



The Insurance Working Group

On the Voluntary Business Preparedness Accreditation and Certification Program

Hosted by:
International Center for Enterprise Preparedness (InterCEP)
New York University

Initial Meeting
March 18, 2008

DRAFT SUMMARY PROCEEDINGS

(6/13/08 Version)

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EXECUTIVE SUMMARY

On March 18, 2008 a diverse group of public sector officials, private sector executives and practicing attorneys convened in an initial online forum of the Insurance Working Group to discuss insurance issues pertaining to the voluntary business preparedness accreditation and certification program currently under development pursuant to US federal legislation.

The discussion focused on the following key issues:

- The insurance industry can act as a major catalyst for businesses to undertake preparedness actions.
- Current efforts to correlate preparedness actions to loss reductions are largely focused on property risk.
- The Terrorist Reinsurance Act (TRIA) also has the effect of reducing the premium charged for exposures to risks associated with terrorism.
- The insurance market is stratified, with larger companies receiving relatively more attention and greater flexibility from underwriters than smaller companies.
- On the whole, underwriters would benefit from data that clearly correlates preparedness actions to a reduction of loss potential.
- Prudent actions taken by businesses may not generally be rewarded by insurers.
- The voluntary business preparedness certification program could provide the insurance industry with a justification for a shift toward more risk-based pricing and other incentives for companies to become more prepared.
- The standard(s) used in the certification program may provide underwriters with a way to systematize their understanding of business continuity practices.
- The audit processes involved with the certification program may provide underwriters with data they cannot access otherwise due to lack of time or expertise.
- Insurance regulators may consider how to promote the incorporation of elements of the certification program in the underwriting process.
- Management consultants to the insurance industry may also frame the certification program as an occasion to pursue competitive advantage.
- Insured companies may take individual and/or collective action to demand acknowledgement of preparedness efforts by insurers.
- There is also an opportunity to incorporate preparedness certification in an ongoing effort to standardize the electronic transmission of underwriting data.
- In order to make sure that the certification process can provide underwriters with information that is relevant to the underwriting process, the insurance industry should actively inform the design and development of the certification program.

ABOUT THE INTERNATIONAL CENTER FOR ENTERPRISE PREPAREDNESS (InterCEP)

- InterCEP is the world's first academic research center dedicated to private sector preparedness & corporate resilience.
- The Alfred P. Sloan Foundation funds InterCEP's research on incentives for business preparedness in the following areas:
 - Insurance, rating agency, mitigating insurance liability, supply chain, corporate governance.
- InterCEP's research focuses on linking the "what" and the "why" of preparedness and resilience:
 - What = preparedness standards and best practices.
 - Why = business & economic motivations to develop greater preparedness.

MEETING AGENDA

- 11:00 – 11:10: Overview of New Law: "The Implementing Recommendations of the 9/11 Commission Act of 2007" (Public Law 110-53 – Title IX, Section 524)
- 11:10 – 11:20: Focusing on the insurance perspective: Key questions
- 11:20 – 12:00: Open, facilitated discussion
- 12:00 – 12:30: Defining the Working Group agenda, including: possible next steps, activities, recommendations, etc.

GROUND RULES

- Participants may contribute directly to the conversation but should be recognized by the moderator first.
- Conference call will be recorded.
- All comments are not-for-attribution.
- Those not participating verbally, please forward your questions and comments throughout the discussion via Question & Answer Function.
- For post-forum comments, please email to intercep@nyu.edu.

OVERVIEW OF NEW LAW

"The Implementing Recommendations of the 9/11 Commission Act of 2007" (Public Law 110-53 – Title IX, Section 524) was signed into law on August 3, 2007. Section 524 calls for the creation of a voluntary business preparedness accreditation and certification program. The legislation stipulates that the program should:

- Provide a method to independently certify the emergency preparedness of private sector organizations, including disaster/emergency management and business continuity programs;
- Be administered outside of government by third party organizations with experience / expertise in managing and implementing voluntary accreditation and certification programs;
- Be voluntary;
- Designate one or more preparedness standards. NFPA 1600 is referenced as an example;
- Integrate/recognize where appropriate existing industry efforts, standards, practices and reporting in this area;
- Give special consideration to small businesses; and
- Protect proprietary and confidential information of companies.

U.S. DEPARTMENT OF HOMELAND SECURITY'S RESPONSIBILITIES

The legislation also assigns the following specific responsibilities to the U.S. Department of Homeland Security:

- Designate one or more organizations to act as the accrediting body to develop and oversee the certification process, and to accredit qualified third parties to carry out the certification program;
- Separately designate one or more standards for assessing private sector preparedness;
- Provide information and promote the business case for voluntary compliance with preparedness standards; and
- Monitor the effectiveness of program on an ongoing basis.

