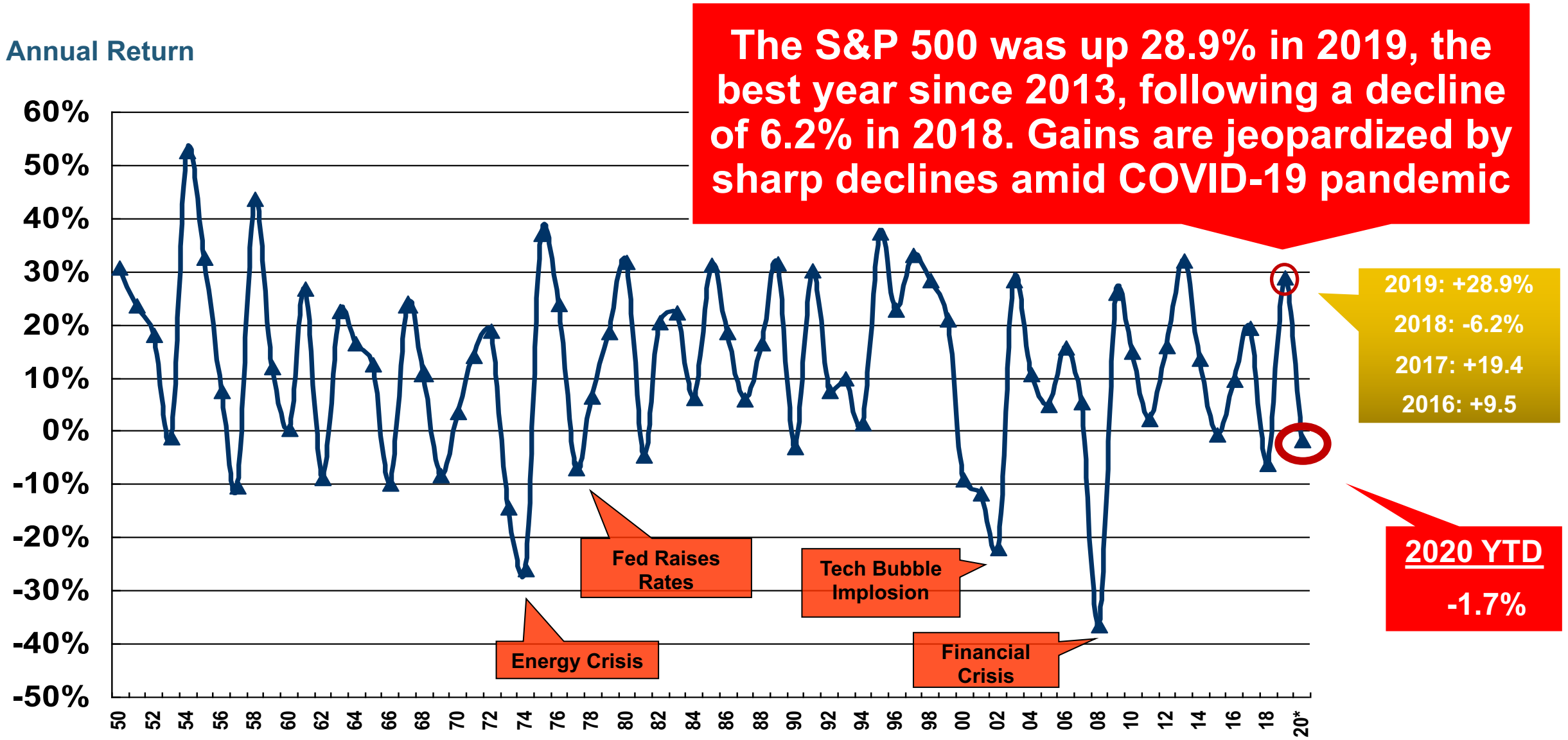


Since roughly 80% of P/C bond/cash investments are in 10-year or shorter durations, most P/C insurer portfolios will have low-yielding bonds for years to come.

*Monthly, constant maturity, nominal rates, through June 2020.

Sources: Federal Reserve Bank at http://www.federalreserve.gov/releases/h15/data.htm. National Bureau of Economic Research (recession dates); Insurance Information Institute.

S&P 500 Index Returns, 1950–2020*



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*Through July 10, 2020.
Source: NYU Stern School of Business: http://pages.stern.nyu.edu/~adamodar/New_Home_Page/datafile/histretSP.html; Center for Risk and Uncertainty Management, University of South Carolina

Financial Markets Have Been *Extremely* Volatile

- **Q2 2020: S&P up 20%, best quarterly gain since 1998; Up 45% since its March 23 trough (2,192 @ close) through July 10**
- **Has the market gotten ahead of itself given the that GDP in Q2 will shrink by 38% (CBO) and unemployment remains in double digits?**
- **March 9: Largest DJIA point drop ever: -2,014 pts. *(-7.79% drop largest % terms since 10/15/08)***

Coronavirus Comeback?

S&P is down just 1.7% for the year and 6.2% from its record high of 3386 on Feb. 19

- **Is market anticipating a "V-shaped" recovery, more stimulus, expedited vaccine…?**

Source: CNBC.com; Center for Risk and Uncertainty Management, University of South Carolina

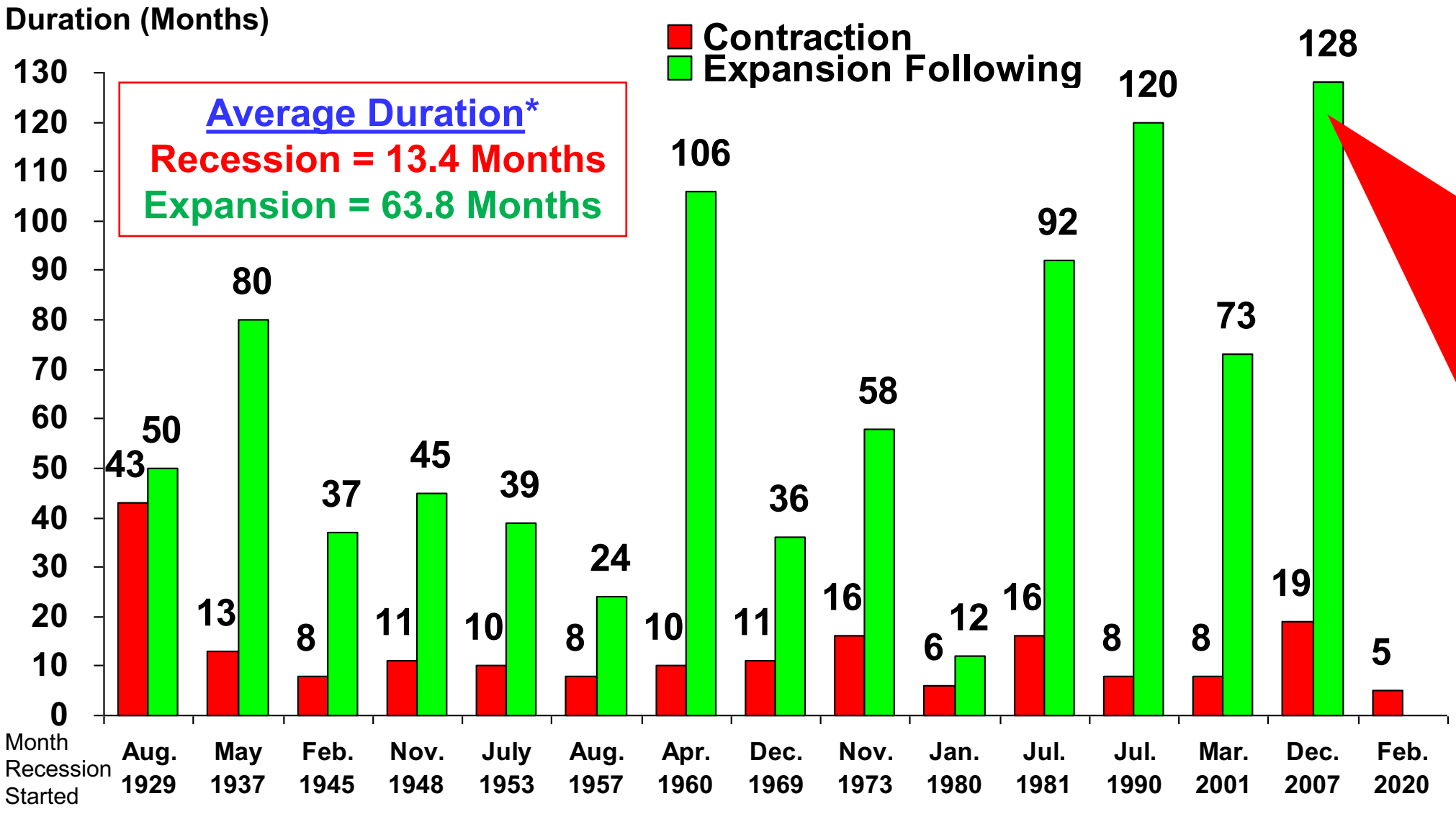
THE ECONOMY

COVID-19 Pandemic Will Directly and Severely Impact Growth As Exposure Growth Rapidly Shrinks

The Strength of the Economy Has Always Influenced Growth in Insurers' Exposure Base Across Most Lines

The Links Between the Economy and the P/C Insurance Industry Are Strengthening

Length of US Business Cycles, 1929-Present*



The most recent economic expansion ended in Feb. 2020 and was the longest in US history (began July 2009)

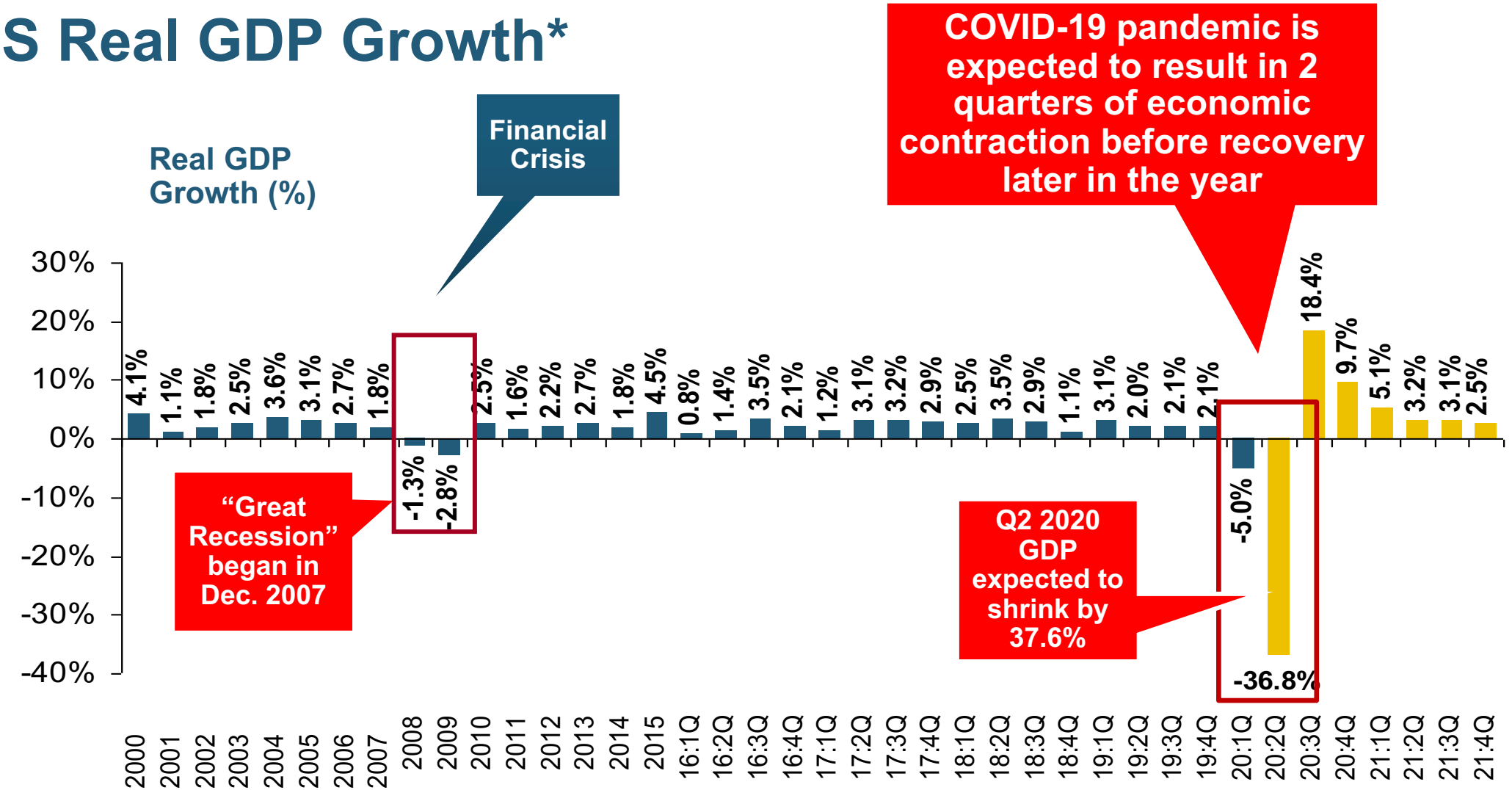
Recession may officially last only 5-8 months

Will likely take 2+ years to recover lost growth

* As of June 2020 but excluding current COVID-19 recession which began in Feb. 2020 and is ongoing.

Sources: National Bureau of Economic Research; Risk and Uncertainty Management Center, University of South Carolina.

