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DEPARTMENT OF THE TREASURY

31 CFR Part 50

RIN 1505–AB66

Terrorism Risk Insurance Program; TRIA Extension Act Implementation

AGENCY: Departmental Offices, Treasury.

ACTION: Interim final rule.

SUMMARY: The Department of the Treasury (Treasury) is issuing this interim final rule as part of its implementation of amendments made to Title I of the Terrorism Risk Insurance Act of 2002 (TRIA, or Act) by the Terrorism Risk Insurance Extension Act of 2005 (Extension Act). The Act established a temporary Terrorism Risk Insurance Program (Program) that was scheduled to expire on December 31, 2005, under which the Federal Government shared the risk of insured losses from certified acts of terrorism with commercial property and casualty insurers. The Extension Act extends the Program through December 31, 2007, and makes other changes which are implemented by this rule. In particular, the rule addresses changes to the types of commercial property and casualty insurance covered by the Act, the requirements to satisfy the Act’s mandatory availability (“make available”) provision and the operation of the new “Program Trigger” provision in section 103(e)(1)(B) of the Act. Published elsewhere in this issue of the **Federal Register** is a notice of proposed rulemaking that proposes to adopt as a final rule the provisions of this interim final rule.

DATES: This interim final rule is effective [**insert date of publication in the Federal Register**]. To submit comments, please refer to the notice of proposed rulemaking published elsewhere in this issue of the **Federal Register**. Comments may be submitted on or before [**insert 30 days after publication in the Federal Register**].

FOR FURTHER INFORMATION CONTACT: Howard Leikin, Deputy Director, or David Brummond, Legal Counsel, Terrorism Risk Insurance Program (202) 622-6770 (not a toll-free number).

SUPPLEMENTARY INFORMATION:

I. Background

A. Terrorism Risk Insurance Act of 2002.

On November 26, 2002, the President signed into law the Terrorism Risk Insurance Act of 2002 (Pub. L. 107-297, 116 Stat. 2322). The Act was effective immediately. The Act's purposes are to address market disruptions, ensure the continued widespread availability and affordability of commercial property and casualty insurance for terrorism risk, and to allow for a transition period for the private markets to stabilize and build capacity while preserving State insurance regulation and consumer protections.

Title I of the Act establishes a temporary federal program of shared public and private compensation for insured commercial property and casualty losses resulting from an act of terrorism which, as defined by the Act, is certified by the Secretary of the Treasury, in concurrence with the Secretary of State and the Attorney General. The Act authorizes Treasury to administer and implement the Terrorism Risk Insurance Program (the Program), including the issuance of regulations and procedures.

Each entity that meets the Act's definition of insurer (well over 2000 firms) must participate in the Program. The amount of federal payment for an insured loss resulting from an act of terrorism is determined by insurance company deductibles and excess loss sharing with the Federal Government as specified in the Act and Treasury's implementing regulations. An insurer's deductible increases each year of the Program, thereby reducing the Federal Government's share of compensation for insured losses each year until the Program expires. An insurer's deductible is calculated based on the value of direct earned premiums collected over certain prescribed calendar periods. Once an insurer has met its individual deductible, the federal payments cover a percentage of the insured losses above the deductible, subject to an industry aggregate limit of \$100 billion.

The Act gives Treasury authority to recoup federal payments made under the Program through policyholder surcharges, up to a maximum annual limit. The Act reduces the Federal share of compensation for insured losses that have been covered under any other federal program. The Act also contains provisions designed to manage litigation arising from or relating to a certified act of terrorism. Section 107 of the Act creates an exclusive federal cause of action, provides for claims consolidation in federal court, and contains a prohibition on federal payments for punitive damages under the Program. The Act provides the United States with the right of subrogation with respect to any payment or claim paid by the United States under the Program.

