# RAIL MARKET REPORT

**Midyear 2024**

Gallagher

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## HEADLINES

- The US rail industry has been facing challenges in finding sufficient insurance coverage, particularly in relation to the significant increase of $323 million insurance cap under the existing Fixing America's Surface Transportation (FAST) Act.[1] There is a possible further significant hike to this cap rate in the pipeline.
- Companies are focusing on accurate property valuations and compliance to reduce potential underinsurance and optimize coverage. Insurance-to-value calculations have shown discrepancies of over 30%, leading to significant program structure gaps.[2]
- The US rail industry is awakening to the major threats relating to cybersecurity, both in terms of internal IT systems and operational systems.[3]
- The Rail Safety Act 2023 could lead to additional operating costs to ensure compliance with new safety measures, particularly for the transport of hazardous materials.[4]

## The US rail industry is at a critical juncture in 2024, grappling with transformative shifts and regulatory developments reshaping its landscape.

From the challenges of meeting expanded insurance requirements under the FAST Act to the potential implications of the Rail Safety Act of 2023, which seeks to enforce stringent safety measures, the industry faces both operational hurdles and regulatory pressures, as well as increased operational costs and stricter insurance terms. Moreover, as cyberthreats evolve and D&O liabilities expand, the need for comprehensive risk management strategies becomes increasingly urgent.

**This report will provide an overview of the fundamental market shifts and significant rail industry changes, as well as providing actionable insights in view of these transformative forces.**

## Capacity challenges and insurance market dynamics

One of the foremost challenges in the rail industry pertains to capacity. In February 2021, under the FAST Act, we witnessed the adjustment of the rail passenger transportation liability cap to $323 million, which, through third-party vendors, PSA carriers, and owners/lessors of trackage, contractually required rail carriers to insure up to the cap and naming them as additional named insureds. As a result, finding adequate coverage has become increasingly difficult due to market fluctuations and carriers' exit from the London and international markets. This trend underscores the increasing importance of robust industry relationships to mitigate gaps in coverage and ensure compliance with developing regulatory requirements. A key to these professional relationships is to have a solid foundation of trust that has been built and refined through years of working through the difficult markets for which the rail space is known to present.

## Increase to rate cap implications

The rail industry saw a significant adjustment to its liability cap under the FAST Act in 2021, requiring carriers to increase insurance coverage to $323 million. This mandate applies broadly across commuter and freight rail sectors, particularly impacting heavy rail operations and necessitating compliance within a tight 30-day window upon announcement. Future increases are anticipated, potentially driven by inflationary adjustments, which could further strain market capacity and operational budgets. Stakeholders must stay vigilant, preparing for regulatory changes that may escalate insurance requirements and associated costs.

## Regulatory landscape and safety concerns

The Rail Safety Act of 2023 looms large over the industry, responding to safety incidents such as the Norfolk Southern East Palestine derailment.[5] This legislation proposes stricter safety measures for transporting hazardous materials, potentially increasing carriers' operational costs and regulatory compliance burdens. The act includes mandates for two-person train crews and heightened fines for safety violations, reflecting an increased focus on safety accountability amid public scrutiny.

## Market response and industry adaptation

While railroads are grappling with the operational and financial implications of regulatory changes and market pressures, the insurance industry is also facing a shortage of experienced rail underwriters due to retirements, complicating the ability to underwrite rail accounts.

Significant losses have led to a drastic rise in excess liability premiums, with a $10 million loss a decade ago now translating to a $150 million loss, adversely affecting carriers' profitability.[6] Consequently, many carriers are reconsidering their involvement in this sector due to the high hazards involved and the potential for catastrophic losses associated with rail accidents, necessitating proactive engagement with underwriters and stakeholders to anticipate and manage these evolving risks.

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**$150 million**

have lead to a rise in excess liability premiums.

# Property, casualty, D&O, and cyber

### Property and casualty

Property values and insurance rates in the rail sector have shown resilience, with a modest increase of about 5% in 2024.[7] Despite this stability, challenges persist, including the rising concern of nuclear verdicts in casualty claims, particularly under the Federal Employers Liability Act (FELA).[8] FELA governs compensation for injuries to railroad workers and is incorporated into rail liability policies, regulated federally. This integration poses significant underwriting challenges due to expansive liability capacity and unpredictable jury decisions.

### Directors & Officers

Directors and officers in the rail sector are increasingly concerned about D&O liability amid growing scrutiny and the potential for cybersecurity breaches. Employment practices liability claims have risen, prompting firms to secure robust D&O coverage to shield executives from personal liability risks arising from their management decisions.

### Cyber insurance

Cybersecurity emerges as a critical concern for railroads, encompassing IT and operational systems. Implementing positive train control (PTC) systems mandates heightened cybersecurity measures to prevent potential disruptions and unauthorized access. However, the rail industry faces challenges in obtaining adequate cyber insurance coverage tailored to its unique operational risks and vulnerabilities.

> “Our detailed risk assessments and thorough analysis provide carriers with a strong sense of reassurance, setting Gallagher apart. We have the resources and actively implement them to help clients understand their true risks. Our commitment to clients' success and protection is paramount. Managing everyday business risks through such dedicated efforts is crucial. While D&O insurance is well established, cyber protection in the rail sector is still emerging. However, we are increasingly helping clients to go beyond merely reacting to cyberthreats to understand their real vulnerabilities.”
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> **Brad Burtram**
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> **Executive Director — Rail, Gallagher**

> “Cybersecurity is a growing concern across all industries, and railroads are increasingly inquiring about cyber coverage. With clients now assessing whether their existing coverage is adequate, we have conducted cyber assessments to identify client vulnerabilities and partnered with our London team, which specializes in transportation, to engage with markets effectively. This collaboration has proven beneficial, allowing us to present compelling information to underwriters and secure the appropriate coverage for our clients.”
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> **Kevin Woods**
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> **Managing Director — Rail, Gallagher**

## Environmental and social governance initiatives

There is a growing emphasis on environmental and social governance (ESG) considerations within the rail industry, driven by environmental sustainability and regulatory expectations.[9] With rail transportation increasingly perceived as a greener alternative to other modes of transport, the rail industry is responding by exploring innovations in sustainability practices and aligning with broader ESG goals to enhance this competitive position.

## Facing challenges with confidence

The rail market is experiencing substantial change characterized by regulatory challenges, technological advancements, and evolving insurance dynamics. As stakeholders navigate these complexities, attune to market shifts, and adopt proactive risk mitigation strategies, Gallagher's rail experts stand ready to provide tailored solutions that anticipate and address these evolving challenges.

> "There is a growing interest in greener transportation options that reduce carbon impact and environmental harm, and rail transportation stands out in this regard. It will be intriguing to see how the next generation of leaders shapes the rail sector and prioritizes sustainability. The industry must adapt and evolve to stay competitive. This leadership transition will be a fascinating development to observe."
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> **Jason D. Majewski**
> **Area Vice President — Rail, Gallagher**

## SOURCES

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[8] "Are Railroad Workers Eligible for Workers' Comp?" Burge & Burge, PC, 02 Apr 2020.

[9] Ott, Anselm, et al. "Good, Better, Best: Railways are Advancing their ESG Agenda," McKinsey, 15 Jun 2023.

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