US Real GDP Growth*

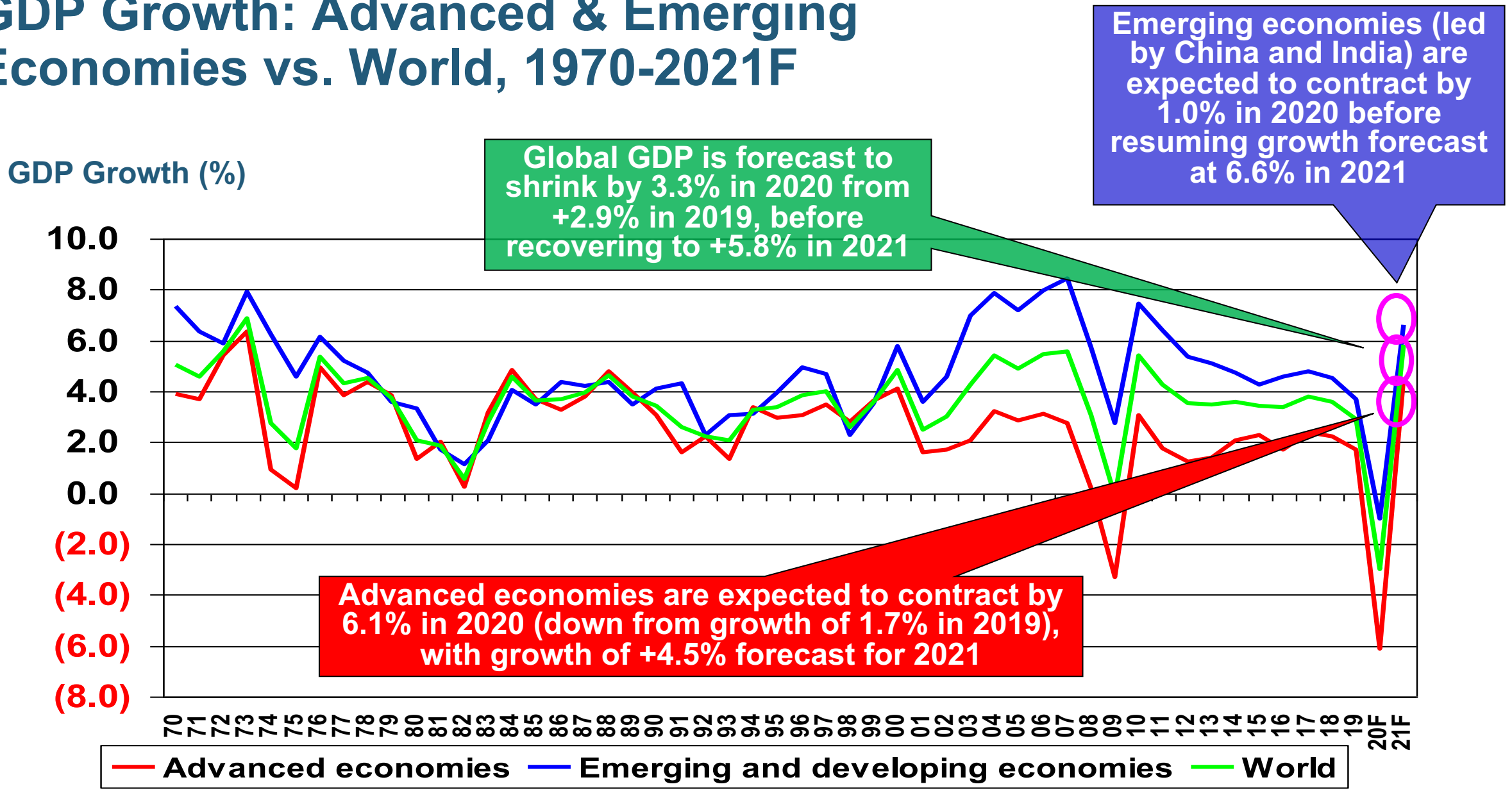


Demand for Insurance Will Be Severely Impacted As the Economy Slows but Should Improve by Late Q3 and into Q4

* Estimates/Forecasts from Wells Fargo Securities.

Source: US Department of Commerce, Wells Fargo Securities 7/20; Center for Risk and Uncertainty Management, University of South Carolina.

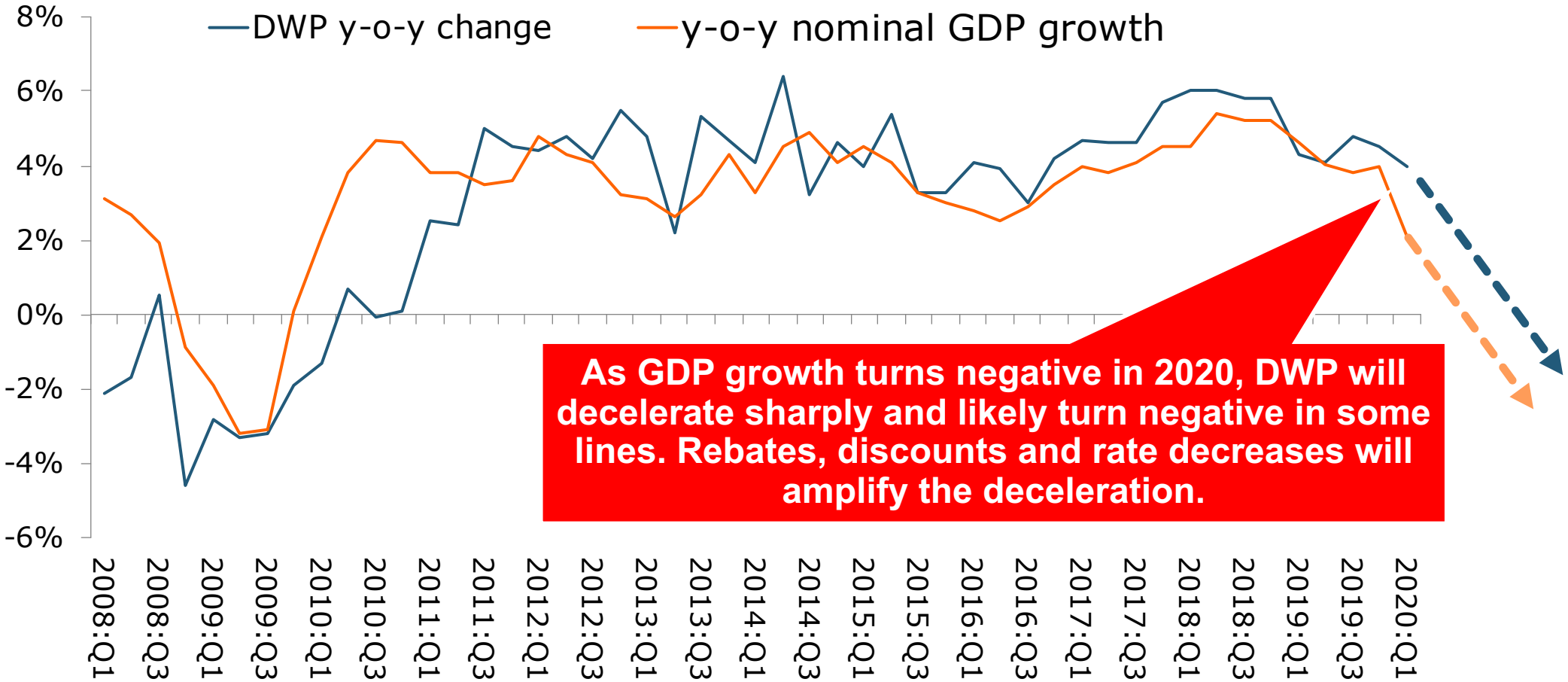
GDP Growth: Advanced & Emerging Economies vs. World, 1970-2021F



Source: International Monetary Fund, *World Economic Outlook*, Apr. 2020;
Univ. of South Carolina, Risk and Uncertainty Management Center.

The Economy Drives P/C Insurance Industry Premiums: 2006:Q1–2020:Q1*

Direct Premium Growth (All P/C Lines) vs. Nominal GDP: Quarterly Y-o-Y Pct. Change

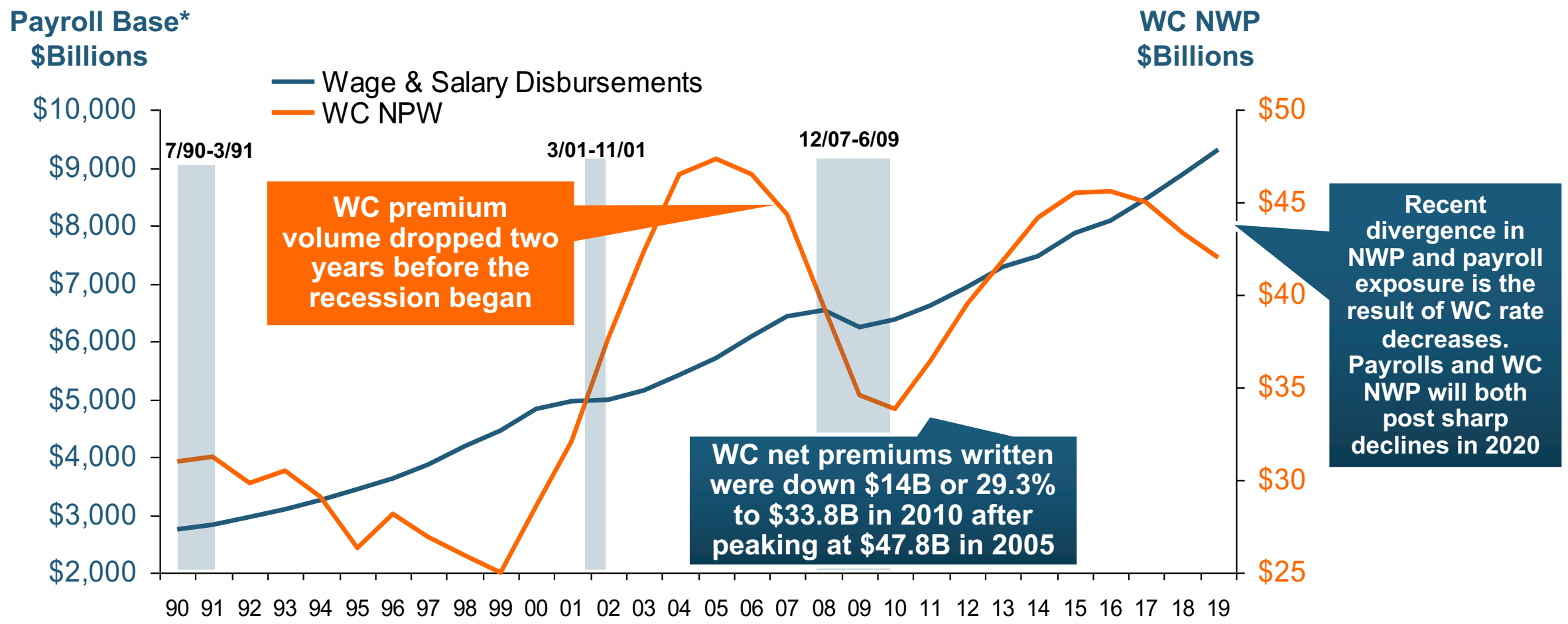


As GDP growth turns negative in 2020, DWP will decelerate sharply and likely turn negative in some lines. Rebates, discounts and rate decreases will amplify the deceleration.

Direct written premiums track nominal GDP fairly tightly over time, suggesting the P/C insurance industry's growth prospects inextricably linked to economic performance.

*2020:Q1 GDP figure is actual. DWP is estimate from Risk and Uncertainty Management Center, University of South Carolina.
Sources: SNL Financial; U.S. Commerce Dept., Bureau of Economic Analysis; ISO; I.I.I.; Risk and Uncertainty Management Center, University of South Carolina.

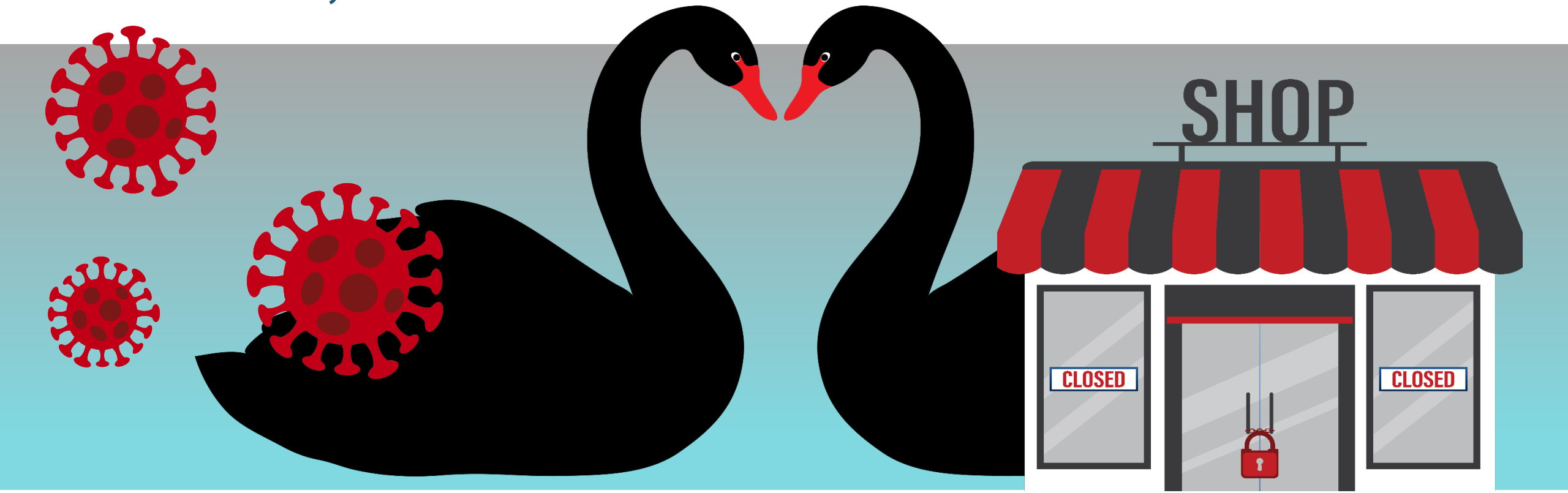
Payroll vs. Workers Comp Net Written Premiums, 1990-2019



Continued payroll growth will benefit WC exposure growth, but falling rates will adversely impact growth in Net Written Premiums

*Private employment; Shaded areas indicate recessions. WC premiums are from NCCI through 2018.
Sources: NBER (recessions); Federal Reserve Bank of St. Louis at http://research.stlouisfed.org/fred2/series/WASCUR.