B. Terrorism Risk Insurance Extension Act of 2005.

The Program was originally set to expire on December 31, 2005. On December 22, 2005, the President signed into law the Terrorism Risk Insurance Extension Act of 2005 (Pub. L. 109-144, 119 Stat. 2660), which extends the Program through December 31, 2007. In doing so, the Extension Act adds Program Year 4 (January 1 – December 31, 2006) and Program Year 5 (January 1 – December 31, 2007) to the Program. In addition, the Extension Act made other significant changes to TRIA that include:

- A revised definition of insurer deductible that adds new Program Years 4 and 5 to the definition. The insurer deductible is set as the value of an insurer's direct earned premium for commercial property and casualty insurance (as now defined in the Act) over the immediately preceding calendar year multiplied by 17.5 percent for Program Year 4 and 20 percent for Program Year 5.
- A revised definition of property and casualty insurance that now excludes commercial automobile insurance; burglary and theft insurance; surety insurance; professional liability insurance; and farmowners multiple peril insurance. Though the definition excludes professional liability insurance, it explicitly retains directors and officers liability insurance.
- Creation of a new Program Trigger for any certified act of terrorism occurring after March 31, 2006, that prohibits payment of Federal compensation by Treasury unless the aggregate industry insured losses resulting from that act of terrorism exceed \$50 million for Program Year 4 and \$100 million for Program Year 5.
- A change to the Federal share of compensation for insured losses. Subject to the Program Trigger, the Federal share is 90 percent of that portion of the amount of insured losses that exceeds the applicable insurer deductible in Program Year 4 and decreases to 85 percent of such amount in Program Year 5.
- Revisions to the recoupment provisions. For purposes of recouping the Federal share of compensation under the Act, the insurance marketplace aggregate retention amount for the two additional years of the Program is increased from the level in Program Year 3. For Program Year 4 the insurance marketplace aggregate retention amount is established as the lesser of \$25 billion and the aggregate amount, for all insurers, of insured losses during Program Year 4. The insurance marketplace aggregate retention amount for Program Year 5 is the lesser of \$27.5 billion and the aggregate amount, for all insurers, of insured losses during Program Year 5.

- A statutory codification of Treasury’s litigation management regulatory requirements in section 50.82 of title 31 of the Code of Federal Regulations (as in effect on July 28, 2004), which requires advance approval by Treasury of proposed settlements of certain causes of action involving insured losses under the Program.

C. Previously Issued Interim Guidance

To assist insurers, policyholders, and other interested parties in complying with immediately applicable requirements of the Extension Act, on December 29, 2005 Treasury issued and posted interim guidance on its website. A Notice containing that interim guidance (Interim Guidance IV) was published in the Federal Register on January 5, 2006 (71 FR 648). The notice stated that the guidance could be relied upon by insurers in complying with new statutory requirements prior to the issuance of regulations, but was not the exclusive means of compliance. The interim guidance is superseded by this interim final rule.

II. Analysis of the Interim Final Rule

This interim final rule incorporates certain changes to 31 CFR Part 50 required by the amendments to TRIA in the Extension Act, which extended the Terrorism Risk Insurance Program by two years, to December 31, 2007. The changes in the rules include new insurer deductible amounts for each of those Program Years, the extension of mandatory availability requirements, the deletion of certain types of insurance from the definition of property and casualty insurance, and a continued safe harbor for the use of model disclosure forms. The interim final rule also incorporates and clarifies statutory changes to the determination of the Federal share of compensation, taking into account the new Program Trigger. The interim final rule generally incorporates interim guidance previously issued by Treasury, except as described in this preamble. Treasury has consulted with the National Association of Insurance Commissioners in developing this rule.

Although Treasury is issuing these requirements as an interim final rule, we are soliciting comments on all aspects of the interim final rule from all interested parties. Published elsewhere in a separate part of this issue of the **Federal Register** is a notice of proposed rulemaking proposing to adopt the provisions of this interim final rule as a final rule.

A. Definitions (§50.5)

The interim final rule incorporates revised definitions for insurer deductible, Program Years, and property and casualty insurance. The rule also adds definitions for professional liability insurance and Program Trigger event.

The revisions to the definitions for insurer deductible and Program Years are straightforward changes based on the Extension Act. They implement that Act's addition of Program Years 4 (calendar year 2006) and 5 (calendar year 2007) and the percentages to be applied to an insurer's direct earned premium for the immediately preceding calendar year in computing insurer deductibles for Program Year 4 (17.5 percent) and Program Year 5 (20 percent).

