TERRORISM RISK INSURANCE EXTENSION ACT OF 2005

COMMONWEALTH OF KENTUCKY
ENVIRONMENTAL AND PUBLIC PROTECTION CABINET
OFFICE OF INSURANCE

The following Advisory Opinion is to advise the reader of the current position of the Kentucky Office of Insurance (the "Office") on the specified issue. The Advisory Opinion is not legally binding on either the Office or the reader.

Kentucky Office of Insurance
Advisory Opinion 2006-01

TO: ALL PROPERTY & CASUALTY INSURERS WRITING COMMERCIAL LINES INSURANCE PRODUCTS, and ALL INSURERS ON THE NAIC QUARTERLY LISTING OF ALIEN INSURERS.

FROM: R. GLENN JENNINGS, EXECUTIVE DIRECTOR
KENTUCKY OFFICE OF INSURANCE

RE: TERRORISM RISK INSURANCE EXTENSION ACT OF 2005

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Background

The Terrorism Risk Insurance Act of 2002 (TRIA) (The Act) was adopted by Congress to provide a temporary federal backstop for incurred losses resulting from defined acts of terrorism, to protect American businesses by minimizing market disruptions, and to ensure widespread availability and affordability of property and casualty insurance for terrorism risks. See Advisory Opinion 2002-7.

The Terrorism Risk Insurance Extension Act of 2005, signed by the President on December 22, 2005, extended the Act for an additional two years - through December 31, 2007.

This advisory opinion supplements Advisory Opinion 2002-7 and is intended 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 that are discussed in the Act. In many cases, insurers' current filings will be adequate to meet the needs of the nation's business.

Several provisions of the initial Act have changed in the extension. The changes include:
• specific inclusion of directors and officers liability insurance;
• deletion of commercial auto, burglary and theft, surety, professional liability, and farm owners multiple peril coverages from eligible lines;
• increase in the individual company deductible for 2006 to 17.5 percent and the 2007 deductible to 20 percent;

• increase in the industry aggregate retention level from $15 billion to $25 billion in 2006 and to $27.5 billion in 2007;
• reduction in the federal share of compensation for covered losses from 90 percent to 85 percent for 2007;
• maintaining the $5 million threshold for certification of a terrorist act, while establishing a per event trigger for federal participation in aggregate insured losses of $50 million for losses occurring after March 31, 2006 and before January 1, 2007 and $100 million for losses occurring in the 2007 Program Year;
• extension of existing litigation management provisions and codification of regulations requiring submission and approval of proposed settlements; and
• directing the President's Working Group on Financial Markets to study long-term availability and affordability of coverage for terrorism losses, including group life and nuclear, biological, chemical and radiological events. The Working Group, in consultation with representatives of the National Association of Insurance Commissioners, the insurance and securities industries and policyholders, is directed to submit a report of its findings to the House Financial Services and Senate Banking Committees by September 30, 2006.

Definition amended by the Terrorism Risk Insurance Extension Act of 2005

Subsection 102(12) of the Act states that the term "property and casualty insurance"
(A) means commercial lines of property and casualty insurance, including
• excess insurance,
• workers' compensation insurance, and
• directors and officers liability insurance, and
(B) does not include
• crop or livestock insurance,
• private mortgage or title insurance,
• financial guaranty insurance issued by monoline financial guaranty insurance corporations,
• medical malpractice,
• health or life insurance, including group life,
• flood insurance provided under the National Flood Insurance Act,
• reinsurance or retrocessional reinsurance,
• commercial automobile insurance,
• burglary and theft insurance,
• surety insurance,
• professional liability insurance, or
• farm owners multiple peril insurance.

All insurers, as defined in the Act in Section 102(6), continue to be required to participate in the Terrorism Insurance Program (the Program) and to make available coverage for "insured losses" in all of their covered commercial lines policies.

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. 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. Kentucky 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 and both certified and non-certified losses in ways that are consistent with the Act, state law and the guidance provided in this advisory opinion. 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, Kentucky law and the requirements of this advisory opinion.

Kentucky has not required disclosure notices be filed along with the policy forms, rates and rating systems; but as disclosure notices are an integral part of the process for notification of policyholders in this state, the notices should be clear and not misleading to business owners in this state. The disclosures should comply with the requirements of the Act and should be consistent with the policy language and rates filed by the insurer.

Filings

All filings should follow the procedures set forth in 806 KAR 13:150 and 806 KAR 14:006 and in the checklists available on our Web site, **http://insurance.ky.gov/kentucky**.

Effective Date

This advisory opinion shall take immediate effect and shall expire on December 31, 2007, unless Congress extends the duration of the Act. This Advisory Opinion, the statutes, administrative regulations, and forms are available on the Kentucky Office of Insurance website, **http://insurance.ky.gov/kentucky**. Any questions should be directed to Robin Coombs, Assistant Director, Property & Casualty Division at (502) 564-3630 x 4294 or **Robin.Coombs@ky.gov**.

/s/ R. Glenn Jennings

R. Glenn Jennings, Executive Director

Kentucky Office of Insurance

January 18, 2006