Government Mandated Business Closures Were the Real Black Swan, Not the Coronavirus



- The US (and world) has endured several other major infectious disease outbreaks killing 100,000+ Americans without shutting down the economy
  - Hong Kong Flu (1968-70)
  - Asian Flu (1957-58)

- It is the reaction to the virus that is unprecedented and represents the *true* Black Swan event
- The ramifications of this decision will be consequential for a generation (e.g., $3 trill. in debt)

Sources: CDC; Risk and Uncertainty Management Center, University of South Carolina

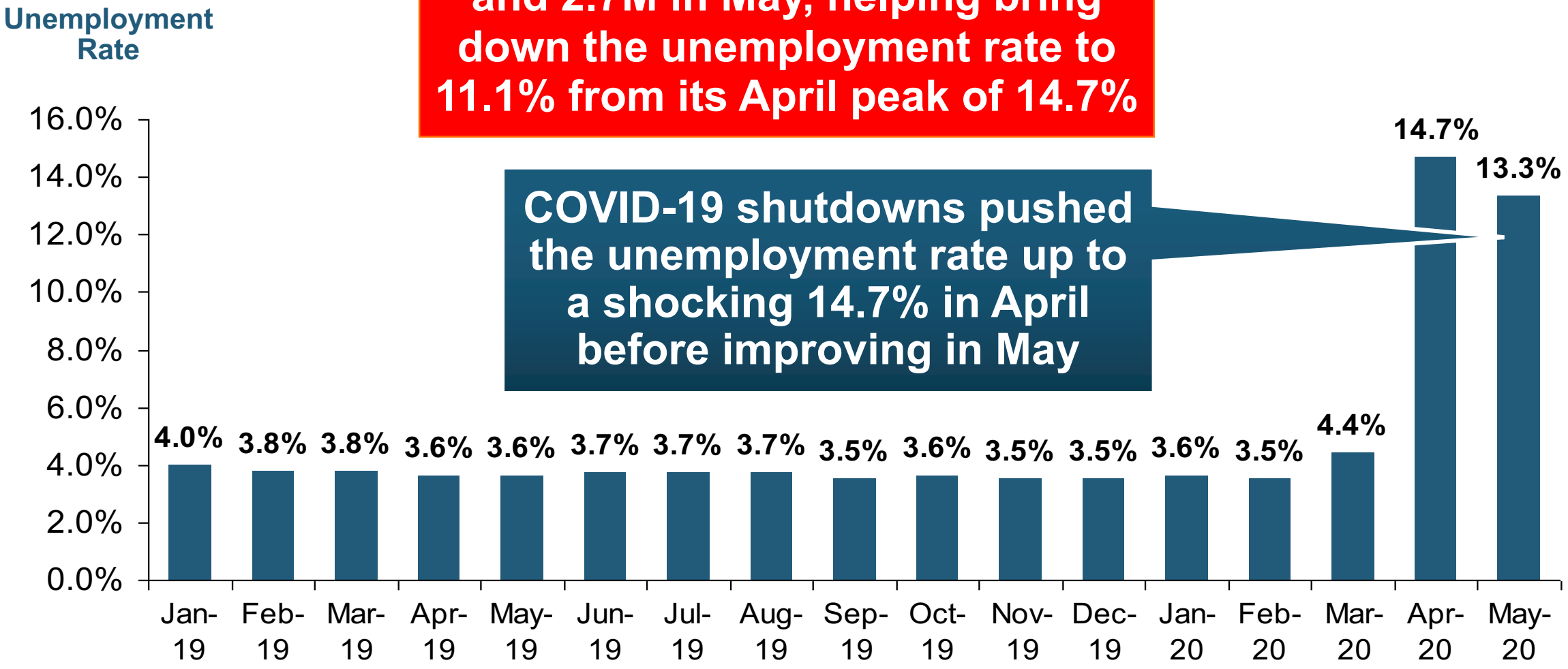
COVID-19 AND IMPACTS ON LABOR MARKETS

COVID-19's Overall Impact on Labor Markets Is the Largest Since the Great Depression

How Long the Scars Last is Dependent on the Pace of Reopening as Well as the Legislative/Regulatory and Tort Environment

Unemployment Rate: Jan. 2019 – June 2020

4.8M jobs were created in June and 2.7M in May, helping bring down the unemployment rate to 11.1% from its April peak of 14.7%



COVID-19 shutdowns pushed the unemployment rate up to a shocking 14.7% in April before improving in May

Source: US Bureau of Labor Statistics; Risk and Uncertainty Management Center, University of South Carolina.

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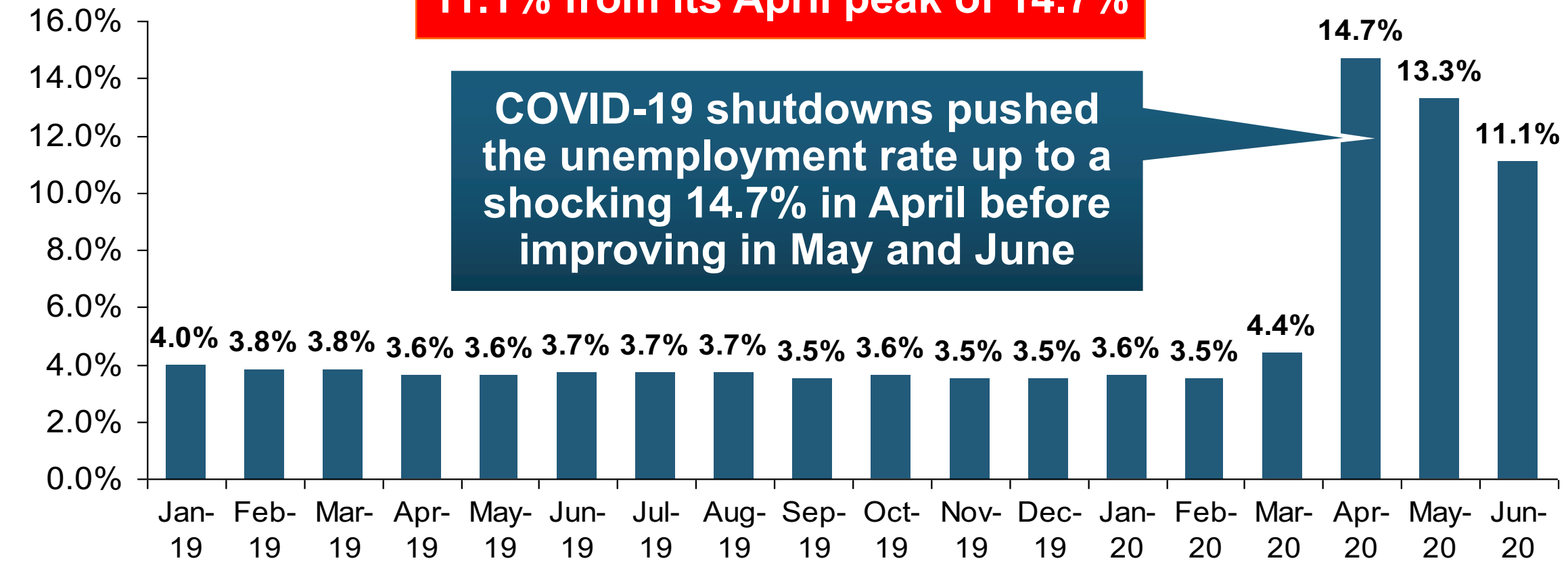
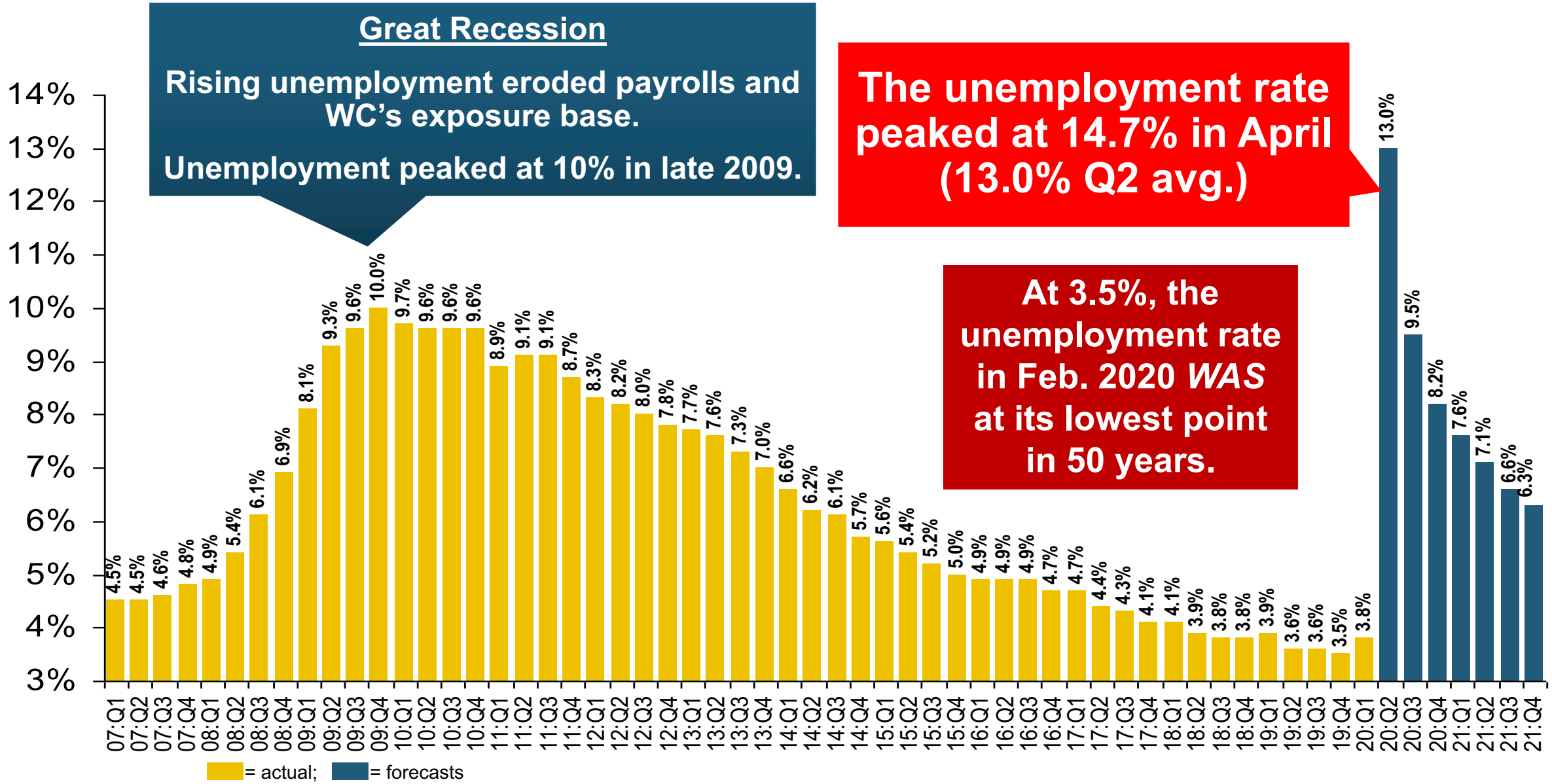


Source: US Bureau of Labor Statistics; Risk and Uncertainty Management Center, University of South Carolina.

US Unemployment Rate Forecast: 2007:Q1–2021:Q4



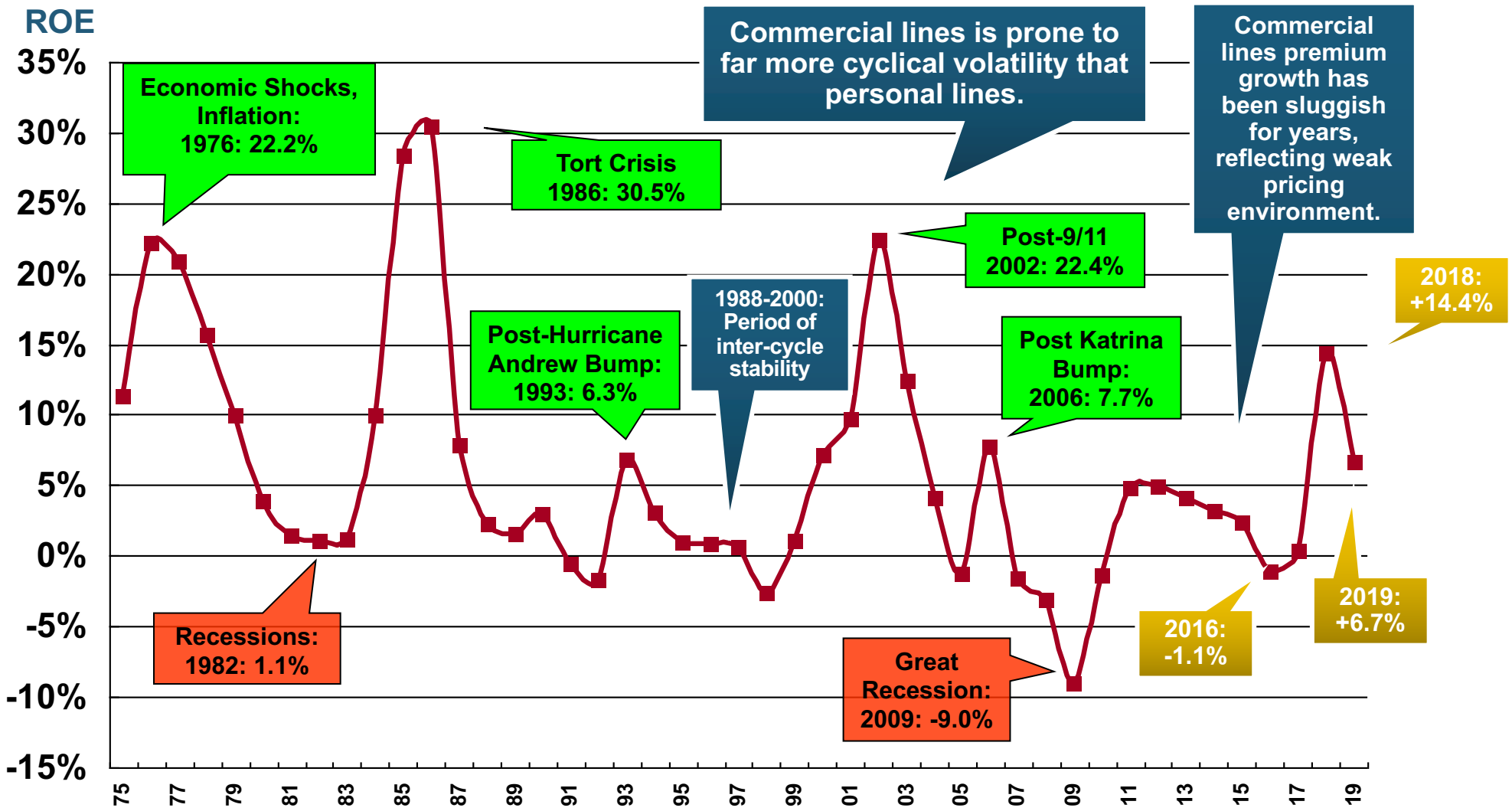
Sources: US Bureau of Labor Statistics; Wells Fargo Securities (7/20 edition); Risk and Uncertainty Management Center, University of South Carolina.

