

FROM: Director, Worldwide Markets
LOCATION: G12
EXTENSION: 5998
DATE: 27 November 2002
REFERENCE: Y2924
SUBJECT: US TERRORISM RISK INSURANCE ACT OF 2002
SUBJECT AREA(S): US commercial insurance business (as defined in the Act)
ATTACHMENTS:
ACTION POINTS: **To note the signing into law of the above Act and the immediate implications for underwriters and brokers**
DEADLINE: **Immediate**

1 Purpose of bulletin

To advise the market that President Bush signed the U.S. Terrorism Risk Insurance Act of 2002, ("the Act") into law yesterday (26/11/2002).

2 Provisions of the Act

Details of the Act were provided in Market Bulletin Y2917, issued on the 22/11/2002.

The Act introduces immediate significant changes to the exclusion and cover of U.S. terrorism risks. An exclusion on a commercial property or casualty insurance contract for an "act of terrorism" as defined under the Act is "void to the extent that it excludes losses that would otherwise be insured losses". From 26/11/2002 underwriters are therefore automatically on risk for defined "acts of terrorism" in the U.S. (as defined in the Act), although – provided they comply with the Act's provisions – they will benefit from the Federal Terrorism Insurance Program introduced by the Act. (See appendix for notices and authorization of the reinstatement of exclusions.)

3 Nullification of Terrorism Exclusions and notification requirements

The Act nullifies Pre-existing Terrorism Exclusions on commercial property and casualty insurance, including marine and aviation business. The Act also requires insurers to provide disclosure to the policyholder of the premium charged for insured losses covered by the Program and the Federal share of compensation for insured losses under the Program.

Failure to comply with notice conditions could result in penalties to insurers and could jeopardise the benefit of the Federal Reinsurance coverage.

These issues were discussed in Market Bulletin Y2917.

4 Notices to Insureds

To assist compliance with the notification requirements a preliminary model notice applicable to policies in force on the date of enactment of this legislation was included in the previous market bulletin. The NAIC has also now compiled a draft notice and the ISO is currently completing its own form of notice for the domestic licensed industry. It is possible that The Treasury Department may develop a “safe harbor” form of notice, perhaps based on the NAIC form, the ISO form, or ours and we will advise the market of developments.

The issue of appropriate forms of notices and responsibilities for notification to Insureds is being actively discussed with the Market through the LMA and the LMIBC.

5 Joint Lloyd’s / LMA Committee

Lloyd’s and the LMA have established a Joint Committee to address the ramifications of the Act for the Lloyd’s market and to take forward the necessary notification to insureds, and required changes in reporting and processing. Contact points for the Committee are John Moloney (John.Moloney@lloyds.com) at the LMA and James Walmsley (James.S.Walmsley@lloyds.com) & Sally Herman (Sally.Herman@lloyds.com) in Lloyd’s Worldwide Markets Division. The LMIBC is fully involved in this activity.

In conjunction with our U.S. legal advisors LeBoeuf, Lamb, Greene & MacRae we are actively discussing issues with The U.S. Treasury and the National Association of Insurance Commissioners. The U.S. Treasury Department and the NAIC will issue ‘implementing regulations’ to clarify issues raised by the insurance industry regarding the Act, although the timing of such guidelines and regulations is currently uncertain.

6 Further Information

We are aware that clarification is urgently required on several issues in order for the market to assess the full implications and take forward the practical implementation. Lloyd’s and the Joint LMA Committee are seeking responses to these issues and monitoring guidance as it becomes available. Extensive market consultation is being undertaken. Further market bulletins will be issued, as information becomes available.

LeBoeuf, Lamb, Greene & MacRae, L.L.P. made presentations on this issue to Lloyd’s on 7 November 2002 and 26 November 2002. Members / Lloyd’s underwriters can obtain copies

of the slides from the LMA, contact: Martin Roberts on Lloyd's extension 8370 (by email at martin.roberts@lloyds.com) or from the Worldwide Markets division in Lloyd's, on extension 6677 (email at market.services@lloyds.com).

