



**ESTADO LIBRE ASOCIADO DE PUERTO RICO
OFICINA DEL COMISIONADO DE SEGURO**

February 14, 2003

RULING NO.: N-AM-2-23-2003

**TO ALL PROPERTY, CASUALTY AND SURETY INSURERS WRITING
COMMERCIAL LINES INSURANCE IN PUERTO RICO, ADVISORY AND RATING
ORGANIZATIONS, THE JOINT UNDERWRITING ASSOCIATION FOR FIRE AND
ALLIED LINES INSURANCE, AND THE COMPULSORY AUTOMOBILE LIABILITY
INSURANCE JOINT UNDERWRITING ASSOCIATION**

**Re: THE TERRORISM RISK INSURANCE ACT OF 2002
APPLICABILITY, GUIDELINES AND PROCEDURES FOR COMPLIANCE**

Dear Ladies and Gentlemen:

The President of the United States of America, George W. Bush, has signed into law, the Terrorism Risk Insurance Act of 2002 (the Act). This federal law establishes a Federal program that provides for a system of shared private and public compensation for insured losses resulting from acts of terrorism, in order to protect consumers by addressing market disruptions and ensure the continued widespread availability and affordability of property and casualty insurance for terrorism risks.

The intent of this Ruling is to advise you of certain provisions of the Act that may require insurers to submit a filing in this jurisdiction and to establish procedures that insurers must use to expedite the filing of the disclosure notices, policy language and the applicable rates that are discussed in the Act.

SCOPE OF THE ACT

This Act creates the Terrorism Insurance Program (the Program) where “insurers” are required to participate and make available “property and casualty insurance” coverage for “insured losses” that do not differ materially from the terms, amounts, and other coverage limitations applicable to losses arising from events other than acts of terrorism. The Secretary of the Treasury (the Secretary) will administer the Program and will pay the Federal share of compensation for insured losses of an insurer during the duration of the Program. The Federal share of compensation will be equal to 90% of insured losses that exceed the insurer’s deductible required during any Program Year, as established in the Act, subject to an aggregate of insured losses of \$100,000,000,000 in any Program year.

DURATION OF THE PROGRAM

The Program terminates on December 31, 2005.

DEFINITIONS

These terms have the following definitions:

- “Insurer”

Any entity and affiliate thereof:

1. that is

- (a) licensed or admitted to engage in the business of providing primary or excess insurance in any state of the United States, the District of Columbia, the Commonwealth of Puerto Rico;
- (b) an eligible surplus line carrier listed on the Quarterly Listing of Alien Insurers of the National Association of Insurance Commissioners (NAIC) or any successor thereto;
- (c) approved for the purpose of offering property and casualty insurance by a Federal agency in connection with maritime, energy, or aviation activity;
- (d) a residual market insurance entity, such as the Puerto Rico Compulsory Automobile Liability Insurance Joint Underwriting Association and the Puerto Rico Joint Underwriting Association for Fire and Allied Lines Insurance;

2. that receives direct earned premium for any type of commercial property and casualty insurance coverage.

- “Property and Casualty Insurance”

Commercial lines of property and casualty insurance, as defined in Sections 4.040 and 4.080 of the Insurance Code of Puerto Rico, including excess insurance, workers’

compensation insurance and surety insurance, as defined in Section 4.090 of the Insurance Code of Puerto Rico, but does not include:

1. crop or livestock insurance (including Federal crop insurance)
 2. private mortgage insurance
 3. financial guaranty insurance issued by monoline financial guaranty insurance corporations
 4. medical malpractice insurance
 5. health or life insurance, including group life insurance
 6. flood insurance provided under the National Flood Insurance Act of 1968
 7. reinsurance or retrocessional reinsurance
- “Act of Terrorism”

Any act certified by the Secretary, in concurrence with the Secretary of State and the Attorney General of the United States—

 1. to be an act of terrorism;
 2. to be a violent act or an act that is dangerous to:
 - (i) human life,
 - (ii) property, or
 - (iii) infrastructure;
 3. to have resulted in damage within the United States, or outside of the United States to an air carrier, a vessel bearing the United States flag or certain other vessels whose insurance coverage is subject to regulation in the United States; or at the premises of a United States mission; and
 4. to have been committed by an individual or individuals acting on behalf of any foreign person or foreign interest, 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.

An act does not qualify as an Act of Terrorism if:

 1. committed as part of the course of a war declared by Congress (except in the case of workers’ compensation coverage), or
 2. property and casualty insurance losses resulting from the act, in the aggregate, do not exceed \$5,000,000.
 - “Insured Losses”

Any loss resulting from an Act of Terrorism (including an act of war, in the case of worker’s compensation insurance) that is covered by Primary or Excess Property and

Casualty Insurance issued by an insurer, if such loss occurs within the United States, or occurs to an air carrier, to a United States flag vessel, regardless of where the loss occurs, or at the premises of any United States mission.