Commercial Lines Growth, Underwriting Performance & Pricing Cyclicality

Pricing Pressures Are Intensifying

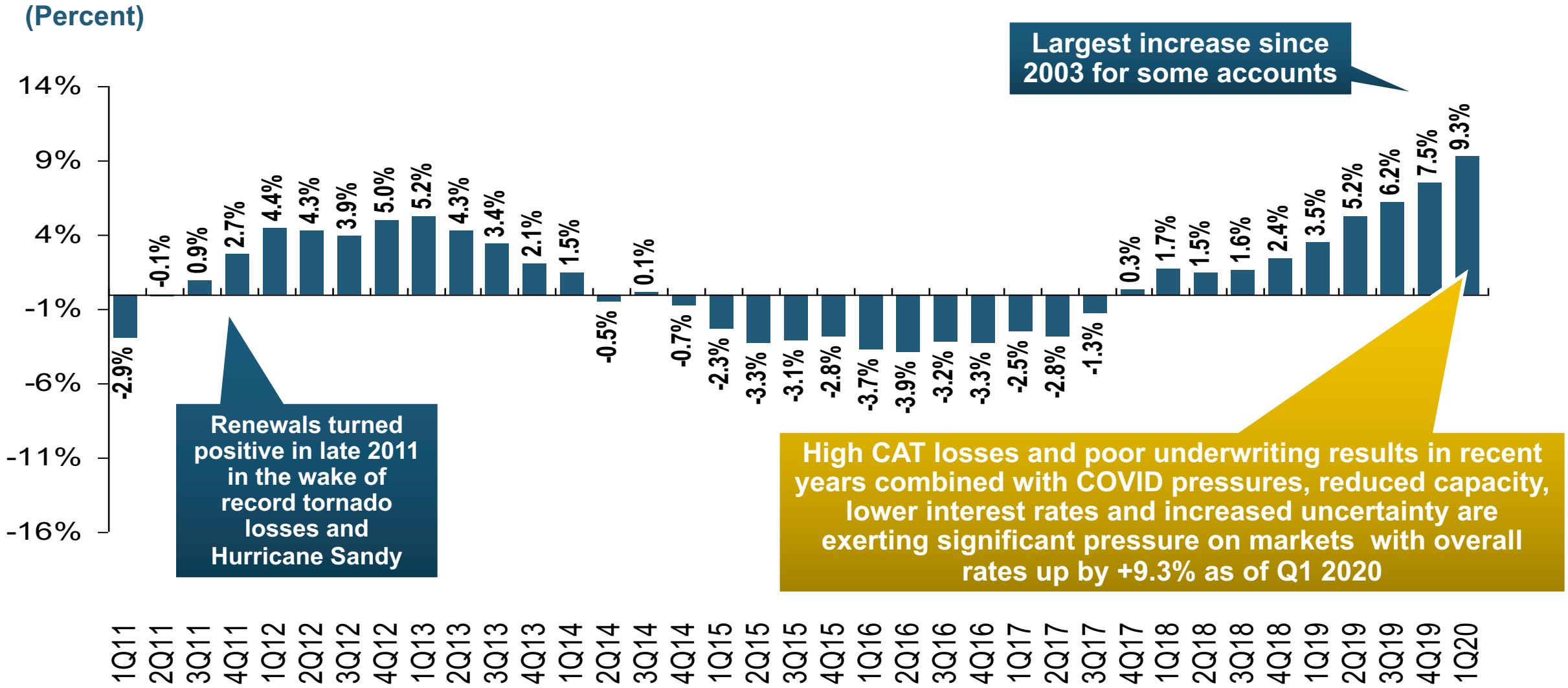
42

Commercial Lines NPW Premium Growth: 1975 – 2019



Note: Data include state funds beginning in 1998.
Source: A.M. Best; Insurance Information Institute; Univ. of South Carolina Center for Risk and Uncertainty Management, ISO.

CIAB: Average Commercial Rate Change, All Lines, 2011:Q1–2020:Q1*

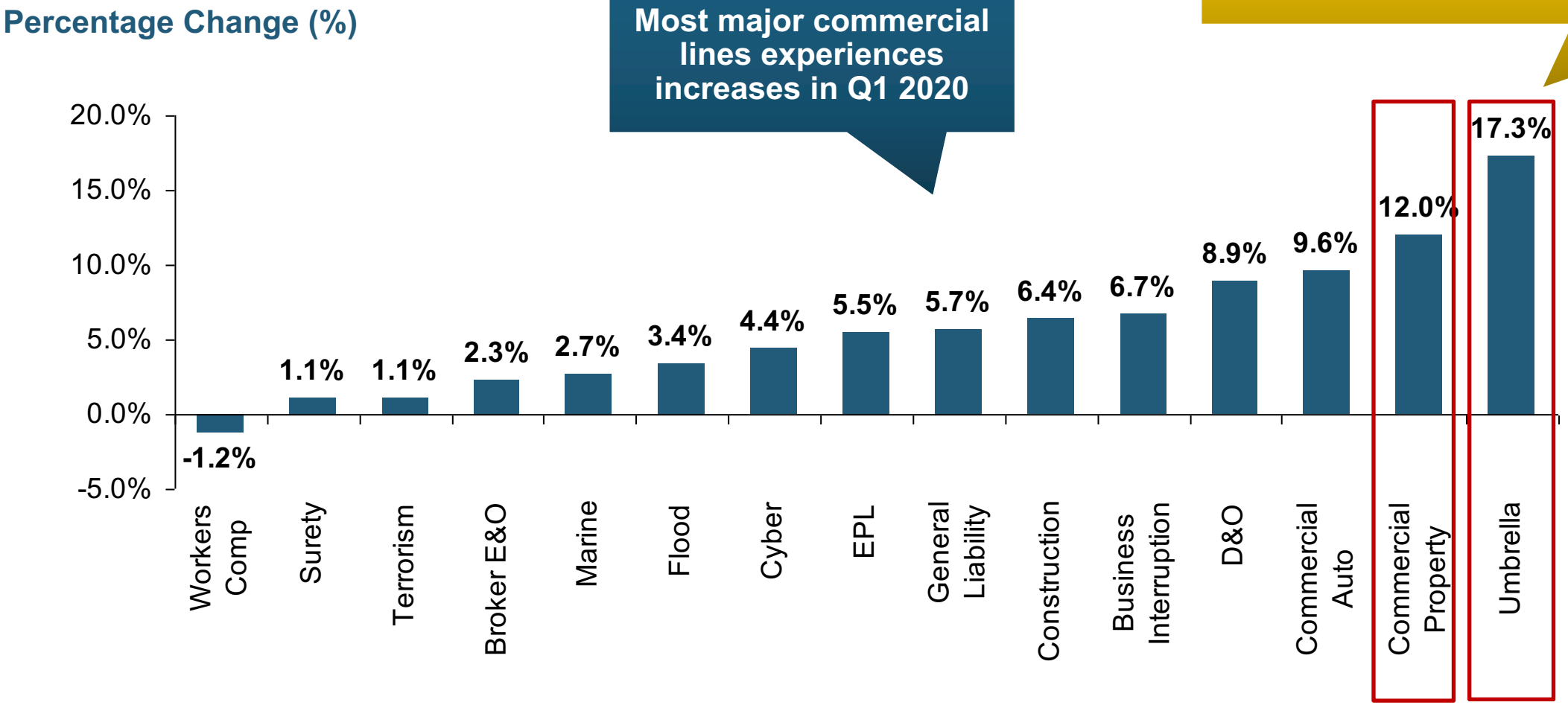


*Latest available.
Note: CIAB data cited here are based on a survey. Rate changes earned by individual insurers can and do vary, potentially substantially.
Source: Council of Insurance Agents & Brokers; Center for Risk and Uncertainty Management, Univ. of South Carolina.

Change in Commercial Rate Renewals, by Line: 2020:Q1

Umbrella now leads all major commercial lines in terms of rate gains, exceeding Commercial Auto and CP

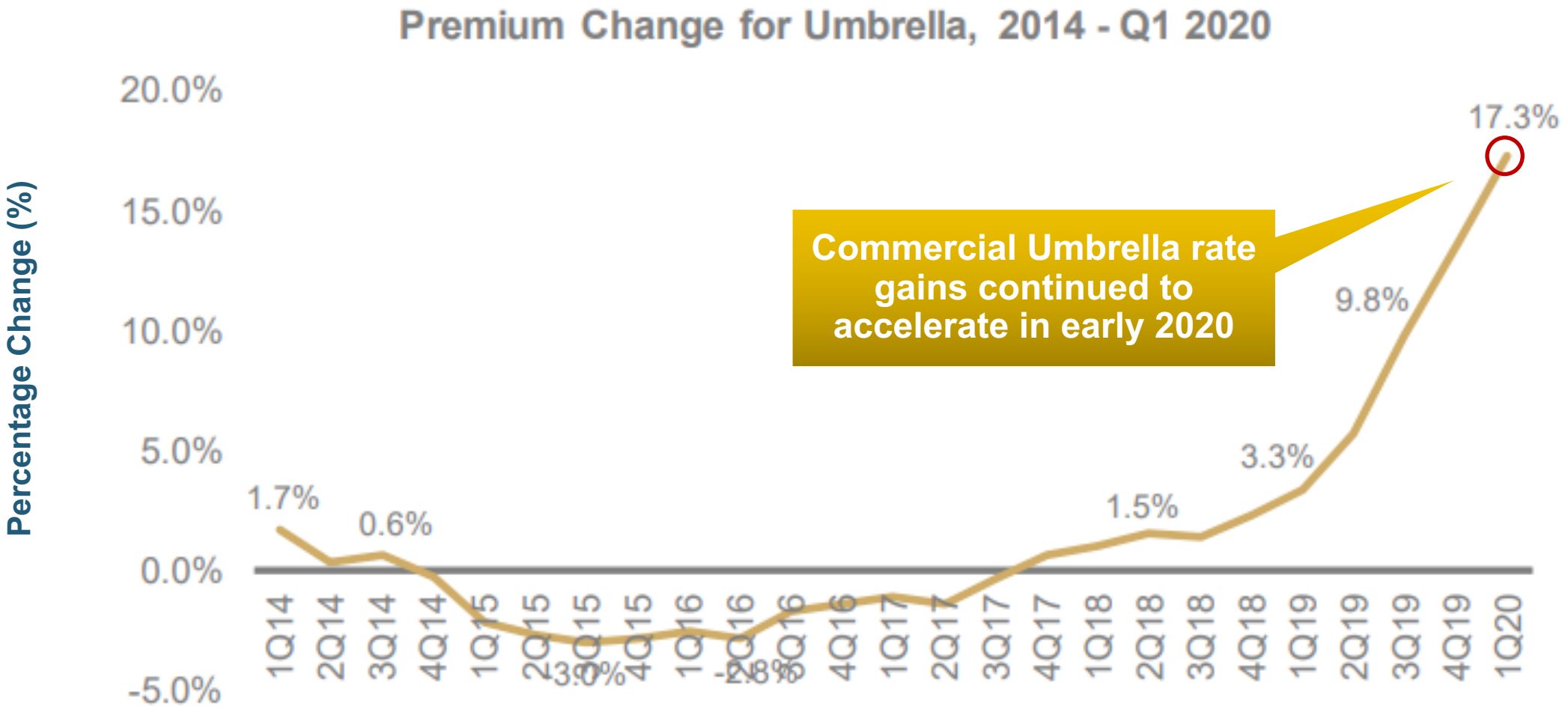
Most major commercial lines experiences increases in Q1 2020



Note: CIAB data cited here are based on a survey. Rate changes earned by individual insurers can and do vary, potentially substantially.

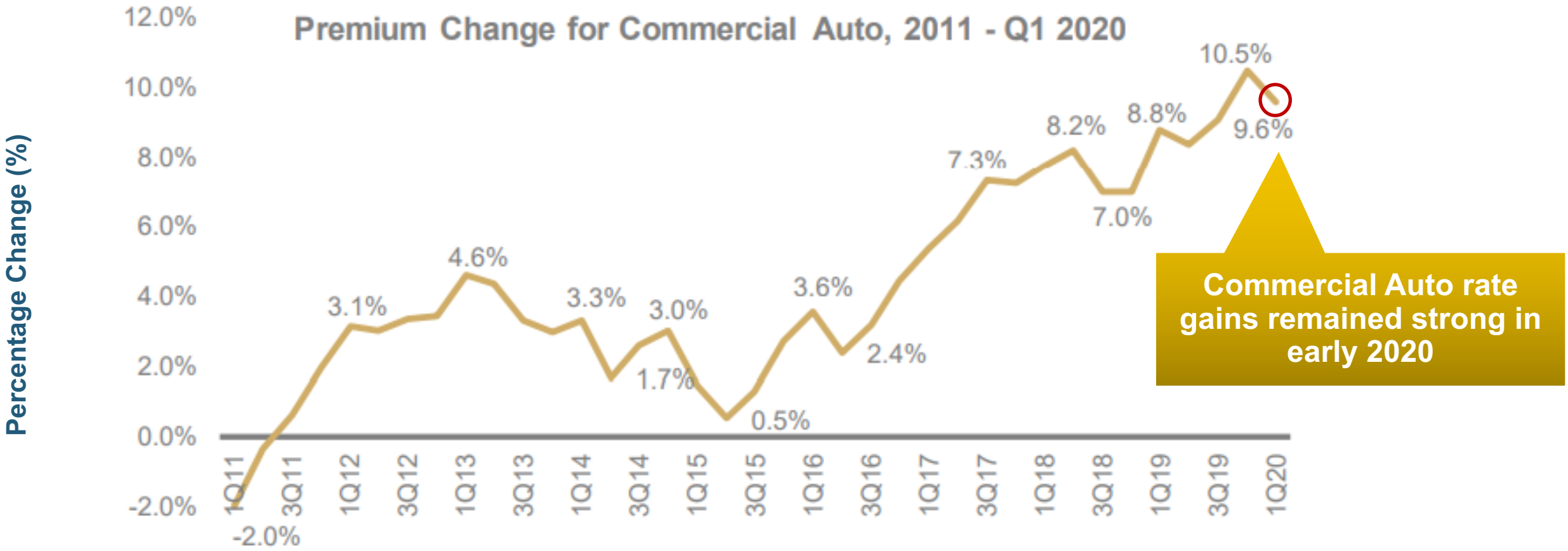
Source: Council of Insurance Agents and Brokers; USC Center for Risk and Uncertainty Management.