The Act in its entirety can be viewed at <http://thomas.loc.gov>. The instructions for viewing the Act are set out in Market Bulletin Y2917 and must be followed to ensure that you are viewing the definitive version of the Act.

This bulletin has been sent to active underwriters and compliance officers of managing agents and Lloyd's brokers.

Appendix

Nullification of Terrorism Exclusions and notification requirements

The Act states that:

Sec 105

(a)GENERAL NULLIFICATION.-Any terrorism exclusion in a contract for property and casualty insurance that is in force on the date of enactment of this Act shall be void to the extent that it excludes losses that would otherwise be insured losses.”

It is emphasised that the term 'terrorism' relates only to a U.S. “act of terrorism”¹ as certified by the Secretary of the Treasury, in concurrence with the Secretary of State and the Attorney General of the United States, meaning that, exclusion is only void to the extent of provision under the Act. To be certified, damage from the terrorist act must occur within the United States (except in the case of air carriers, vessels or if occurring on the premises of a U.S. mission) and must have been perpetrated on behalf of a foreign person or foreign interest.

The previous bulletin should be consulted for more detailed information on definitions.

Insurers included under the Program must “make available”, in respect of all relevant commercial property and casualty policies², coverage for insured losses resulting from “acts of terrorism”.

Insurers must therefore notify the insured, offering coverage for “acts of terrorism”. Additional premium may be charged. Having notified the insured, insurers may reinstate exclusions in respect of “acts of terrorism” if:

- The customer authorises the reinstatement of the exclusion in writing; or
- The customer fails to pay any stated additional premium (the insured must be provided with at least 30 days notice of the date on which the terrorism exclusion will be reinstated if no payment is received). Underwriters will be on risk from the date of enactment. Further clarification is being sought in relation to coverage issues during the 30 days between notice being sent to the insured and their response.

Underwriters are on risk from the date of enactment.

¹ The Act provides that the limit for aggregated insured losses per calendar year (2003 also includes the transition period) is \$100 billion for all “acts of terrorism”.

² All commercial P & C lines are affected, excepting: Reinsurance, crop, medical malpractice, personal lines, PMI, mono-line financial guaranty, National Flood Insurance Programs and life and health. Marine, aviation and transport business is encompassed under the Act. Coverage will apply to US situs risks / losses arising from “acts of terrorism” in the U.S, except in the case of designated air carriers, vessels and U.S. missions. Further clarification is being sought on whether “all property and casualty insurance policies” is limited to U.S. insureds, or all insureds with U.S. exposures. As we understand it to date it will be limited to U.S. insureds. The benefits of the reinsurance program would, however, in the event of an “act of terrorism” resulting in damage in the US, extend to non U.S. insureds suffering losses in the U.S. as a result of such an “act of terrorism”, if they have general coverage with an insurer encompassed in the Program. Further guidance is expected from the U.S. Treasury in the near future.

Market Supervision will be monitoring this key risk. Managing Agents' systems must record evidence of notification and procedures must be put in place to track responses from insureds. Thereafter, systems and procedures must monitor exposure on an on-going basis.

Again, it is emphasised that the previous market bulletin should be consulted for further detail on the Act – particularly specific definitions. More detailed information for in-force and later-issued policies is also covered.

Sec 103

“(b) CONDITIONS FOR FEDERAL PAYMENTS.—No payment may be made by the Secretary under this section with respect to an insured loss that is covered by an insurer, unless—

(1) the person that suffers the insured loss, or a person acting on behalf of that person, files a claim with the insurer;

(2) the insurer provides clear and conspicuous disclosure to the policyholder of the premium charged for insured losses covered by the Program and the Federal share of compensation for insured losses under the Program—

(A) in the case of any policy that is issued before the date of enactment of this Act, not later than 90 days after that date of enactment;

(B) in the case of any policy that is issued within 90 days of the date of enactment of this Act, at the time of offer, purchase, and renewal of the policy; and

(C) in the case of any policy that is issued more than 90 days after the date of enactment of this Act, on a separate line item in the policy, at the time of offer, purchase, and renewal of the policy;”