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REAL ESTATE BOARD OF NEW YORK

United States House of Representatives
Committee on Financial Services
2129 Rayburn House Office Building
Washington, D.C. 20515

Submitted via electronic mail to fsctestimony@mail.house.gov

Statement of John N. Lieber
before a Hearing of
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Subcommittee on Capital Markets, Insurance,
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"The Need to Extend the Terrorism Risk Insurance Act"

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Introduction:

Chairman Frank, Chairman Kanjorski, Ranking Member Pryce, members of the committee – Good Morning. My name is Janno Lieber. I am Senior Vice President at Silverstein Properties, where I have overall responsibility for the World Trade Center rebuilding project. I'm here this morning to testify not only on behalf of the Silverstein organization, but also on behalf of the Real Estate Board of New York (REBNY) and its members. Over the past few years, REBNY has been an effective leader on this very important issue of terrorism insurance. Thanks are particularly due to the efforts of two members of the REBNY Board who – in addition to leading a couple of the most substantial real estate firms in the entire country -- have spent countless hours on this issue: Steve Green, who is testifying with me here today, and Bill Rudin. I should also acknowledge the work of Steve Spinola, the President of REBNY, and Marolyn Davenport of his staff.

Thank you for making the trip to New York City. Over the past five years, this committee has given New York and its people tremendous support as we have faced the various impacts of 9.11 -- not least in the area of terrorism insurance. I'd also like to thank Chairman Kanjorski and Congresswoman Pryce for scheduling this hearing early in the session, and for making TRIA extension a priority.

Background:

As you know, the Silverstein organization leased the commercial office portions of the World Trade Center site from the Port Authority of New York and New Jersey just six weeks prior to September 11, 2001. Since that terrible day, our entire effort has been focused on rebuilding lower Manhattan as a dynamic mixed-use district, including a Memorial commemorating the 2,749 lives lost.

After several years of planning and extensive public dialogue, all parties are united as to what will be built at the World Trade Center – and also where, when and by whom. In late 2006, the new business arrangements between Silverstein Properties and our partners at the Port Authority of New York and New Jersey were formally and finally agreed upon – with the full support of the State of New York, the State of New Jersey and the City of New York. This means that the entire World Trade Center site -- including four exceptional skyscrapers designed by world-renowned architects -- will be rebuilt by 2012. You saw the beginnings of this work when you visited the site this morning. These soaring towers will make a magnificent contribution to the rebirth of lower Manhattan, joining the Calatrava-designed PATH Transportation Hub, expanded retail, a new Performing Arts Center, and, of course, the Memorial to make lower Manhattan one of the most exceptional places in the world.

Over the past few years, since the enactment of TRIA, the private insurance market has rebounded -- to a degree. However, in some areas, especially densely developed areas perceived as "high risk," there is simply insufficient insurance capacity – both terrorism insurance, and other insurances that have a terrorism component, such as builder's risk insurance. Thus, the circumstances that prompted Congress to create TRIA – *a shortage or unavailability of insurance, threatening market disruption* – still prevail. As detailed below, this is very much the case in lower Manhattan, which has suffered two terrorist attacks since 1993. Worse, there is a very real possibility that the expiration of TRIA or the program's inability to deal with lower Manhattan's unique circumstances could actually *trigger* a halt to the rebuilding of the World Trade Center and the rest of lower Manhattan.

We believe the debate about TRIA ought to focus less on the insurance industry and more on the policyholders – the owners, builders and managers of commercial and residential real estate in New York City. TRIA was designed to assure that terrorism insurance would be available and affordable to policyholders in order to protect the jobs in our buildings and the construction jobs that follow from our ability to develop buildings – including large-scale development projects like the one you saw this morning at Ground Zero. While reports indicate it is working reasonably well on a national scale, here in New York City – the largest real estate market in the country – it has been only partly successful, and there is a need for additional steps to encourage the insurance industry to make more capacity available.

Need for Permanent or Long-Term TRIA Extension:

The most important action Congress can take to assure availability of terrorism coverage for densely developed areas like New York City is to extend TRIA either permanently or for a very long period, i.e., no less than fifteen years. A long-term program is necessitated by the basic realities of how buildings are financed, built and insured on large-scale development projects. Large-scale developments -- a category that includes a very large portion of the projects in New York City -- can take a very long time from start to finish, including a three-to-five year design, planning and approval process, followed by several years of construction, and another few years of lease-up. TRIA needs to be tailored to match the timelines and exposures that the construction industry, lenders and insurers analyze when making decisions about whether to build, finance or insure these large-scale projects. The failure to do so will create inefficiencies in the market and impede new construction. And a short term renewal will not solve this problem.

Focus first on how the duration of the TRIA program impacts on the financing process. Today, most large commercial loans are securitized in order to create bonds that are purchased by institutional investors. Lenders often do not hold the loans that they originate, but usually sell all or a portion of the loans for regulatory or liquidity reasons. In order to receive investment-grade ratings from credit rating agencies -- which are often necessary to get investors to purchase the bonds -- the underlying collateral must be secured. The potential that a project might lose access to terrorism coverage -- for example, if the TRIA program expired – will impact on a project's ability to obtain an investment-grade rating; this is especially true of construction projects in highly concentrated, "high-risk" areas like Midtown or lower Manhattan. The federal backstop provided by TRIA, of course, does not guarantee that the insurance industry will actually make terrorism coverage available in these and other "high-risk" areas, or in adequate amounts; other changes to the program will be necessary to accomplish that goal. However, making the program permanent at least eliminates the risk that rating agencies must account for the possibility that a project will be unable to purchase insurance in the marketplace because the federal backstop has disappeared.

