

MONTANA STATE AUDITOR

JOHN MORRISON
STATE AUDITOR



COMMISSIONER OF INSURANCE
COMMISSIONER OF SECURITIES

Advisory Memorandum

TO: *All Property and Casualty Insurers Writing Commercial Lines Insurance Products*

FROM: *John Morrison, Montana State Auditor, Commissioner of Insurance*

DATE: *September 18, 2008*

RE: *Filing Procedures for Compliance with the Provisions of the Terrorism Risk Insurance Program Reauthorization Act of 2007*

Background

There has been much uncertainty in the markets for commercial lines property and casualty insurance coverage in light of the substantial losses experienced by the industry on September 11, 2001. Soon after the tragic events, many reinsurers announced that they did not intend to provide coverage for acts of terrorism in future reinsurance contracts. This led to a concerted effort on behalf of all interested parties to seek a temporary federal backstop to calm market fears over future terrorist attacks and the ability of the insurance industry to allocate capital to provide coverage for these unpredictable and potentially catastrophic events. As a result, Congress enacted and the President signed into law in November 2002, the Terrorism Risk Insurance Act of 2002 (the Act). This federal law provides a federal backstop for defined acts of terrorism and imposes certain obligations on insurers. The Act was extended for a two-year period covering Program Years 2006 and 2007. The Act has now been extended for an additional seven years through December 31, 2014, with the enactment of the Terrorism Risk Insurance Program Reauthorization Extension Act of 2007.

The intent of this advisory memorandum is to advise you of certain provisions of the Act, as extended, that may require insurers to submit a filing in this state of the disclosure notices, policy language and the applicable rates as a result of the Act.

Several provisions of the initial Act have changed in the 2007 extension. Those changes include:

- Revising the definition of a certified act of terrorism to eliminate the requirement that the individual(s) are acting on behalf of any foreign person or foreign interest.
- Extending the program through December 31, 2014.

- Requiring clear and conspicuous notice to policyholders of the existence of the \$100 billion cap.
- Fixing the Insurer Deductible at 20% of an insurer's direct earned premium, and the federal share of compensation at 85% of insured losses that exceed insurer deductibles.
- Fixing the program trigger at \$100 million for all additional program years.
- Requiring the U.S. Treasury to promulgate regulations for determining pro-rata shares of insured losses under the program when insured losses exceed \$100 billion.
- Requiring the Comptroller General to study the availability and affordability of insurance coverage for losses caused by terrorist attacks involving nuclear, biological, chemical, or radiological materials and issue a report not later than one year after the enactment of the Terrorism Risk Insurance Program Reauthorization Act of 2007.
- Requiring the Comptroller General to determine whether there are specific markets in the United States where there are unique capacity constraints on the amount of terrorism insurance available and issue a report not later than 180 days after the enactment of the Terrorism Risk Insurance Program Reauthorization Act of 2007.
- Requiring the President's Working Group on Financial Markets to continue an ongoing study of the long-term availability and affordability of terrorism risk insurance.
- Accelerating the timing of the mandatory recoupment of the federal share through policyholders' surcharges.

Other terms of the Act, as amended by the Terrorism Risk Insurance Extension Act of 2005, remain unchanged.

Definition of Act of Terrorism

One of the changes made to TRIA with the enactment of the Terrorism Risk Insurance Program Reauthorization Act of 2007 was a revision to the definition of an act of terrorism that eliminated the requirement that an individual or individuals that carry out an act of terrorism be acting on behalf of a foreign person or foreign interest. In short, this means that acts formerly referred to as "domestic" terrorism may now be certified as an act of terrorism under TRIA.

Section 102(1) defines an *act of terrorism* for purposes of the Act. Please note that the unmodified reference to "the Secretary" refers to the Secretary of the Treasury. The revised Section 102(1)(A) states, "The term "act of terrorism" means any act that is

certified by the Secretary, in concurrence with the Secretary of State, and the Attorney General of the United States—(i) to be an act of terrorism; (ii) to be a violent act or an act that is dangerous to—(I) human life; (II) property; or (III) infrastructure; (iii) to have resulted in damage within the United States, or outside the United States in the case of—(I) an air carrier or vessel described in paragraph (5)(B); or (II) the premises of a United States mission; and (iv) to have been committed by an individual or individuals, as part of an effort to coerce the civilian population of the United States or to influence the policy or affect the conduct of the United States Government by coercion.” Section 102(1)(B) states, “No act shall be certified by the Secretary as an act of terrorism if—(i) the act is committed as part of the course of a war declared by the Congress, except that this clause shall not apply with respect to any coverage for workers’ compensation; or (ii) property and casualty insurance losses resulting from the act, in the aggregate, do not exceed \$5,000,000.” Section 102(1)(C) and (D) specify that the determinations are final and not subject to judicial review and that the Secretary of the Treasury cannot delegate the determination to anyone.

