

TERRORISM RISK INSURANCE ACT OF 2002: OUTLINE

DURATION

- Three-year program, lasting through 2005.

SCOPE

- Program is limited to acts of international terrorism (domestic terrorism is not covered).
- Treasury Secretary determines what an “act of terrorism” is for purposes of the program – using a definition included in the legislation.
- To be covered by the program, an act must cause at least \$5 million in damages.
- Program covers workers’ compensation losses from acts of war, as well as from terrorism (this is different from other lines of coverage).

FINANCIAL STRUCTURE

- The federal government is responsible for paying 90 percent of each insurer’s primary property-casualty losses above that insurer’s annual program deductible.
- Each insurer’s annual deductible is based on a comparison of that insurer’s covered losses in that year to its direct earned premium for lines of business covered by the program in the prior year.
- The amount of each insurance company’s individual deductible (i.e., retention) scales upward each year of the program:

2002 = up to 1 percent of the prior year’s earned premium

2003 = 7 percent

2004 = 10 percent

2005 = 15 percent

- The program has an annual cap: losses in excess of \$100 billion are not covered.

POLICYHOLDER SURCHARGES

- Surcharges are mandated for any difference (gap) underneath an annual aggregate loss figure and the total amount of insurer loss payments (deductibles plus their 10 percent quota share).
- The industry aggregate loss figures used to determine whether or not there will be a surcharge are: \$10 billion in year 1, \$12.5 billion in year 2, and \$15 billion in year 3.

- Surcharges above the annual numbers, up to the program limit of \$100 billion, are at Treasury's discretion. The decision about whether to impose such surcharges would be based on economic conditions.

LINES OF INSURANCE INCLUDED IN PROGRAM

- The program only provides coverage for commercial lines of insurance, with certain specific exclusions (crop insurance, mortgage guarantee, monoline financial guaranty, medical malpractice, the national flood insurance program, life and health insurance).
- Business interruption (a portion of commercial property insurance) is fully covered.
- Surety insurance is covered.
- Excess lines are covered.
- Workers' compensation is covered – not only for terrorist acts, but also for acts of war. War is not covered for any other line of coverage.

TYPES OF INSURANCE ENTITIES INCLUDED IN PROGRAM

- All licensed primary insurers are covered, as well as surplus lines companies, state workers' compensation funds and all residual market mechanisms.
- The Treasury Secretary can extend coverage to additional captive insurance companies, as well as to self-insurers and to group life insurers.

INSURER OBLIGATIONS

- Insurers must make terrorism coverage available during the program's first two years in the following way: to the extent that a policy otherwise covers a particular type of loss, the insurer must make coverage available for that type of loss if it occurs as the result of a terrorist act.
- The insurer's "make available" obligation applies to commercial insurance policies in force on the date enactment; it also applies to new policies after that date.
- As a condition for federal reimbursement by Treasury, insurers must provide, for every covered policy, a "clear and conspicuous" notice of the federal share of compensation for terrorism losses under the Act. That notice may be in the form of a separate statement for current policies, as well as for policies issued for the first ninety days of the program. After the

ninety-day period, the notice must be part of the policy.

- If an insurer also charges a premium for terrorism coverage, it must state the amount of that premium charge on the policy.
- Customers/Policyholders can turn down the coverage.

ENFORCEMENT

- The Treasury Department has responsibility for enforcing the law, as well as administering and implementing the program, including insurer obligations for providing notices to policyholders and monitoring claims payments.

RELATIONSHIP TO STATE LAW

- State-approved exclusions for international acts of terrorism that were in effect prior to the Act's enactment are voided as soon as the law is signed. However, they may be reinstated either through an agreement between the insurer and the policyholder, or if the policyholder does not wish to pay the premium for terrorism coverage (termination of coverage for failure to pay premium is not unique to terrorism coverage).
- State authority to disapprove an insurance terrorism rate if it is excessive, inadequate or unfairly discriminatory is retained.
- State authority to make certain that insurance policy forms meet state legal requirements is retained.
- In order to for insurers to meet the Act's requirement for immediate implementation, any state law providing for prior approval of rates or forms (or time delays in implementing a rate or form) would not be applicable during the first year of the program.
- The new federal definition of "act of terrorism" pre-empts state law.

CIVIL LIABILITY

- A federal cause of action is created for all personal injury, property damage and death actions arising out of, or related to, a terrorist act.
- The federal cause of action pre-empts state causes of action.
- Federal cases would be consolidated in an appropriate federal District

Court (or courts).

- Federal funds may not be used to pay punitive damage awards.