CURRENT STATUS

As of March 18, 2008, the current status of the certification program development process (to the best of InterCEP's knowledge) reflects the following:

- A 'Framework for Voluntary Preparedness' encompassing multiple preparedness standards and other guidance has been developed by key organizations (RIMS, DRII, ASIS, NFPA) with the support of the Alfred P. Sloan Foundation.¹ This document argues for flexibility within a framework in terms of preparedness standards and related certification activity.
- DHS preparing to report soon to Congress on a plan for program development.
- A potential accreditation body has been identified and notification published: ANAB.
- One or more preparedness standards are still to be designated.

THE WORKING GROUPS INITIATIVE

The objectives of InterCEP's initiative to organize Working Groups focused on the voluntary business preparedness accreditation and certification program are as follows:

- To identify existing practices and principles in specific topical areas relevant to private sector preparedness;
- In view of these practices and principles, to identify issues, opportunities and potential strategies relevant to the design and implementation of the voluntary business preparedness certification program; and,
- To gather these outputs generated by Working Group participants and communicate them to program stakeholders including where appropriate DHS, accrediting and certifying bodies.

Building on InterCEP's ongoing research on the business case for preparedness, there are currently five Working Groups, each focused on a particular area of business benefit that could potentially be enhanced by the certification program: insurance, legal, rating agency, supply chain, and business reporting requirements.

¹ Cf. "Framework for Voluntary Preparedness – Briefing Regarding Private Sector Approaches to H.R. 1 and public Law 110-53 'Implementing Recommendations of the 9/11 Commission Act of 2007' Title IX" prepared by representatives of ASIS International, DRII, NFPA, and RIMS. Available at www.sloan.org

THE INSURANCE PERSPECTIVE

InterCEP's ongoing research on the insurance incentives for business preparedness has indicated that corporations with effective emergency management and business continuity programs could benefit from relatively lower insurance costs and better policy terms.² With regard to the potential significance for the insurance industry of the voluntary business certification program, discussion among participants in the initial meeting of the Insurance Working Group is framed by the following key questions:

- How do insurance underwriters currently take account of preparedness efforts undertaken by firms:
 - In business interruption policies;
 - In director's and officer's (D&O) liability policies; and
 - In property and casualty policies?
- How should the preparedness certification program be designed and implemented to facilitate greater acknowledgement of business preparedness in insurance underwriting?

DISCUSSION

InterCEP has identified general themes touched on during the Working Group discussion. In this summary, these themes are briefly articulated, and then specific issues relevant to each theme are presented.

- **The insurance industry can act as a major catalyst for businesses to undertake preparedness actions.**
 - Participants acknowledged that the economic incentives controlled by the insurance industry play a major role in business decision-making when it comes to preparedness activities.
 - In the 9/11 Commission Report as well as the Intelligence Reform Act of 2004, where they first talked about NFPA 1600, there was a special role given to credit rating agencies and insurers to help promote preparedness. The question remains: how does and how has the insurance industry been promoting preparedness?
 - Although insurance incentives can serve as a catalyst for proactive preparedness activities, these incentives must be coherent with the realities of the proprietary nature of underwriting, the proprietary nature of rating, the proprietary nature of competitive planning and strategy.
 - The challenge is to determine within the existing context for underwriting first, what the appetite is for the development of new insurance incentives for preparedness, and second, what the effect of that appetite might be in view of the voluntary business preparedness certification program.
- **Current efforts to correlate preparedness actions to loss reductions are largely focused on property risk.**
 - Current insurance industry practice is to focus on preparedness actions relevant to physical property risk first, and to factor business interruption coverage into that premium.
 - With regard to casualty and liability insurance, there is not currently a great deal of consideration given to preparedness activities undertaken by companies.
 - Participants suggested that in many cases business interruption insurance premiums are currently not risk-based, and that in effect the coverage is basically given away.
 - One participant suggested that if an insurer were to pull business interruption insurance coverage out of the package policy and tell companies that they could have it back only if

²<http://www.nyu.edu/intercep/Insurance%20Incentives%20for%20Corporate%20Preparedness%2017%20Oct%2006.pdf>

they developed a business continuity plan, this might provide a clear incentive to undertake preparedness.

- **The Terrorist Reinsurance Act (TRIA) also has the effect of reducing the premium charged for exposures to risks associated with terrorism.**
 - Although participants affirmed the importance of TRIA, it was noted that the amount of the premium being charged for terrorism is somewhere between 1.5 to 3% of property coverage.
 - Because policies are not priced in accordance with actual risks associated with terrorism, it creates a problem with insurance incentives for efforts to mitigate the potential risk impacts associated with terrorism, including both physical and business interruption impacts.