As a result of the definitions of Act of Terrorism and Insured Losses contained in the Act, there are essentially two distinct types of losses that a business might face resulting from terrorism. One type of loss is the Insured Loss that is defined within and covered by the provisions of the Act. For convenience, we will adopt the moniker of *certified loss* to refer to losses resulting from certified Acts of Terrorism. The second type of loss that a business might face is one that does not fit within the definition of Insured Losses, as defined. For convenience, we will adopt the moniker of *non-certified loss* to refer to losses resulting from an act of terrorism that is not certified by the Secretary. The most significant difference between these losses is that the *certified losses* will always involve a foreign person or foreign interest, while the *non-certified losses* may not.

PREEMPTION AND NULLIFICATION OF PRE-EXISTING TERRORISM EXCLUSIONS

Previous to the enactment of the Act, this Office approved terrorism exclusions endorsements for use in Puerto Rico for various commercial lines of business, which were filed by the Insurance Services Office, Inc. (ISO). These endorsements were the product of ISO's discussions with the National Association of Insurance Commissioners.

However, the Act voids any terrorism exclusion found in a property and casualty insurance contract that is in force on the date of the enactment of the Act (November 26, 2002) to the extent that it excludes losses that would otherwise be Insured Losses covered by the Act (*certified losses*). The Act also voids any state approval of any terrorism exclusion from a property and casualty insurance contract that is in force on the date of enactment of this Act to the extent that it excludes losses that would otherwise be Insured Losses covered by the Act (*certified losses*).

To this effect, the Act allows insurers to "reinstate a preexisting provision in a contract for commercial property and casualty insurance that is in force on the date of enactment of this Act and that excludes coverage" for *certified losses*, only if one of the following two conditions are met:

1. The insurer received a written statement from the insured that affirmatively authorizes such reinstatement, or
2. If the insured has failed to pay any additional premium charged by the insurer for providing such terrorism coverage and the insurer provided notice to the insured, at least 30 days before any such reinstatement, of:
 - a. the additional premium charged,
 - b. his right with respect to this coverage, and

- c. the date in which the exclusion would have been reinstated if no payment was received.

If an insurer intends to reinstate an exclusion on in-force policies, as allowed under the Act, it may only reinstate an exclusion that previously existed on the policy.

Please note that the preemption of the Puerto Rico filing statute regarding forms (Section 11.110 of the Insurance Code of Puerto Rico, 26 L.P.R.A. sec. 1110), applies only to contract language that is applicable to *certified losses*.

Regarding *non-certified losses*, we will continue to allow the same limitations included in terrorism exclusions endorsements approved by this Office previous to the enactment of the Act, which provide coverage for acts of terrorism under certain circumstances. For policies providing property insurance coverage, the following limitations would apply to *non-certified losses*:

- Exclusion for acts of terrorism only apply if the acts of terrorism result in industry-wide insured losses that exceed \$25,000,000 for related incidents that occur within a 72 hour period;
- Exclusions for acts of terrorism are not subject to the limitations above if:
 1. The act involves the use, release or escape of nuclear materials, or that directly or indirectly results in nuclear reaction or radiation or radioactive contamination;
 2. The act is carried out by means of the dispersal or application of pathogenic or poisonous biological or chemical materials; or
 3. Pathogenic or poisonous biological or chemical materials are released, and it appears that one purpose of the terrorism was to release such materials.

For policies providing liability insurance coverage, the following limitations would apply to *non-certified losses*:

- Exclusion for acts of terrorism only apply if the acts of terrorism result in industry-wide insured losses that exceed \$25,000,000 for related incidents that occur within a 72 hour period; or
- Fifty or more persons sustain death or serious physical injury for related incidents that occur within a 72 hour period. For purposes of this provision serious physical injury means:
 1. Physical injury that involves a substantial risk of death;
 2. Protracted and obvious physical disfigurement; or
 3. Protracted loss of or impairment of the function of a bodily member or organ.

- Exclusions for acts of terrorism are not subject to the limitations above if:
 1. The act involves the use, release or escape of nuclear materials, or that directly or indirectly results in nuclear reaction or radiation or radioactive contamination;
 2. The act is carried out by means of the dispersal or application of pathogenic or poisonous biological or chemical materials; or
 3. Pathogenic or poisonous biological or chemical materials are released, and it appears that one purpose of the terrorism was to release such materials.

To this effect, insurers must inform this Office if they will use, for new and renewal business, an exclusion other than that previously approved by this Office which contains the above-mentioned limitations. If the previously approved exclusions are not going to be used, exclusions for *non-certified losses* must be filed for **prior approval** to this Office.

This jurisdiction 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 established in Section 102(1)(B) of the Act, on any policy that provides coverage for *certified losses*. Insurers may submit language containing coverage limitations for *certified losses* that exceed \$100 billion.