Change in Commercial Umbrella Renewals: 2011:Q1 to 2020:Q1



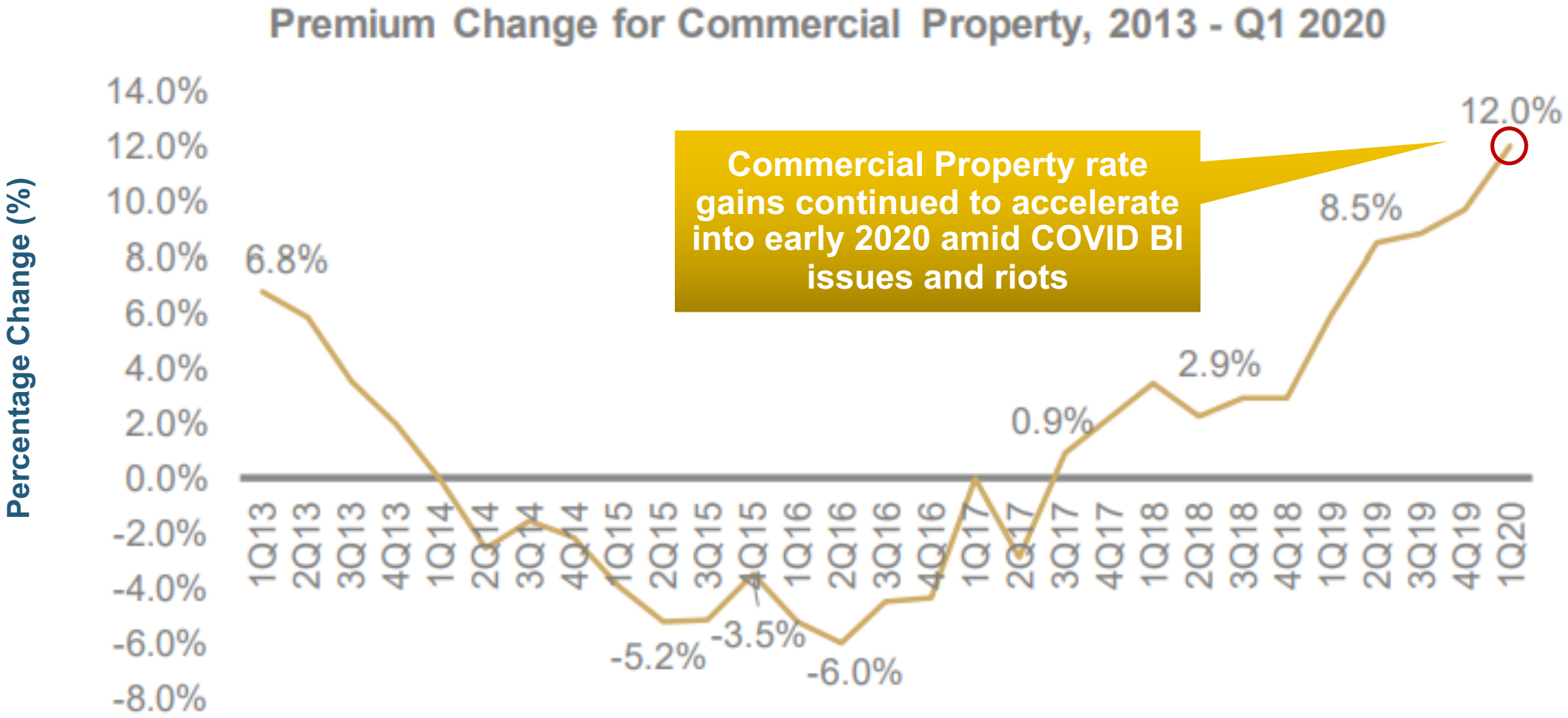
Note: CIAB data cited here are based on a survey. Rate changes earned by individual insurers can and do vary, potentially substantially.
Source: Council of Insurance Agents and Brokers.

Change in Commercial Auto Rate Renewals: 2011:Q1 to 2020:Q1



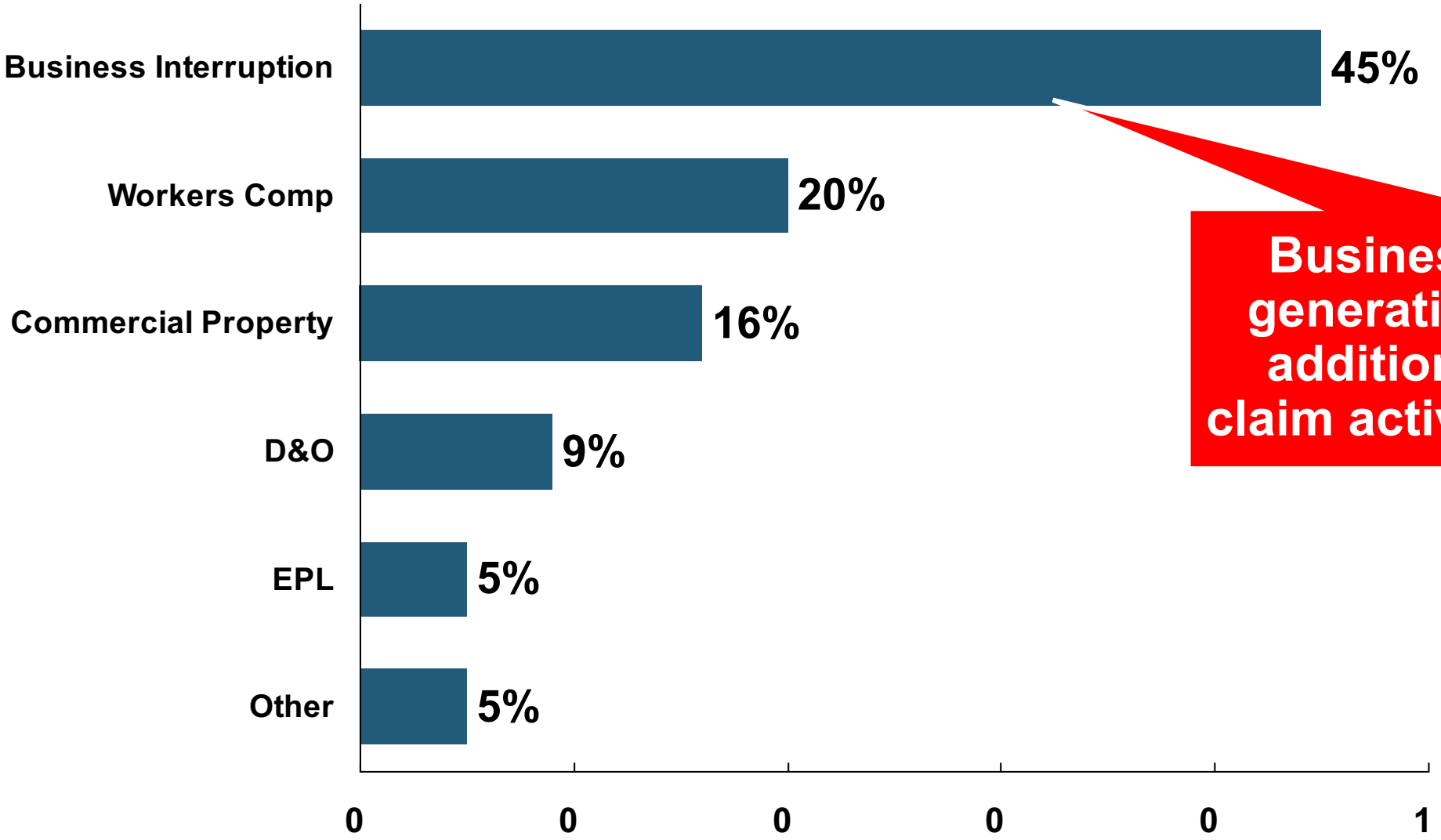
Note: CIAB data cited here are based on a survey. Rate changes earned by individual insurers can and do vary, potentially substantially.
Source: Council of Insurance Agents and Brokers.

Change in Commercial Property Rate Renewals: 2011:Q1 to 2020:Q1



Note: CIAB data cited here are based on a survey. Rate changes earned by individual insurers can and do vary, potentially substantially.
Source: Council of Insurance Agents and Brokers.

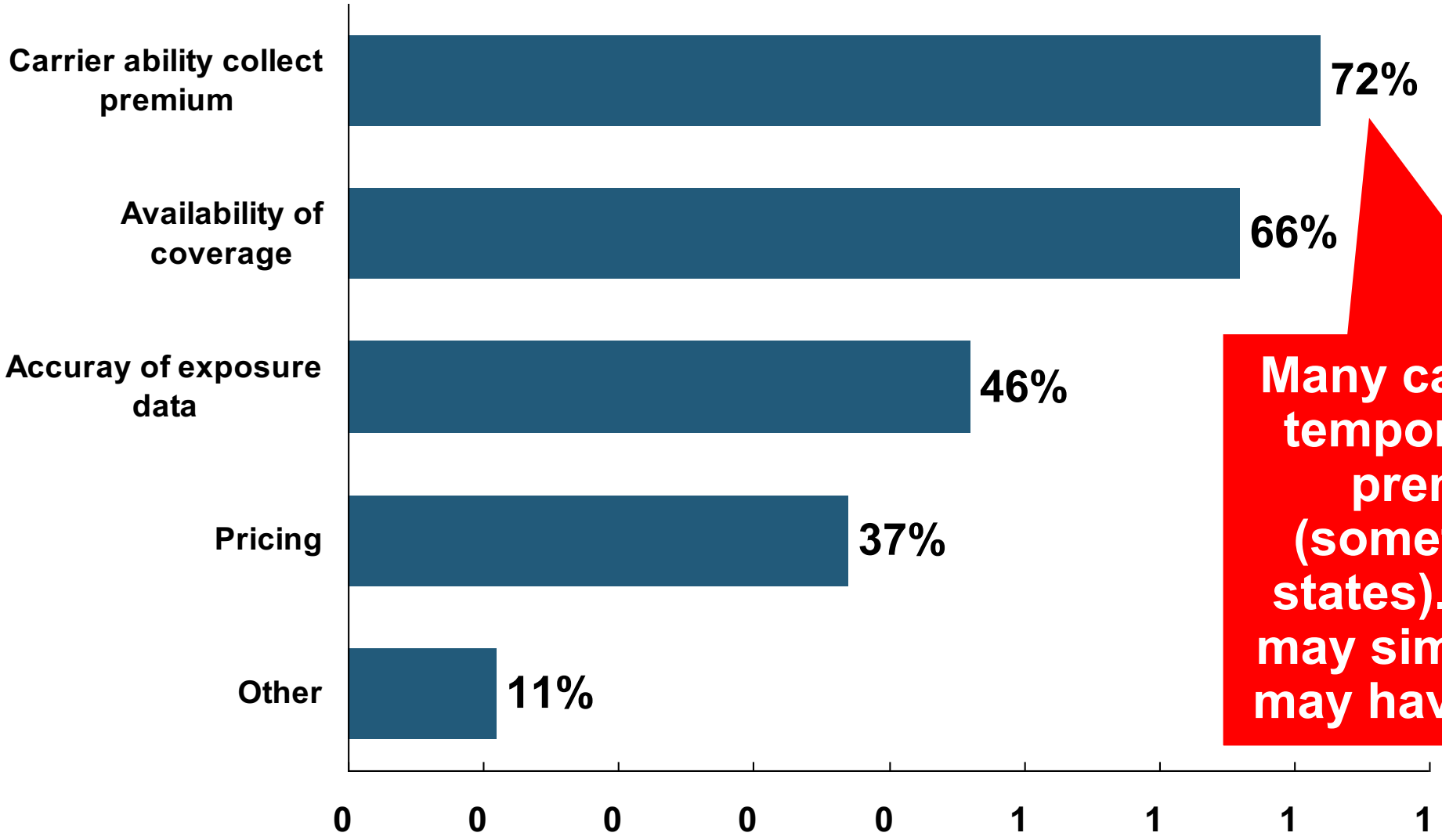
Respondents Reporting Increased COVID-Related Claims Activity for Commercial Lines: 2020:Q1*



Business Interruption is generating by far the most additional COVID-related claim activity, followed by WC

*Survey period was from April to May 1, hence Q1 responses were likely influenced by experience after Q1.
Source: Council of Insurance Agents and Brokers, *COVID-19 Supplement.*

Insurer/Broker Activities Affected by COVID: 2020:Q*
(% respondents indicating impact observed)



Many carriers have afforded temporary forbearance on premium collections (sometimes mandated by states). In other case, risks may simply not be paying or may have ceased operations

*Survey period was from April to May 1, hence Q1 responses were likely influenced by experience after Q1.
Source: Council of Insurance Agents and Brokers, *COVID-19 Supplement.*

P/C Insurance Issues in the Era of COVID-19

Business Interruption

Workers Compensation

P/C Insurance Coverage & COVID-19

- **Insurers have received tens of thousands of claims related to COVID-19 losses**
  - **Workers comp**
  - **Business Interruption**
  - **GL**
  - **Event Cancellation**
  - **Travel Insurance**
  - **D&O**
  - **Trade Credit**
  - **Mortgage**
  - **EPL**
- **Crises tend to precipitate efforts to stretch contract language in an effort to:**
  - **Find coverage where none exists**
  - **Find coverage where none was intended**
  - **Find coverage for which no premium was paid**
- **Politicians frequently pile on: Zero political risk**