- **The insurance market is stratified, with larger companies receiving relatively more attention and greater flexibility from underwriters than smaller companies.**
 - With bigger companies the pricing mechanism is often flexible enough to accommodate incentives for preparedness.
 - Larger companies are also more likely to be able to take care of themselves in most cases because of their size and resources often support dedicated departments for business continuity or risk management.
 - Among smaller companies, not only do they lack the resources to undertake significant preparedness activities, there is also not so much flexibility in the underwriting process to acknowledge whatever actions they might take.
 - One participant suggested that the stratification in the market creates a situation that is almost like being on two different planets. From this perspective, any systematized attempt to acknowledge preparedness in the underwriting process would have to be radically different for large companies than for small ones, and it may not be realistic to assume that any system developed for one segment of the market would ripple outward to effectively accommodate the other segments.
 - As a caveat to this notion, another participant noted that while the insurance underwriting process might be different for differently-sized companies, a standardized audit process would involve exactly the same process steps for small and large companies, though these steps would naturally take longer to complete the greater the size and scope of the firm being audited.

- **On the whole, underwriters would benefit from data that clearly correlates preparedness actions to a reduction of loss potential.**
 - On a conceptual and anecdotal basis, underwriters acknowledge that preparedness generally minimizes the impact of emergencies.
 - Nonetheless, for underwriters there optimally needs to be a clear data collection point that shows the correlation between preparedness actions and reduced loss potential by insured businesses.
 - One possibility might be to look within the processes that already exist within the insurance industry, possibly involving the Insurance Services Office (ISO) or others, to identify that data collection point that would correlate preparedness actions to loss potential.
 - In order to build a credible and substantial database to allow for a more detailed correlation, it may take years to identify companies or organizations that actually undertake preparedness actions, and then watch and see how they react to a major disaster event.

- **Prudent actions taken by businesses may not generally be rewarded by insurers.**
 - One participant suggested that if anything has been driving people into the alternative risk marketplace, it is not that they cannot get insurance for being reckless, but because they cannot get the economic value out of traditional insurance when they try to be prudent by developing robust preparedness programs.

- **The voluntary business preparedness certification program could provide the insurance industry with a justification for a shift toward more risk-based pricing and other incentives for companies to become more prepared.**
 - The basic economic equation in the insurance industry is that companies pay a premium for someone else to determine and bear a certain amount of risk. The assumption is that other insureds are being similarly rated to determine whether they are in the same risk pool, and that the premiums they pay are also appropriate. However, participants suggested that premium pricing (for all the various reasons outlined above) is not always risk-based, and thus that some firms may be paying too much while others may be paying too little for insurance.
 - The certification program may however provide insurance firms with an opportunity for the insurance industry introduce more rational and disciplined pricing into the marketplace by telling firms that if they get certified, your rates will stay the same, whereas if you do not, you will in fact have a different rate structure because you are not taking on these steps that reduce both your own exposure (in terms of retentions) and carrier exposure (in terms of potential covered loss).
- **The standard(s) used in the certification program may provide underwriters with a way to systematize their understanding of business continuity practices.**
 - Some businesses are already presenting their business continuity programs to underwriters, in particular with reference to their worker concentrations in particular geographic locations.
 - Other firms are beginning to see underwriters asking questions about worker concentrations and then subsequently asking questions about business continuity programs, emergency management activities, efforts to plan for how to care for employees if something would happen particularly at these concentrated areas.
 - If such efforts could be systematized in conjunction with the certification program, it would be easier for underwriters and insureds as well.
 - From an underwriter's perspective, there would be value in looking at a certification that a company has. The fact that some third party has come in and done that audit may help the underwriter's analysis and decision-making process.
- **The audit processes involved with the certification program may provide underwriters with data they cannot access otherwise due to lack of time or expertise.**
 - Insurance companies do not necessarily want to be the ones that send out people to conduct the audits – typically including interviews, document reviews, observations and the generation of a narrative report – to figure out whether an entity is prepared.
 - If however there were a third party certification program that underwriters could have confidence in, it might be taken into account in underwriting and risk assessment processes.
- **Insurance regulators may consider how to promote the incorporation of elements of the certification program in the underwriting process.**
 - While the regulatory community has not heretofore been heavily engaged in this issue, it could provide a level of protection vis-à-vis the antitrust laws when it comes to discussion among insurance firms of how to price risk.
 - The regulatory community could also use its existing oversight of underwriting and rating activities to promote inclusion of preparedness certification as a relevant factor.
 - Other participants expressed concern that if insurers as well as insureds did not stand up and take the lead with respect to the certification program, there would likely be more regulation, whether through the federal bodies or through the insurance regulators in all 50 states.
- **Management consultants to the insurance industry may also frame the certification program as an occasion to pursue competitive advantage.**