The Terrorism Risk Insurance Act, as amended, contains in Section 103(1)(B) a program trigger of \$100 million in aggregate industry insured losses resulting from a certified act of terrorism before federal reimbursement is triggered.

This state will not allow exclusions of coverage for acts of terrorism that fail to be *certified losses* solely because they fall below the \$5,000,000 threshold in Section 102(1)(B) on any policy that provides coverage for acts of terrorism that fail to be *certified*. Insurers required to file policy forms may submit language containing coverage limitations for *certified losses* that exceed \$100 billion in the aggregate.

Submission of Rates, Policy Form Language and Disclosure Notices

If an insurer relies on an advisory organization to file loss costs and related rating systems on its behalf, no rate filing is required unless an insurer plans to use a different loss cost multiplier than is currently on file for coverage for *certified losses*. Insurers that develop and file rates independently may choose to maintain their currently filed rates or submit a new filing. The rate filing should provide sufficient information for the reviewer to determine what price would be charged to a business seeking to cover *certified losses*. This state will accept filings that contain a specified percentage of premium to provide for coverage for *certified losses*. Insurers may also choose to use rating plans that take into account other factors such as geography, building profile, proximity to target risks and other reasonable rating factors. The insurer should state in the filing the basis that it has for selection of the rates and rating systems that it chooses to apply. The supporting documentation should be sufficient for the reviewer to determine if the rates are excessive, inadequate or unfairly discriminatory.

Insurers subject to policy form regulation must submit the policy language that they intend to use in this state. The policy should define *acts of terrorism* in ways that are consistent with the Act, as amended, state law and the guidance provided in this bulletin. The definitions, terms and conditions should be complete and accurately

describe the coverage that will be provided in the policy. Insurers may conclude that current filings are in compliance with the Act, as amended, state law and the requirements of this bulletin. However, if policy forms make a distinction between acts of a foreign person or foreign interest and a domestic person or domestic interest, it is likely that a filing is required.

Another change introduced in the Terrorism Risk Insurance Program Reauthorization Act of 2007 is a new disclosure requirement for any policy issued after the enactment of the Act. Specifically, in addition to other disclosure requirements previously contained in TRIA, insurers must now also provide clear and conspicuous disclosure to the policyholder of the existence of the \$100 billion cap under Section 103(e)(2), at the time of offer, purchase and renewal of the policy.

The Commissioner requests that the disclosure notices be filed for informational purposes. The policy forms, rates and rating systems, which are an integral part of the process for notification of policyholders in this state, should be clear and not misleading to business owners in this state and must be filed and approved as required by Montana law. The disclosures should comply with the requirements of the Act, as amended, and should be consistent with the policy language and rates filed by the insurer.

Effective Date

This advisory memorandum shall take immediate effect and shall expire on December 31, 2014, unless Congress extends the duration of the Act.

Questions regarding this advisory should be directed to:

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Attachment A

POLICYHOLDER DISCLOSURE NOTICE OF TERRORISM INSURANCE COVERAGE

You are hereby notified that under the Terrorism Risk Insurance Act, as amended, that you have a right to purchase insurance coverage for losses resulting from acts of terrorism, *as defined in Section 102(1) of the Act*: The term “act of terrorism” means any act that is certified by the Secretary of the Treasury—in concurrence with the Secretary of State, and the Attorney General of the United States—to be an act of terrorism; to be a violent act or an act that is dangerous to human life, property, or infrastructure; to have resulted in damage within the United States, or outside the United States in the case of certain air carriers or vessels or the premises of a United States mission; and to have been committed by an individual or individuals as part of an effort to coerce the civilian population of the United States or to influence the policy or affect the conduct of the United States Government by coercion.

