McKenna Long & Aldridge LLP
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Information Advisory

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The Terrorism Risk Insurance Act of 2002

The Terrorism Risk Insurance Act of 2002 ("the Act") was signed into law on November 26, 2002. In short, the Act creates a federal program under which the federal government will be responsible for 90% (up to $100 billion) of insurance industry losses arising from future terrorism acts that exceed certain specified amounts. The Act has important implications for all corporate policyholders, and also raises a number of yet unanswered questions.

The most immediate effect of the Act is that all terrorism exclusions in commercial property and liability policies are null and void as of November 26, 2002 -- the date the Act was signed into law. Though the Act mandates that insurers provide some form of terrorism coverage, the Act does not require that insurers provide coverage for all types of terrorism risks. Insurers are required only to make available coverage for acts of terrorism (as defined in the Act) that does not "differ materially" from the terms, amounts and other coverage limitations offered to policyholders for non-terrorism-related losses. According to interim guidance issued by the Department of Treasury, "if an insurer does not cover all types of risks . . . (*e.g.,* nuclear, biological, or chemical events) an insurer would not be required to make such coverage available."

Policyholders should review carefully their current policies to determine what types of terrorism losses may or may not be covered under such policies in the absence of any explicit terrorism exclusions. Be aware that even prior to the implementation of the terrorism exclusion drafted in the aftermath of 9-11, insurers were arguing that many types of terrorism risks were not covered under standard commercial property and liability policies.

Insurers are permitted under the Act to charge an increased premium for coverage without a terrorism exclusion. By February 26, 2003 (many insurers will likely do so much sooner), insurers must notify policyholders of the amount of any such additional premium. A policyholder must pay the additional premium within 30 days to avoid reinstatement of terrorism exclusions in its policies. Policyholders may opt to retain a terrorism exclusion and not pay any additional premium. The decision, though, will have to be made relatively quickly. Complicating matters, the premiums will depend upon the insurer, type of policy and nature of the policyholder's business and locations, and are likely to be quite divergent particularly over the next few months while the market for terrorism coverage stabilizes. Currently, there is no limit on the amount of premiums that may be charged.

Policyholders also are likely to see new language or forms providing some measure of terrorism coverage. The Insurance Services Office ("ISO") recently announced that it has filed new forms, containing "standardized" terrorism coverage, with all state insurance regulators. Policyholders should scrutinize any new coverage forms or language to ensure that the forms provide adequate protection for their own risks. Through December 31, 2002, state approval of new forms and rates is waived, making it even more important that policyholders carefully review any new language.

Among the questions that must still be answered are: the extent to which the Act applies to offshore markets, like those in Bermuda, and/or to policyholder owned captives; will premiums be returned for stand-alone terrorism policies purchased by companies after the terrorism exclusion was inserted into their standard policies; to what extent do pre-existing exclusions preclude coverage for terrorism losses.

Contact Information

McKenna Long & Aldridge's Insurance Recovery Group, which counsels and represents policyholders in insurance matters, is closely following rapidly occurring developments under the Act, and is available to address any questions you may have about this topic. For more information, please contact Matt Schlesinger (202-496-7651 or mschlesinger@mckennalong.com), Andrew Reidy (202 496-7741 or areidy@mckennalong.com), or Murray Sacks (202 496-7137 or msacks@mckennalong.com).

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