There are other lender concerns that should be taken into consideration in determining the duration of the TRIA program. A substantial percentage of large, fixed-rate commercial loans are for terms of at least ten years -- in some cases longer. If the term of a loan exceeds the length of a TRIA extension, the lenders must assess the risk of having to terminate the loan early because the borrower defaults on the covenant to maintain specified terrorism coverage. Alternatively, the lender will simply decide not to write the loans for a longer period than TRIA or not to write such loans at all.

Another aspect of the financing issue is that construction lenders need to know that permanent financing will be available to re-pay construction loans at the time of project completion -- financing that may not be available if TRIA has expired before the project is completed and the buildings are fully leased. Further, project participants -- including construction managers, contractors, owners, and lenders – normally require that project insurance policies be *non-cancelable* during the course of construction. Some insurers will reserve the right to cancel if reinsurance changes. A long term extension of TRIA is necessary to give all parties the confidence that terrorism insurance would *not* be cancelled as a result of the disappearance of the federal backstop.

In short, lenders, builders, and owners – who make up the membership of REBNY -- cannot embark on high-value construction projects where it is impossible to get insurance to protect against the risk of a loss. Most likely, developers will not initiate these projects if there is no guarantee they will have access to terrorism insurance through the period of construction -- and, thereafter, until after the expiration of the five-plus years of the statutes of repose governing design and construction design flaws.

Need for Additional Capacity:

I want to discuss one other major challenge today faced by large-scale projects in high risk areas -- the shortage of capacity. All over New York City, real estate owners and developers are struggling to obtain and maintain sufficient terrorism insurance. I spoke to one major owner whose lower Manhattan portfolio is worth roughly $10 Billion, but who has been unable to obtain more than $1 Billion of terrorism coverage. Another company was forced to delay a multi-hundred million dollar development while their businesspeople traveled to Europe, Asia and other foreign markets seeking to secure terrorism coverage. This shortfall in the terrorism coverage available here – which continues even though the TRIA program is in place -- is causing a wide variety of legal and business problems for these owner and many others like them.

The project I oversee for Silverstein – the World Trade Center rebuilding – provides a clear example. The World Trade Center will cost in the range of $13-$15 billion in total, including the four office towers, PATH Hub, the Memorial and all the infrastructure to serve this new district. But according to the leading insurance consultants and brokers in New York City, even with the current TRIA extension in place there is now less than $750 million worth of coverage available in the entire lower Manhattan market.

We strongly believe that a TRIA extension ought to address the capacity problem of densely developed urban areas branded as "high risk" by the insurance industry -- for example, lower Manhattan, Times Square and the Grand Central Station area. Today you are hearing from Mayor Bloomberg and several others, including Steve Green, one of the very largest owners in the City, about the need to address the problems of the current TRIEA relating to certified and non-certified acts – the foreign versus domestic distinction -- and so-called NBCR events. These proposed general "fixes" to TRIA are badly needed in order to free up terrorism insurance capacity. However, even if these important corrections are made there will *still* be questions about whether the incentives will be sufficient to attract more capacity to certain areas perceived as "high risk." Therefore, we suggest that consideration be given to additional actions – for example, (a) reducing the current "deductible retention" applicable to insurers under the current TRIEA for policies written to cover projects in areas that have previously experienced acts of terrorism or are otherwise judged "high-risk," and/or (b) reducing the current $100 million TRIEA program trigger. We are not absolutely wedded to any particular mechanism. But we do need this committee's leadership and creativity to find a way to assure that terrorism insurance is available to Midtown and lower Manhattan and other areas like them, where there is now a significant capacity shortfall. Obviously, it would be a great disappointment to everyone involved with the TRIA program if the redevelopment of the World Trade Center were seriously hindered by an inability to obtain terrorism insurance.

There is one other step Congress can take in order to free up terrorism insurance capacity. We also urge that a TRIA extension clarify the scope of TRIA coverage by making it clear that TRIA is a backstop for *all* proximate consequences of a terrorist attack, including a fire or collapse following an attack – as well as damages from the initial impact or explosion. Unfortunately, the scope of TRIA coverage is currently somewhat unclear, and therefore terrorism risk is bleeding into non-terrorism builder's risk and property insurances and causing a shortage of capacity for those coverages – especially in certain highly concentrated, "high-risk" areas like lower Manhattan.

Conclusion:

The TRIA program is essential to give projects any chance of obtaining the terrorism insurance which lenders and investors will require. It has been a success and it should be made permanent. However, according to our insurance professionals, it would not now be possible, even with the TRIA extension in place -- to adequately insure even *one* of the four office buildings now planned for construction on the World Trade Center site. Also, this doesn't account for the terrorism insurance needs of several other office buildings and a major transportation hub being constructed nearby – which will all have the effect of lessening capacity even further. In order to assure that commercial development thrives in our major urban centers, it is critical that the Government continue to work with the private sector to develop a long-term, workable solution, including some adjustments to the TRIA program designed to increase terrorism risk insurance capacity in high risk areas.

Thank you again for allowing us to participate today.