- One participant suggested that some management consultancy should start encouraging its clients to step outside of the existing box and take the lead in the industry by improving their underwriting strategies and incorporating preparedness activities into the pricing equation.
- Another participant said that while some discussions about how to take the lead in the marketplace have already begun, moving from the conversations to the competitive stage, is a long and difficult road.
- **Insured companies may take individual and/or collective action to demand acknowledgement of preparedness efforts by insurers.**
 - Another possibility for driving the development of insurance incentives for preparedness is to approach it from a consumer demand standpoint.
 - For example, one participant suggested that an organization such as the Risk & Insurance Management Society (RIMS) might help develop the business case by assembling its members who are putting these preparedness programs together and demanding better or more disciplined underwriting from their insurance companies.
- **There is also an opportunity to incorporate preparedness certification in an ongoing effort to standardize the collection and electronic transmission of underwriting data.**
 - There is an ongoing initiative focused on developing a common insurance application form that would collect underwriting data and allow it to be electronically transmitted. This initiative is being undertaken by the RIMS technology advisory committee together with ACORD, a nonprofit association whose mission is to facilitate the development and use of standards for the insurance, reinsurance and related financial services industries.
 - One participant suggested that the certification program might be integrated into this initiative as one data point that would be included in all underwriting proposals.
- **In order to make sure that the certification process can provide underwriters with information that is relevant to the underwriting process, the insurance industry should actively inform the design and development of the certification program.**
 - For example, multinational companies with global risk exposures often turn to non-US-based carriers for coverage. These offshore insurance firms should be integrated into the ongoing dialogue about how to design and develop the certification program in order to make certain that potential insurance incentives for certification are maximized.

INTERCEP'S ACTIVITIES

InterCEP is committed to supporting the Insurance Working Group by undertaking the following activities:

- Produce high-level summary proceedings of Working Group meetings, to be drafted by InterCEP, then vetted with participants, and finally distributed for stakeholder consideration;
- Develop greater awareness within the general business community of the voluntary business preparedness certification program;
- Produce research output that presents knowledge generated by the working group relevant to the design and implementation of the voluntary business preparedness accreditation and certification program;
- Develop an online clearinghouse of documentation relevant to the voluntary business preparedness accreditation and certification program.

SETTING THE WORKING GROUP AGENDA MOVING FORWARD

Next steps possibly to be undertaken by InterCEP with the support and involvement of members of the Insurance Working Group include:

- Support the organization of one or more forums that would bring together insurance companies and their customers (i.e., representatives of companies that purchase insurance) on this issue. The focus of these forums would be to allow insurance customers who have undertaken preparedness efforts to voice their concerns and desire to have insurance companies acknowledge preparedness more in their underwriting process including over time in the determination of premium pricing and other terms. The Risk Insurance & Management Society (RIMS) would be a most appropriate convener in this regard. InterCEP and the Working Group could support this and other efforts as appropriate.
- Support greater inclusion of information about business preparedness in the insurance underwriting process. In particular, work with the existing effort to develop a common electronic application form for insurance and advocate that this form include information regarding preparedness efforts by applicant companies including potentially whether or not the company has been certified by voluntary private sector preparedness certification program (as well as potentially more detailed assessment information).
- Explore the experience of insurance firms that have proactively sought to mitigate the risks of their customers and the results of these efforts on maximum foreseeable losses for those customers. Evaluate whether this approach should be adopted by other insurance firms and if so how.
- Solicit involvement in the Working Group from other stakeholders, including:
 - Management consulting firms specializing in the insurance industry;
 - Business continuity consultants such as SunGard, HP, IBM, etc.;
 - State insurance regulatory agencies and their professional associations.
- Support an insurance industry statement in support of business preparedness which indicates a willingness by insurance companies to acknowledge preparedness activities by customer companies in their underwriting and risk assessment.
- Explore and identify instances in which voluntary certification to standards (e.g., ISO 9000 or ISO 14000) is already taken into consideration in insurance underwriting processes.

With respect to each of these possible next steps, InterCEP seeks feedback and indications of interest from Working Group participants and readers of this document in response to the following questions:

- Do you think these next steps would have value?
- Do you have any information relevant to these next steps?
- Would you like to get involved and help craft these next steps?

In general, InterCEP is committed to shaping an agenda for the Working Group, including additional next steps and other action items, based on the feedback gathered from participants in response to these additional questions:

- Who else should be at this table?
- In what forums should this discussion be taking place?
- Who/what are the most relevant individuals, job titles, organizations, associations, etc.?
- What concrete next steps can be taken to acknowledge, integrate, and credit existing efforts?
- Additional next steps – what are we missing?
- What meeting formats are most appropriate to maximize participation and productivity?
- How regularly should Working Group meetings be scheduled?

InterCEP encourages readers of this document and other stakeholders to contact us on an ongoing basis with questions, comments and suggestions regarding the Working Group agenda, as well as in reference to the broader process of developing and implementing the certification program. InterCEP's efforts to support this process are undertaken independently with the support of the Alfred P. Sloan Foundation.

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