



PAUL FRANK + COLLINS P.C.

MEMORANDUM

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To: Captive Insurance Clients and Friends of Paul Frank + Collins

From: William D. Riley, Alan D. Port, Stephanie J. Mapes and Peter J. McDougall

Re: Update on Treasury Interim Guidance Concerning Terrorism Risk Insurance Program Reauthorization Act of 2007

Date: January 3, 2008

TREASURY ISSUES INTERIM GUIDANCE CONCERNING TERRORISM RISK INSURANCE PROGRAM REAUTHORIZATION ACT OF 2007

The U.S. Treasury Department issued Interim Guidance Concerning the Terrorism Risk Insurance Program Reauthorization Act of 2007 (“TRIPRA”) on December 31, 2007. TRIPRA was signed into law by President Bush on December 26, 2007. The Interim Guidance, which is effective immediately, addresses TRIPRA’s effect on compliance issues associated with the mandatory availability and disclosure notice requirements first implemented under the Terrorism Risk Insurance Act of 2002 (“TRIA”). Although currently in draft form, Treasury has stated that the Interim Guidance “may be relied upon by the public” pending publication of the document in its final form.

In addition to extending the Terrorism Risk Insurance Program through December 31, 2014, TRIPRA contains two provisions that directly affect the mandatory availability and disclosure notice requirements of TRIA. First, TRIPRA revises the definition of the term “act of terrorism” by removing “the requirement that the act of terrorism be committed by an individual acting on behalf of any foreign person or foreign interest in order to be certified as an ‘act of terrorism’ for purposes of [TRIA].” Second, TRIPRA requires insurers to disclose to policyholders the \$100 billion cap on liability under the Program. These statutory changes are the primary subjects of

the Interim Guidance, which is available at: http://www.ustreas.gov/offices/domestic-finance/financial-institution/terrorism-insurance/pdf/interim_guidance_12312007.pdf.

A. Initial Offers of Coverage and Renewal of Existing Policies

The Interim Guidance states that “any initial offers of coverage” or “offers of renewal of existing policies” that are made on or after the date of the enactment of TRIPRA (December 26, 2007) must reflect the revised definition of the term “act of terrorism.” As before, such initial offers and renewals must provide “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.” The disclosed premium, however, “must now reflect the premium charged for insured losses,” with such “insured losses” encompassing the amended definition of “act of terrorism” as used in TRIA.

In addition to disclosing the applicable premium for terrorism coverage and the federal share of compensation, TRIPRA adds the requirement that insurers disclose to the policyholder the existence of the \$100 billion cap on liability under the Program. Under the liability cap provision, “if the aggregate insured losses exceed \$100 billion during a Program Year, Treasury shall not make any payment for any portion of the amount of such losses that exceeds \$100 billion, and no insurer that has met its deductible shall be liable for the payment of any portion of the amount of such losses that exceeds \$100 billion.” The liability cap disclosure requirement applies to any policy issued after December 26, 2007.

With respect to timing, the Interim Guidance states that “Treasury expects that all insurers will provide compliant initial and renewal offers and disclosures as quickly as possible.” Recognizing the operational difficulties that many insurers may face in meeting its requirements, the Interim Guidance goes on to state that “Treasury considers March 31, 2008, to be the latest reasonable date for compliant offers of coverage and disclosures to policyholders (including reprocessing of policies, if necessary, where a compliant post-December 26, 2007 offer and/or disclosure was not possible), barring unforeseen or unusual circumstances.” If the March 31 deadline is not met by an insurer, “Treasury will expect the insurer to demonstrate, when submitting a claim for the Federal share of compensation under the Program, why it could not comply by that date.”

Finally, where a policy renewal or application was processed in 2007 for coverage becoming effective in 2008 and the insurer did not offer terrorism coverage to the insured (perhaps by assuming that the Program would not be renewed), the Interim Guidance provides that terrorism coverage must be made available to the insured and all disclosure requirements satisfied. Treasury expects such actions to occur “as quickly as possible.”

B. Mid-Term Policies

With respect to a policy that is “mid-term as of January 1, 2008,” the Interim Guidance states that the insurer does not have to issue a new offer of coverage consistent with the revised definition of “act of terrorism” if coverage for the duration of the policy term was offered in compliance with TRIA at the time the offer was made. Similarly, a new disclosure regarding

premium is not necessary for such a policy. Nevertheless, if existing coverage for an act of terrorism does not extend for the balance of the policy term beyond December 31, 2007 (because of the operation of a policy exclusion or some other mechanism), then a new offer of coverage must be made with respect to the duration of the policy term. Furthermore, if for any reason the insurer makes a new offer of coverage during the policy term (on or after December 26, 2007), then the offer must be consistent with the make available and disclosure requirements of TRIA, as amended by TRIPRA.

C. Model Disclosure Forms

Prior to TRIPRA, Treasury allowed insurers to use NAIC Model Disclosure Forms Nos. 1 and 2 to satisfy the disclosure requirements of TRIA. The Interim Guidance continues this practice under TRIPRA. The NAIC has now updated its Model Disclosure Forms to include the changes mandated by TRIPRA. The updated forms are available at:

http://www.naic.org/documents/topics_tria_disclose1.pdf (Form No. 1: disclosure to accompany offer of terrorism coverage to the insured)

http://www.naic.org/documents/topics_tria_disclose2.pdf (Form No. 2: disclosure for policy that includes terrorism coverage)

D. Existing Policy Language

The Interim Guidance acknowledges Treasury's "understanding" that "the language in property and casualty insurance policies describing a 'certified' act of terrorism covered by TRIA and other (or 'non-certified') acts of terrorism has varied" and that "insurers have designed their insurance contracts and notifications to policyholders concerning potential changes to the certification criteria for 'acts of terrorism' differently." Despite this acknowledgement, the Interim Guidance goes on to vaguely declare that "[i]nsurers must determine how their policy language and particular circumstances are affected by the revised definition of an act of terrorism." Following this admonition, the Interim Guidance states:

The decision whether to certify an act of terrorism will be governed by the criteria in TRIA, as amended by [TRIPRA]. Treasury will consider losses resulting from an act of terrorism (as now defined in TRIA) that are covered by an insurer under a policy for property and casualty insurance to be insured losses covered by the Program, provided the insurer makes payment to the policyholder in accordance with the terms and conditions of the policy, appropriate business practices, and other applicable requirements and conditions.

This statement appears to suggest some flexibility on the part of Treasury with respect to the adequacy of language describing certification criteria in an existing policy. In our view, however, if the language of an existing policy is in any way ambiguous, the safest course of action is to issue a policy endorsement that eliminates the ambiguity.

If you have any questions regarding TRIA, TRIPRA or this memorandum, please feel free to contact William D. Riley at (802) 658-2311 or wriley@pfclaw.com. Although William Riley is our principal contact on this matter, please also feel free to contact Alan D. Port, Stephanie J. Mapes or Peter J. McDougall at (802) 658-2311 or aport@pfclaw.com, smapes@pfclaw.com and pmcdougall@pfclaw.com respectively.

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