YOU SHOULD KNOW THAT WHERE COVERAGE IS PROVIDED BY THIS POLICY FOR LOSSES RESULTING FROM CERTIFIED ACTS OF TERRORISM, SUCH LOSSES MAY BE PARTIALLY REIMBURSED BY THE UNITED STATES GOVERNMENT UNDER A FORMULA ESTABLISHED BY FEDERAL LAW. HOWEVER, YOUR POLICY MAY CONTAIN OTHER EXCLUSIONS WHICH MIGHT AFFECT YOUR COVERAGE, SUCH AS AN EXCLUSION FOR NUCLEAR EVENTS. UNDER THE FORMULA, THE UNITED STATES GOVERNMENT GENERALLY REIMBURSES 85% OF COVERED TERRORISM LOSSES EXCEEDING THE STATUTORILY ESTABLISHED DEDUCTIBLE PAID BY THE INSURANCE COMPANY PROVIDING THE COVERAGE. THE PREMIUM CHARGED FOR THIS COVERAGE IS PROVIDED BELOW AND DOES NOT INCLUDE ANY CHARGES FOR THE PORTION OF LOSS THAT MAY BE COVERED BY THE FEDERAL GOVERNMENT UNDER THE ACT.

YOU SHOULD ALSO KNOW THAT THE TERRORISM RISK INSURANCE ACT, AS AMENDED, CONTAINS A \$100 BILLION CAP THAT LIMITS U.S. GOVERNMENT REIMBURSEMENT AS WELL AS INSURERS' LIABILITY FOR LOSSES RESULTING FROM CERTIFIED ACTS OF TERRORISM WHEN THE AMOUNT OF SUCH LOSSES IN ANY ONE CALENDAR YEAR EXCEEDS \$100 BILLION. IF THE AGGREGATE INSURED LOSSES FOR ALL INSURERS EXCEED \$100 BILLION, YOUR COVERAGE MAY BE REDUCED.

Acceptance or Rejection of Terrorism Insurance Coverage

<input type="checkbox"/>	I hereby elect to purchase terrorism coverage for a prospective premium of \$ _____.
<input type="checkbox"/>	I hereby decline to purchase terrorism coverage for certified acts of terrorism. I understand that I will have no coverage for losses resulting from certified acts of terrorism.

Policyholder/Applicant's Signature

Insurance Company

Print Name

Policy Number

Date

**POLICYHOLDER DISCLOSURE
NOTICE OF TERRORISM
INSURANCE COVERAGE**

Coverage for acts of terrorism is included in your policy. You are hereby notified that under the Terrorism Risk Insurance Act, as amended in 2007, the definition of act of terrorism has changed. As defined in Section 102(1) of the Act: The term "act of terrorism" means any act that is certified by the Secretary of the Treasury—in concurrence with the Secretary of State, and the Attorney General of the United States—to be an act of terrorism; to be a violent act or an act that is dangerous to human life, property, or infrastructure; to have resulted in damage within the United States, or outside the United States in the case of certain air carriers or vessels or the premises of a United States mission; and to have been committed by an individual or individuals as part of an effort to coerce the civilian population of the United States or to influence the policy or affect the conduct of the United States Government by coercion. Under your coverage, any losses resulting from certified acts of terrorism may be partially reimbursed by the United States Government under a formula established by the Terrorism Risk Insurance Act, as amended. However, your policy may contain other exclusions which might affect your coverage, such as an exclusion for nuclear events. Under the formula, the United States Government generally reimburses 85% of covered terrorism losses exceeding the statutorily established deductible paid by the insurance company providing the coverage. The Terrorism Risk Insurance Act, as amended, contains a \$100 billion cap that limits U.S. Government reimbursement as well as insurers' liability for losses resulting from certified acts of terrorism when the amount of such losses exceeds \$100 billion in any one calendar year. If the aggregate insured losses for all insurers exceed \$100 billion, your coverage may be reduced.

The portion of your annual premium that is attributable to coverage for acts of terrorism is _____, and does not include any charges for the portion of losses covered by the United States government under the Act.

I ACKNOWLEDGE THAT I HAVE BEEN NOTIFIED THAT UNDER THE TERRORISM RISK INSURANCE ACT, AS AMENDED, ANY LOSSES RESULTING FROM CERTIFIED ACTS OF TERRORISM UNDER MY POLICY COVERAGE MAY BE PARTIALLY REIMBURSED BY THE UNITED STATES GOVERNMENT, MAY BE SUBJECT TO A \$100 BILLION CAP THAT MAY REDUCE MY COVERAGE AND I HAVE BEEN NOTIFIED OF THE PORTION OF MY PREMIUM ATTRIBUTABLE TO SUCH COVERAGE.

Policyholder/Applicant's Signature

Print Name

Date

Name of Insurer: _____

Policy Number: _____

DRAFTING NOTE: An insurer may choose not to use the acknowledgement section for workers compensation.