Business Interruption

Efforts to Create Coverage Where None Exists

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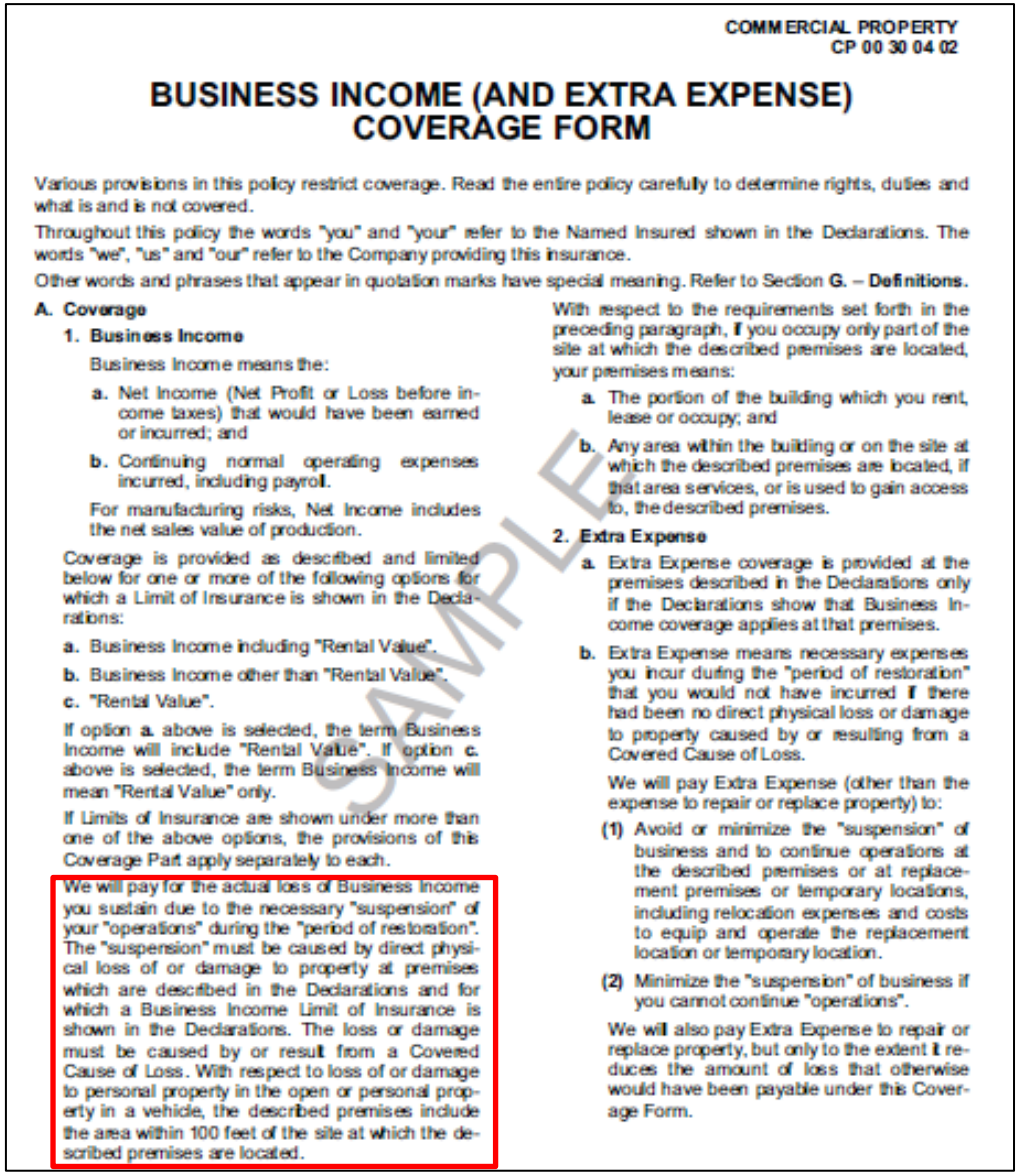
Business Interruption Coverage (BIC) & COVID-19

- **Business interruption policies clearly exclude COVID-19 claims**

- **The ISO Business Income form contains the following language:**

  - ***"We will pay for the actual loss of Business Income you sustain due to the necessary "suspension" of your "operations" during the "period of restoration". The "suspension" must be caused by direct physical loss of or damage to property…The loss or damage must be caused by or the result of a covered cause of loss." [from ISO form: CP 00 30 04 02]***



COMMERCIAL PROPERTY
CP 00 30 04 02

BUSINESS INCOME (AND EXTRA EXPENSE) COVERAGE FORM

Various provisions in this policy restrict coverage. Read the entire policy carefully to determine rights, duties and what is and is not covered.

Throughout this policy the words "you" and "your" refer to the Named Insured shown in the Declarations. The words "we", "us" and "our" refer to the Company providing this insurance.

Other words and phrases that appear in quotation marks have special meaning. Refer to Section **G. – Definitions.**

A. Coverage

1. Business Income

Business Income means the:

a. Net Income (Net Profit or Loss before income taxes) that would have been earned or incurred; and

b. Continuing normal operating expenses incurred, including payroll.

For manufacturing risks, Net Income includes the net sales value of production.

Coverage is provided as described and limited below for one or more of the following options for which a Limit of Insurance is shown in the Declarations:

a. Business Income including "Rental Value".

b. Business Income other than "Rental Value".

c. "Rental Value".

If option **a.** above is selected, the term Business Income will include "Rental Value". If option **c.** above is selected, the term Business Income will mean "Rental Value" only.

If Limits of Insurance are shown under more than one of the above options, the provisions of this Coverage Part apply separately to each.

We will pay for the actual loss of Business Income you sustain due to the necessary "suspension" of your "operations" during the "period of restoration". The "suspension" must be caused by direct physical loss of or damage to property at premises which are described in the Declarations and for which a Business Income Limit of Insurance is shown in the Declarations. The loss or damage must be caused by or result from a Covered Cause of Loss. With respect to loss of or damage to personal property in the open or personal property in a vehicle, the described premises include the area within 100 feet of the site at which the described premises are located.

With respect to the requirements set forth in the preceding paragraph, if you occupy only part of the site at which the described premises are located, your premises means:

a. The portion of the building which you rent, lease or occupy; and

b. Any area within the building or on the site at which the described premises are located, if that area services, or is used to gain access to, the described premises.

2. Extra Expense

a. Extra Expense coverage is provided at the premises described in the Declarations only if the Declarations show that Business Income coverage applies at that premises.

b. Extra Expense means necessary expenses you incur during the "period of restoration" that you would not have incurred if there had been no direct physical loss or damage to property caused by or resulting from a Covered Cause of Loss.

We will pay Extra Expense (other than the expense to repair or replace property) to:

(1) Avoid or minimize the "suspension" of business and to continue operations at the described premises or at replacement premises or temporary locations, including relocation expenses and costs to equip and operate the replacement location or temporary location.

(2) Minimize the "suspension" of business if you cannot continue "operations".

We will also pay Extra Expense to repair or replace property, but only to the extent it reduces the amount of loss that otherwise would have been payable under this Coverage Form.

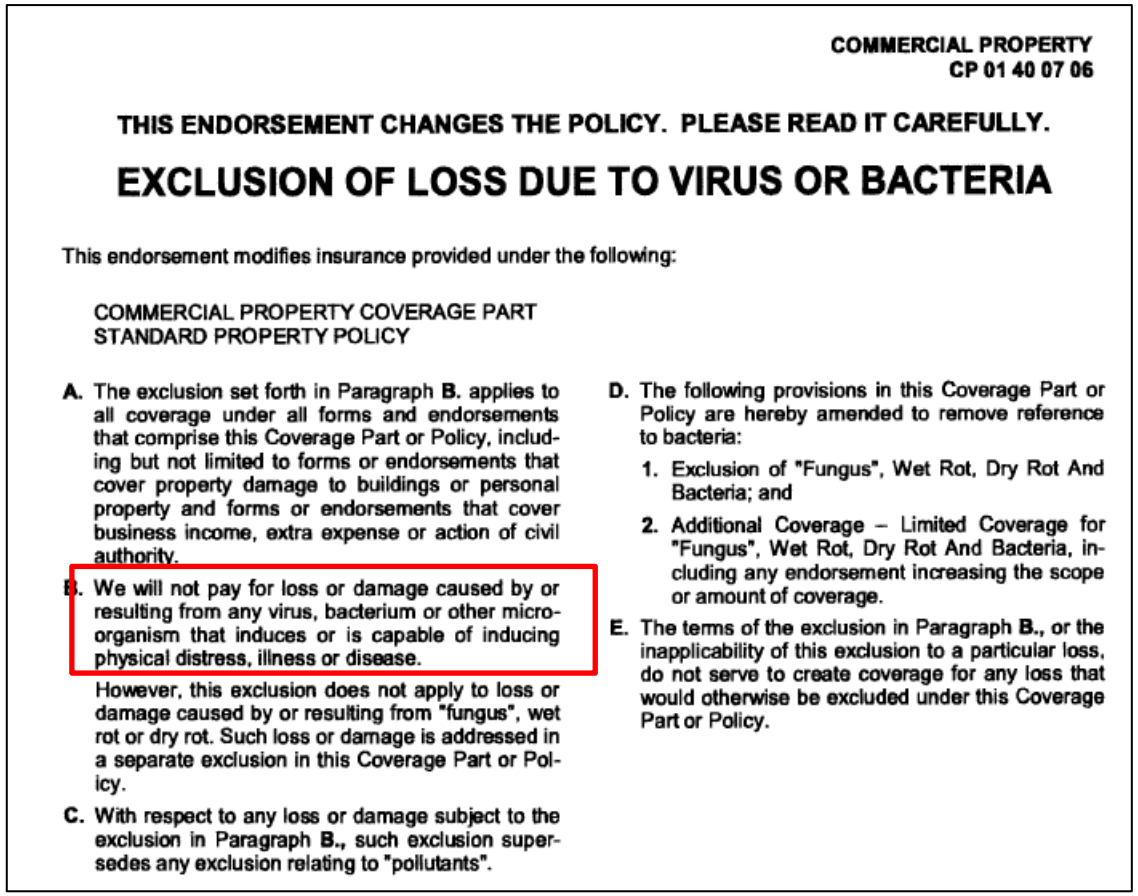
SAMPLE

Exclusion of Loss Due to Virus or Bacteria

- **Business property and hence business interruption coverage also clearly excludes loss or damage due to viruses via exclusion**

- **The ISO "Exclusion of Loss Due to Virus or Bacteria" contains the following language:**

  - ***"We will not pay for loss or damage caused by or resulting from any virus, bacterium or other microorganism that induces or is capable of inducing physical distress, illness or disease."*** *[from ISO form: CP 01 40 07 06]*



COMMERCIAL PROPERTY
CP 01 40 07 06

THIS ENDORSEMENT CHANGES THE POLICY. PLEASE READ IT CAREFULLY.

EXCLUSION OF LOSS DUE TO VIRUS OR BACTERIA

This endorsement modifies insurance provided under the following:

COMMERCIAL PROPERTY COVERAGE PART
STANDARD PROPERTY POLICY

A. The exclusion set forth in Paragraph **B.** applies to all coverage under all forms and endorsements that comprise this Coverage Part or Policy, including but not limited to forms or endorsements that cover property damage to buildings or personal property and forms or endorsements that cover business income, extra expense or action of civil authority.

B. We will not pay for loss or damage caused by or resulting from any virus, bacterium or other microorganism that induces or is capable of inducing physical distress, illness or disease.

However, this exclusion does not apply to loss or damage caused by or resulting from "fungus", wet rot or dry rot. Such loss or damage is addressed in a separate exclusion in this Coverage Part or Policy.

C. With respect to any loss or damage subject to the exclusion in Paragraph **B.**, such exclusion supersedes any exclusion relating to "pollutants".

D. The following provisions in this Coverage Part or Policy are hereby amended to remove reference to bacteria:

1. Exclusion of "Fungus", Wet Rot, Dry Rot And Bacteria; and
2. Additional Coverage – Limited Coverage for "Fungus", Wet Rot, Dry Rot And Bacteria, including any endorsement increasing the scope or amount of coverage.

E. The terms of the exclusion in Paragraph **B.**, or the inapplicability of this exclusion to a particular loss, do not serve to create coverage for any loss that would otherwise be excluded under this Coverage Part or Policy.

Business Interruption Coverage & COVID-19: STATES

- **Several states have attempted to override/invalidate/abrogate the longstanding, unambiguous language in commercial property and BIC contracts that makes it clear no coverage exists**

- **At least 7 states: NJ, OH, LA, MA, PA, NY and SC plus DC have introduced legislation that would oblige insurers to provide BIC to policyholders who purchased such coverage, irrespective of the "direct physical loss or damage" requirement and virus exclusion.**

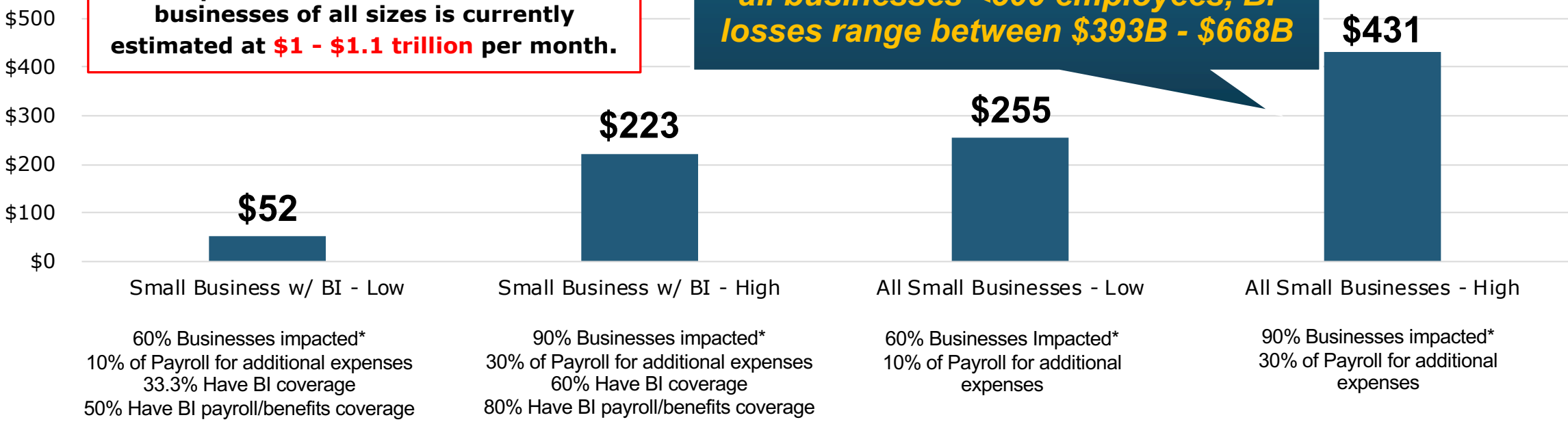
- **From Massachusetts S. 2888 (as of 3/25/20)**

  - *"…**no insurer in [Massachusetts] may deny a claim** for the loss of use and occupancy and business interruption on **account of (i) COVID-19 being a virus** (even if the relevant insurance policy excludes losses resulting from viruses); **or (ii) there being no physical damage to the property** of the insured or to any other relevant property*

Estimated Monthly U.S. Business Interruption Coronavirus Losses for Small Business—Potential Range (<100 Employees; $Bill)

The potential for such losses for all businesses of all sizes is currently estimated at $1 - $1.1 trillion per month.