We will accept the following definition for *non-certified act of terrorism*, or one that is more liberal to policyholders:

The phrase “non-certified act of terrorism” means a violent act or an act that is dangerous to human life, property; or infrastructure that is committed by an individual or individuals and that appears to be part of an effort to coerce a civilian population or to influence the policy or affect the conduct of any government by coercion, and the act is not certified as a terrorist act pursuant to the Federal Terrorism Risk Insurance Act of 2002.

SUBMISSION OF RATES AND POLICY FORM LANGUAGE

With regard to the filing and approval of rates and forms, Section 106(a)(2)(B) of the Act states that “during the period beginning on the date of enactment of this Act and ending on December 31, 2003, rates and forms for terrorism risk insurance coverage covered by this title and filed with any State shall not be subject to prior approval or a waiting period under any law of a State that would otherwise be applicable...”. The subsection further provides that “nothing in this title affects the ability of any State to invalidate a rate as excessive, inadequate, or unfairly discriminatory, and with respect to forms, where a State has prior approval authority, it shall apply to allow subsequent review of such forms”.

The Federal exemption is limited to prior approval of rates and forms intended to provide coverage for insured losses as defined in the Act (*certified losses*). Accordingly, the exemption does not apply to rates and forms that exclude or limit coverage for acts of terrorism not covered by the Act. However, in view that, pursuant to our Ruling No. N-AM-11-10-2001 of December 21, 2001, rate filing requirements for certain commercial lines of insurance are suspended, this Office will not be requiring rate filings for those classes, subdivisions or combinations of insurance covered by said Ruling.

In those cases where rate filing must be submitted, the insurer should provide sufficient information for us to determine what price would be charged to a business seeking to cover *certified losses*. Insurers may choose to use rating plans that take into account 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 this Office 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 to provide coverage for *certified losses* within a reasonable time after they are implemented. We will consider 30 days to be a reasonable time for purposes of completing an expedited filing of policy language. The forms should define *acts of terrorism* and both *certified* and *non-certified losses* in ways that are consistent with the Act, the Insurance Code of Puerto Rico and the guidance provided in this Ruling. The definitions, terms and conditions should be complete and accurately describe the coverage that will be provided in the policy.

DISCLOSURES AND THE EFFECT OF THE ACT ON EXISTING, NEW AND RENEWAL POLICIES

In order to be reimbursed by the Secretary for insured losses under the Program, insurers are required to provide clear and conspicuous disclosure to the policyholders of the premium charged for insured losses covered by the Program and the Federal share of compensation for insured losses under the Program. This disclosure must be provided:

1. not later than 90 days after the date of enactment of the Act, in the case of any policy that was issued before said date;
2. at the time of offer, purchase and renewal of the policy, in the case of any policy issued within 90 days of the date of enactment of the Act;
3. at the time of offer, purchase, and renewal of the policy, on a separate line item in the policy, in the case of any policy issued more than 90 days after the date of enactment of the Act. Pursuant to the Interim Guidances issued by the Secretary, Treasury deems an insurer to be in compliance with the separate line item requirement of the Act if it makes the required "clear and conspicuous" disclosure

- (i) on the declarations page of the policy, (ii) elsewhere within the policy itself, or (iii) in any rider or endorsement that is made a part of the policy.

There are disclosures required for both in-force and new and renewal business. These disclosures must be provided in all circumstances, whether terrorism coverage is included under the policy or the insured has the option to decline the terrorism coverage. Any insurer that uses the NAIC model disclosure forms, enclosed with this Ruling, as its disclosures for policies issued within 90 days from the enactment of the Act will be deemed by this Office to be in compliance with the Act. This Office requests that the disclosure notices used with policies issued more than 90 days after the enactment of the Act be submitted within 30 days period after the date they are first used. The disclosure notices are an integral part of the process for notification of policyholders and should be clear and not misleading to business owners in Puerto Rico. The disclosures should comply with the requirements of the Act and should be consistent with any policy language and rates filed or used by the insurer.

To assist the insurance industry in complying with the Act, the Department of the Treasury has issued three Interim Guidance Notices which can be found at www.treasury.gov/trip.

FORMS WITH INSTRUCTIONS

Attached to this Ruling is a uniform filing transmittal form that has been agreed upon by Puerto Rico and other jurisdictions. An insurer or advisory organization wishing to receive expedited treatment of its filing shall complete the EXPEDITED FILING TRANSMITTAL DOCUMENT—FOR TERRORISM RISK INSURANCE FORMS AND PRICING as directed. In addition, the insurer(s) or advisory organization submitting the filing must certify that the filing is consistent with this Ruling, the Insurance Code of Puerto Rico and the provisions of the Act, by signing the appropriate blank on the transmittal form. If this filing is for multiple companies, please provide a copy of the transmittal header for each company.

We hereby order all insurers to notify of the contents of this Rulings to its managers, general agents and agents.

Strict compliance with this Ruling is required.

Cordially,

Fermin M. Contreras-Gómez
Commissioner of Insurance

Enclosures