Monthly BI losses for small business vary widely depending on underlying assumptions but expansive legislation would result in higher estimates; *For all businesses <500 employees, BI losses range between $393B - $668B*



60% Businesses impacted*
10% of Payroll for additional expenses
33.3% Have BI coverage
50% Have BI payroll/benefits coverage

90% Businesses impacted*
30% of Payroll for additional expenses
60% Have BI coverage
80% Have BI payroll/benefits coverage

60% Businesses Impacted*
10% of Payroll for additional expenses

90% Businesses impacted*
30% of Payroll for additional expenses

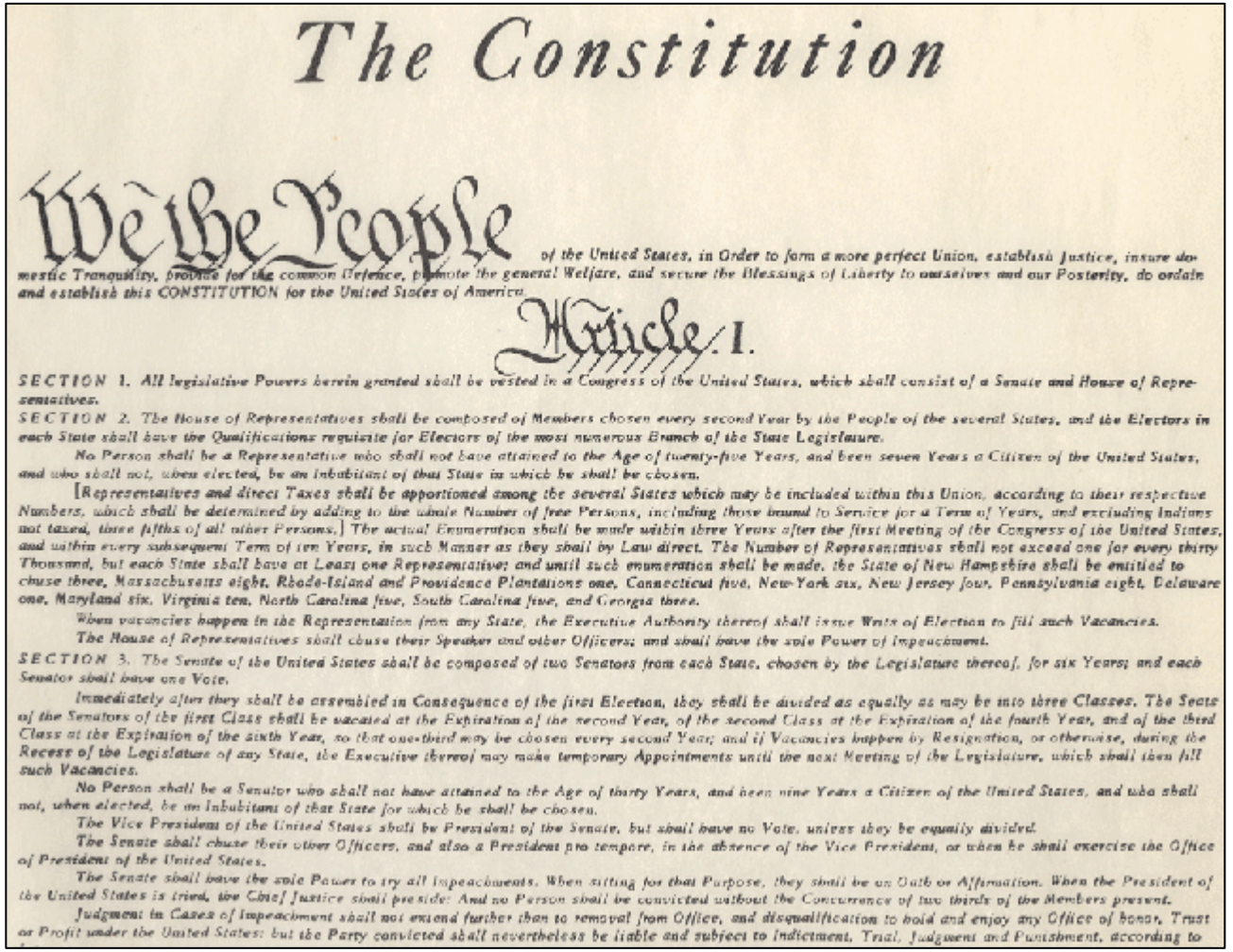
* Businesses impacted: Proportion of businesses completely or substantially closed related to coronavirus
Assumptions: Losses if standard insurance policy exclusions for viruses/pandemics are voided and physical loss/damage requirement is stricken; three main coverages - profit lost, payroll/benefits, additional expenses; average annual $2m revenue and 7% profit margin; non-wage benefits of small businesses are 25% less than that for average US businesses

Source: APCIA, April 2020.

Legislation in several states would trample over contracts and destroy the state's insurance markets

States to Insurers: We're Fine with the Obliteration of the Obligations of Contracts Clause

- State actions to override and ignore legal, longstanding and regulator approved contract language is a clear violation of the Constitution
- The **Obligation of Contracts Clause** (aka "Contracts Clause") is found in **Article I** of the **United States Constitution**
- Generally speaking, this clause was added to the Constitution in order to *prohibit states from interfering with private contracts.*



The Constitution

We the People of the United States, in Order to form a more perfect Union, establish Justice, insure domestic Tranquility, provide for the common Defence, promote the general Welfare, and secure the Blessings of Liberty to ourselves and our Posterity, do ordain and establish this CONSTITUTION for the United States of America.

Article. I.

SECTION 1. All legislative Powers herein granted shall be vested in a Congress of the United States, which shall consist of a Senate and House of Representatives.

SECTION 2. The House of Representatives shall be composed of Members chosen every second Year by the People of the several States, and the Electors in each State shall have the Qualifications requisite for Electors of the most numerous Branch of the State Legislature.

No Person shall be a Representative who shall not have attained to the Age of twenty-five Years, and been seven Years a Citizen of the United States, and who shall not, when elected, be an Inhabitant of that State in which he shall be chosen.

[Representatives and direct Taxes shall be apportioned among the several States which may be included within this Union, according to their respective Numbers, which shall be determined by adding to the whole Number of free Persons, including those bound to Service for a Term of Years, and excluding Indians not taxed, three fifths of all other Persons.] The actual Enumeration shall be made within three Years after the first Meeting of the Congress of the United States, and within every subsequent Term of ten Years, in such Manner as they shall by Law direct. The Number of Representatives shall not exceed one for every thirty Thousand, but each State shall have at Least one Representative; and until such enumeration shall be made, the State of New Hampshire shall be entitled to chuse three, Massachusetts eight, Rhode-Island and Providence Plantations one, Connecticut five, New-York six, New Jersey four, Pennsylvania eight, Delaware one, Maryland six, Virginia ten, North Carolina five, South Carolina five, and Georgia three.

When vacancies happen in the Representation from any State, the Executive Authority thereof shall issue Writs of Election to fill such Vacancies.

The House of Representatives shall chuse their Speaker and other Officers; and shall have the sole Power of Impeachment.

SECTION 3. The Senate of the United States shall be composed of two Senators from each State, chosen by the Legislature thereof, for six Years; and each Senator shall have one Vote.

Immediately after they shall be assembled in Consequence of the first Election, they shall be divided as equally as may be into three Classes. The Seats of the Senators of the first Class shall be vacated at the Expiration of the second Year, of the second Class at the Expiration of the fourth Year, and of the third Class at the Expiration of the sixth Year, so that one-third may be chosen every second Year; and if Vacancies happen by Resignation, or otherwise, during the Recess of the Legislature of any State, the Executive thereof may make temporary Appointments until the next Meeting of the Legislature, which shall then fill such Vacancies.

No Person shall be a Senator who shall not have attained to the Age of thirty Years, and been nine Years a Citizen of the United States, and who shall not, when elected, be an Inhabitant of that State for which he shall be chosen.

The Vice President of the United States shall be President of the Senate, but shall have no Vote, unless they be equally divided.

The Senate shall chuse their other Officers, and also a President pro tempore, in the absence of the Vice President, or when he shall exercise the Office of President of the United States.

The Senate shall have the sole Power to try all Impeachments. When sitting for that Purpose, they shall be on Oath or Affirmation. When the President of the United States is tried, the Chief Justice shall preside: And no Person shall be convicted without the Concurrence of two thirds of the Members present.

Judgment in Cases of Impeachment shall not extend further than to removal from Office, and disqualification to hold and enjoy any Office of honor, Trust or Profit under the United States: but the Party convicted shall nevertheless be liable and subject to Indictment, Trial, Judgment and Punishment, according to

The **Contracts Clause** states:

"No State shall...pass any...Law impairing the Obligation of Contracts..."

Update on Business Continuity Disputes

- **Hundreds of BI suits have been filed against insurers**
  - Most are still making their way through the court system
  - Some cases will be consolidated in late July
- **Recently, some courts have made decisions favoring insurers**
- ***Gavrilides Management Company v. Michigan Insurance (July 2020)***
  - MI Circuit Court judge dismissed complaint brought by owner of 2 MI restaurants
  - Judge said BI must be triggered by *"something with material existence. . . that alters the physical integrity of the property."*
  - Court rejected argument that the virus exclusion was "vague"
  - Court determined that no factual development could change the complaint's allegation that loss of access to the premises and not physical damage to the property was the cause of the damages

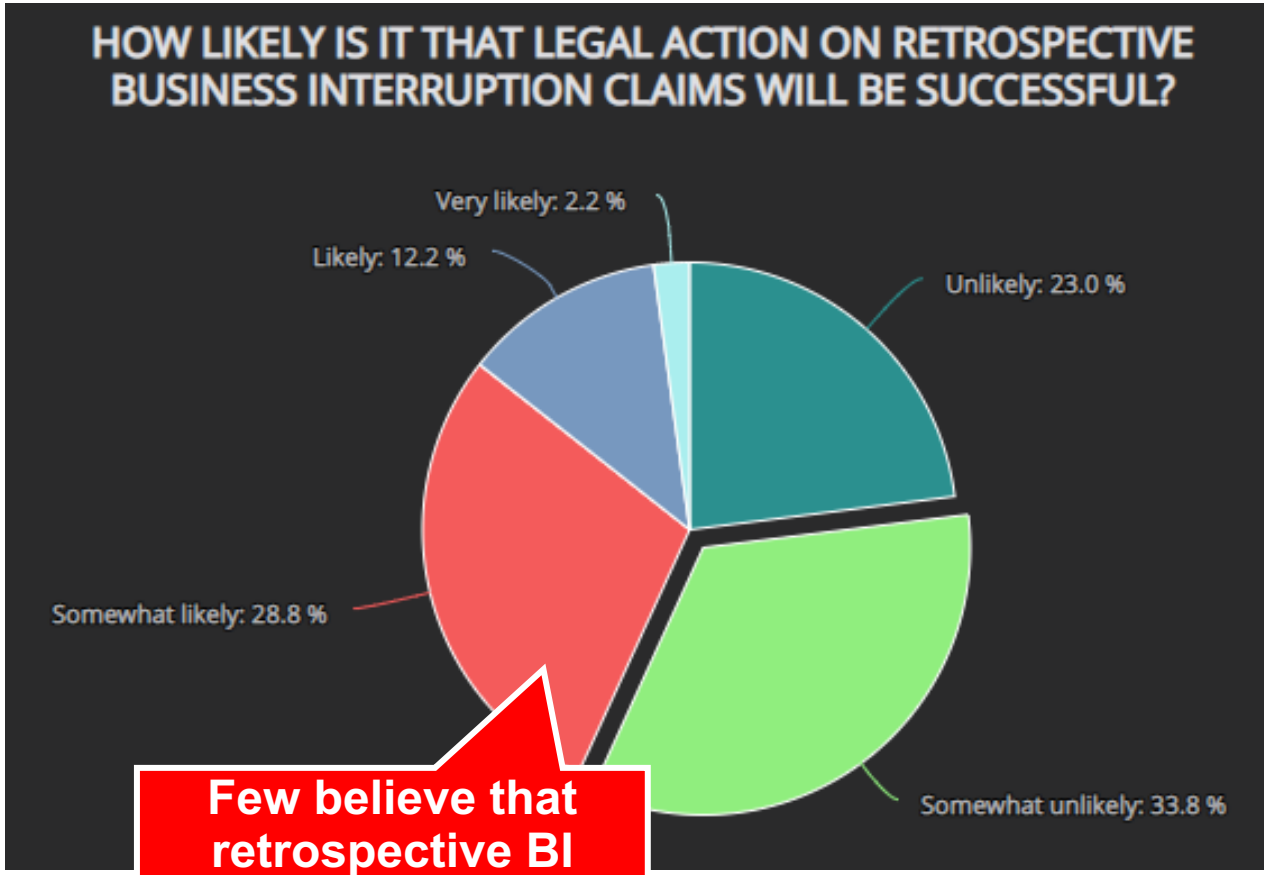
Source: PropertyCasualty360.com; July 7, 2020.

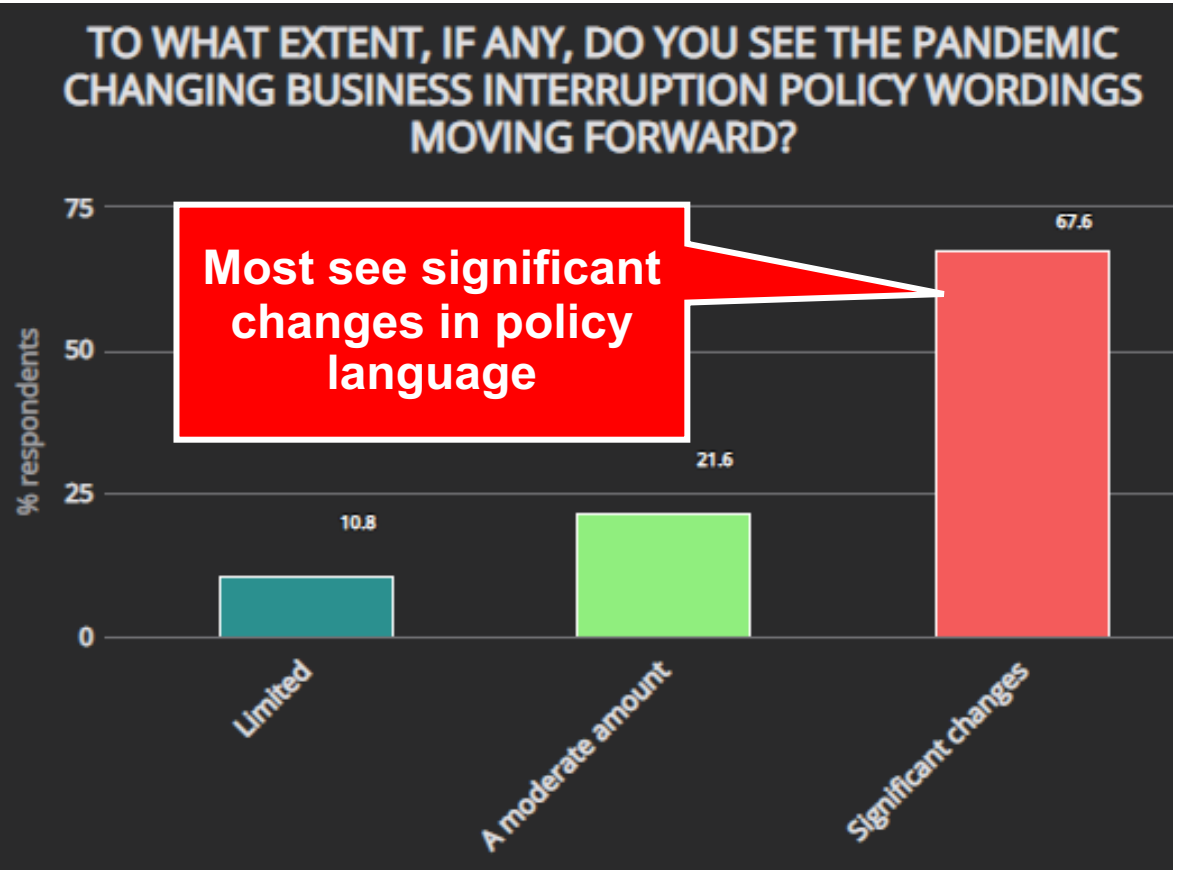
Update on Business Continuity Disputes

- ***Social Life Magazine, Inc. v. Sentinel Ins* (May 14, 2020)**
  - Southern District Court of NY concluded "New York law is clear" in requiring actual property damage to trigger business interruption coverage.
  - Because the insured's coverage theory rested on a government shutdown in the absence of any property damage, the Court denied its preliminary injunction motion, reasoning "this is just not what's covered under these insurance policies."
    - Note: As a publisher, Social Life Magazine was deemed a "nonessential business" by NY state, resulting in the inability of employees to work at the premises
  - Social Life's argument was essentially the same as in *Gavrilides v. Michigan Insurance* with the court ruling in essentially the same way as well, using virtually identical reasoning
  - Neither court bought the argument that a government shutdown in the absence of physical damage would trigger BI coverage

Source: Duane Morris LLP accessed at: https://www.lexology.com/library/detail.aspx?g=c97ba73d-2795-48e1-876c-8ec44387c2af

Market Survey: COVID-19 Litigation and Policy Language Impacts





Source: Artemis COVID-19 Market Survey (June 2020) accessed at: https://www.artemis.bm/coronavirus-survey-update/

Is a Pandemic Risk Insurance Act (PRIA) Really Needed?

- 9/11 produced widespread disruption through global (re)insurance markets and threatened the ability of the nation to recover from an unprecedented disaster
- The COVID-19 pandemic creates few meaningful disruptions in p/c (re)insurance markets
- TRIA was a very targeted, efficient solution that has brought nearly two decades of stability to the market
- Commercial insurers are not an appropriate or efficient means for the delivery of aid for viral outbreaks
- The $3+ trillion in federal emergency relief packages (as of 6/1) will use existing, efficient channels (e.g.,SBA,) for the delivery of targeted assistance to millions of businesses, individuals (direct payments, unemployment insurance) and other entities

BUSINESS INSURANCE.

Momentum builds for government pandemic backstop

Posted On: Mar. 24, 2020 2:47 PM CST

Claire Wilkinson

Legislation is in the works that would provide a go-forward mechanism for a federal backstop for pandemic risk insurance and could be introduced as soon as in the next 30 days, sources say.

The legislation would establish a pandemic risk insurance program, akin to the federal terrorism insurance backstop known as TRIA, they said.

A draft bill outlining the proposal has been circulated, led by House Financial Services Committee Chairwoman Maxine Waters, D-Calif., they said. The office of Chairwoman Waters did not return a call for comment.

The proposed backstop insurance mechanism could be added to later tranches of a financial aid package that Congress is negotiating, sources said.

Total federal stimulus including Federal Reserve bond purchases totals ~$6T - $8T or *approximately 30% of GDP + $1T infrastructure proposal…*

Why PRIA Is a Well-Intentioned but Bad Idea

- **Unlike TRIA, PRIA would create a large potential balance sheet liability for insurers**
- **This is because PRIA would impose a 5% coinsurance provision for industrywide BI losses exceeding a $250 million industrywide and a 5% individual company deductible equal to 5% DPE. The total of all individual insurer deductible is ~$12B**
  - **This is distinct from TRIA where the "reinsurance" is effectively "free"**
- **Program is capped at $750 billion so a 5% co-insurance requirement implies a potential industry liability of up to $37.5 billion**
- **These deductibles and coinsurance requirements would have potentially material implications for:**
  - **(Re)insurance balance sheets**
  - **RBC ratios**
  - **Surplus**

116TH CONGRESS
2D SESSION

H. R. _____

To establish a Pandemic Risk Reinsurance Program, and for other purposes.

IN THE HOUSE OF REPRESENTATIVES

M___. _____ introduced the following bill; which was referred to the Committee on _____

A BILL

To establish a Pandemic Risk Reinsurance Program, and for other purposes.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,

SECTION 1. SHORT TITLE.

This Act may be cited as the "Pandemic Risk Insurance Act of 2020".

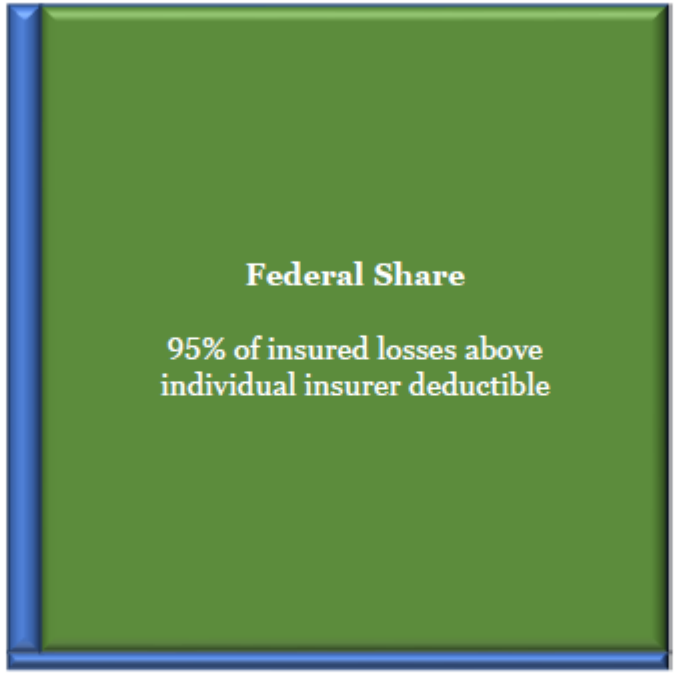
PPP program blew though $700B in only a few weeks

Source: Risk and Uncertainty Management Center, University of South Carolina and Centers for Better Insurance, "*Pandemiic Risk Insurance Act of 2020: Summary and Key Risks,*" June 2020.

Why PRIA Is a Well-Intentioned but Bad Idea

Up to $37.5B in liability for insurers

Total potential insurer liability under PRIA is almost $50 billion—nearly double the insured property losses from 9/11 and larger than every disaster in history other than Hurricane Katrina



Insurer Co-Share
5% of insured losses above individual insurer deductible

The insurer deductible and liability cap are based on insured losses from all covered public health emergencies declared in any one calendar year.

Liability Cap
Neither insurers nor Treasury have any obligations above the liability cap.

Claim payouts are pro-rated if it appears the cap may be reached.

Potentially $12B of liability for insurers

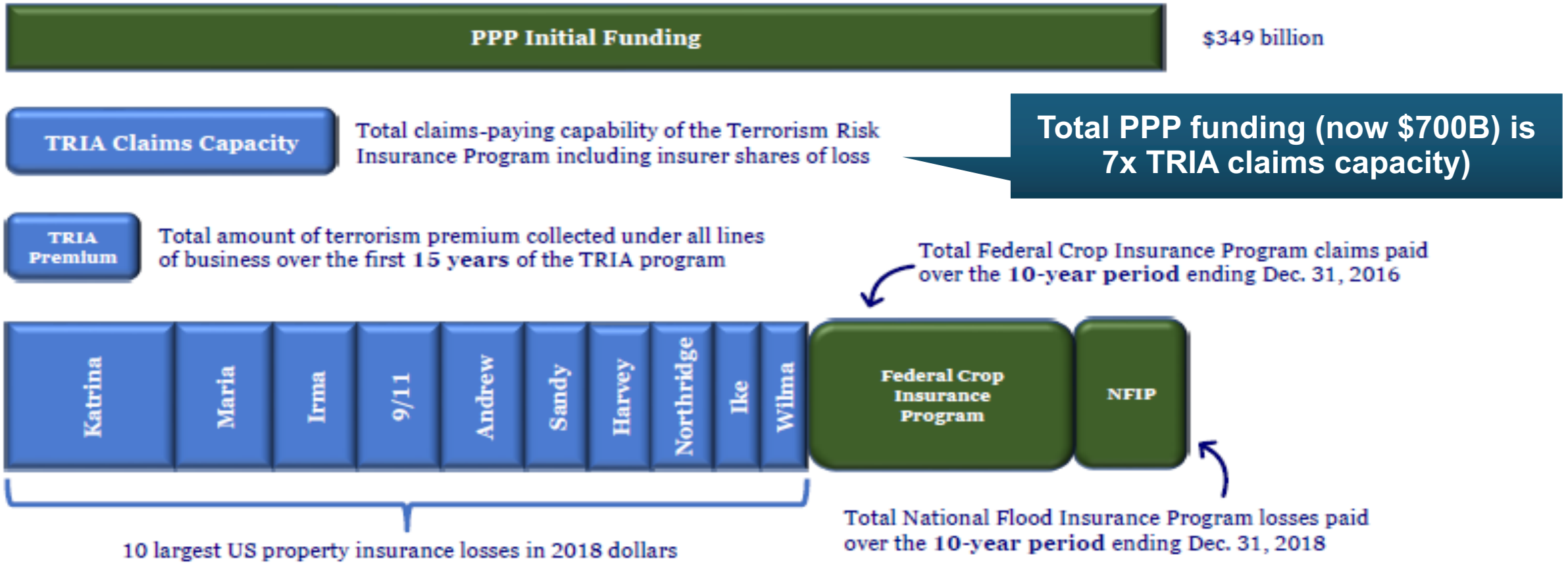
Program Trigger
Treasury may not make a payment under the program unless total insured losses from a declared public health emergency exceed $250 million.

Individual Insurer Deductible
5% of insurer's prior year direct earned premium for most commercial property and casualty lines of business

The total of all individual insurer deductibles is about $12 billion.

Source: Risk and Uncertainty Management Center, University of South Carolina and Centers for Better Insurance, "*Pandemic Risk Insurance Act of 2020: Summary and Key Risks,*" June 2020.

Why PRIA Is a Well-Intentioned but Bad Idea



The insurance claims administration capabilities necessary to investigate, document and payout an amount of insurance claims equivalent to the just the initial $349B in funding for the Paycheck Protection Program funding would be the same as if the top 10 US insurance catastrophes occurred in the same month PLUS 10 years of NFIP claim PLUS 10 years of federal Crop Insurance claims

Source: Centers for Better Insurance, *Insurance Programs for Pandemic Events*, (4/20); Risk and Uncertainty Management Center.

Business Continuity Protection Program (BCPP)

- **Purpose:** The BCPP is designed to bolster the country's economic resilience by providing timely and efficient financial protection and payroll support to the private sector in the event of a future declared public health emergency.
  - Has support of several industry group: APCIA, NAMIC, Big I
  - No balance sheet risk to the insurance industry

- **Structure:**
  - Businesses purchase revenue replacement assistance from the BCPP – up to 80% of payroll, employee benefits and operating expenses
  - Provides 3 months of relief payments
  - Payouts based on prior year's tax return
  - Relief is automatically triggered following a federally declared public health emergency

Source: APCIA

Business Continuity Protection Program (BCPP)

- **Business Continuity Payments:**
  - Businesses purchase revenue replacement assistance through state-regulated insurance entities that voluntarily participate with the BCPP
  - Relief would be automatically triggered and immediately paid following a Presidential viral emergency declaration (no advance documentation or claims adjustment)

- **Program Administration**
  - The BCPP would be run by FEMA, with limited administrative assistance from private contractors
  - Post-relief auditing for valid use of funds enforced through fines, required repayment, and criminal penalties
  - Every year, the BCPP shall consider purchasing reinsurance from payments received to protect federal taxpayers
  - The BCPP would work with risk mitigation experts to develop pandemic and viral risk mitigation guidelines and safety standards for businesses that would be provided to the purchaser at time of application and payment

Source: APCIA

Workers Compensation

Some Pressure Points

Payroll Exposure Is Contracting Rapidly

COVID-19: Efforts to Expand Presumption Continue

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Workers Compensation & COVID-19

- **Workers compensation written for COVID-19 exposed risks (e.g., hospitals, first responders, etc.) will likely see a spike in both severity and frequency**
- **Some states will require costs associated with precautionary quarantines of COVID-19 exposed workers**
- **Impact arising from "Essential Industries" unclear (e.g., grocery stores)**
- **Outside COVID-19 exposed segments—Large, Swift Drop in Payroll Exposure**
  - ***Drop in WC payroll exposure base could be the fastest and largest in history*** given the record 33.5 million initial unemployment claims data (week ending May 2nd) with much more to come
  - Wage growth, which had been making gains, will also slow
  - Overall likely net reduction in claim frequency

Workers Compensation & COVID-19

- **At least 12 states have expanded WC presumptions for COVID-19. Most restrict the assumption to "front-line" workers (e.g., health, 1st responders)**
  - **AK, AR, CA, KY, MI, MN, MO, NH, ND, UT and WA (as of June 5)**

- **Examples of presumption expansion beyond "front-line" workers: *KY and IL***
  - **On April 10, KY extended WC presumption to day care, grocery store and postal worker**
  - **June 5, IL Gov. Pritzker signed HB 2455 for extended to a very large number of occupations, including:**
  - Individuals employed by grocery stores, pharmacies, convenience stores, food banks, media outlets, gas stations, banks, hardware stores, educational institutions, transportation providers, manufacturing facilities and restaurants, as long as individuals employed by essential businesses and operations are required by their employment to encounter members of the general public or to work in employment locations of more than 15 employees.

SUMMARY

- The P/C Insurance Industry Remains Strong, Stable, Sound and Secure
- The Rapid Economic Slowdown Will Temper P/C Growth, Especially in Economically Sensitive Lines (especially Workers Comp)
- Asset Price Volatility Will Persist and Low Interest Rates Will Pressure Investment Earnings for Years
- COVID-19 Exposures Are Substantial but Manageable with Headline Risk on BI and WC Issues

UNIVERSITY OF
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Thank you for your time and your attention!

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Download at www.uscriskcenter.com