Section 102(12) of TRIA was also amended to exclude additional types of insurance from the definition of property and casualty insurance under the Program. The Act now excludes from the definition commercial automobile insurance, burglary and theft insurance, surety insurance, professional liability insurance, and farmowners multiple peril insurance. To the extent the newly excluded types of insurance represent specific lines of business on the NAIC Annual Statement, Treasury is continuing to utilize NAIC line of business definitions in implementing the Act. The newly excluded types of insurance which may correspond to lines of business on the NAIC Annual Statement are: Line 3 – Farmowners Multiple Peril; Line 19.3 – Commercial Auto No-Fault (personal injury protection); Line 19.4 – Other Commercial Auto Liability; Line 21.2 – Commercial Auto Physical Damage; Line 26 – Burglary and Theft; and Line 24 – Surety. In addition, the interim final rule makes clear that these types of insurance are excluded from the definition of property casualty insurance, regardless of how their premiums may be reported.

The only type of insurance that is newly excluded from the definition of property and casualty insurance in the Act, but is not a specific line of business on the NAIC Annual Statement, is contained in new subsection 102(12)(xi) of TRIA – professional liability insurance. In this interim final rule, Treasury is providing the following definition of “professional liability insurance”:

Professional liability insurance means insurance coverage for liability arising out of the performance of professional or business duties related to a specific occupation, with coverage being tailored to the needs of the specific occupation. Examples include abstracters, accountants, insurance adjusters, architects, engineers, insurance agents and brokers, lawyers, real estate agents, stockbrokers and veterinarians. For purposes of this definition, professional liability insurance does not include directors and officers liability insurance.

Insurers are to use this definition in identifying policies excluded from the Program, as well as for determining which policies have premiums that should be subtracted from Line 17 – Other Liability on the NAIC Annual Statement when computing direct earned premium for Program purposes.

This definition is derived from the definition of “Professional Errors and Omissions Liability” found in the Uniform Property & Casualty Coding Matrix currently utilized by the System for Electronic Rate and Form Filing (SERFF) sponsored by the National Association of Insurance Commissioners (NAIC).¹ However, this definition is

¹ The Matrix can be found on the NAIC website at http://www.naic.org/industry_home.htm.

not meant to limit insurers to the filing code (17.0019) specified under SERFF for “Professional Errors and Omissions Liability”. Certainly, policies and coverages that employ the SERFF filing code will meet the interim final rule definition of professional liability insurance. Treasury acknowledges that many insurers and insurance support organizations do not utilize the SERFF mechanism for all their form filings. Thus, the definition in the interim final rule is intended to have a broader application than the SERFF filing process and should not be viewed as limited to one particular SERFF filing code.

Directors and officers liability insurance, which is sometimes considered a type of professional liability insurance, is not included in the definition of professional liability insurance. Section 102(12)(A) of the Act now explicitly includes directors and officers liability insurance in the definition of property and casualty insurance. This change does not substantively modify the previous definition of property and casualty insurance under the Act, but is a statutory clarification that directors and officers liability insurance is distinct from professional liability insurance. Premium for directors and officers liability insurance may be already included in Line 17 – Other Liability on the NAIC Annual Statement, one of the commercial lines of business listed in Treasury’s current regulations defining property and casualty insurance (31 C.F.R. 50.5(l)), if not otherwise excluded. Treasury recommends that insurers consult the definition of “Directors & Officers Liability” found in the Uniform Property & Casualty Coding Matrix now being utilized by SERFF if further guidance is needed on what constitutes “Directors & Officers Liability” insurance.

The Extension Act revision to TRIA section 102(12) specifically excludes “farm owners multiple peril insurance”, a particular type of insurance which is also a specific line of business on the NAIC Annual Statement, from the definition of property and casualty insurance. Insurers have asked whether monoline farm insurance coverages are similarly excluded. There is no clear guidance in the legislative history of the Extension Act on this issue. Based on the plain meaning of the statute, Treasury believes it is appropriate to interpret this exclusion as applicable only to *multiple peril* coverages insuring farm risks. Single peril or monoline coverages insuring farm risks would continue to meet the Act’s definition of property and casualty insurance. Treasury notes that the premiums for such policies are usually reported, or otherwise allocated, to one of the commercial lines of insurance on the NAIC Annual Statement (or an equivalent reporting system) listed in the definition of property and casualty insurance in Treasury’s regulations.

Treasury is aware of some concerns with this result on the part of some smaller insurance entities, such as farm and county mutuals. With this in mind, Treasury requests that any comments on this issue focus on the practical implications of this issue and articulate a basis for any assertion that monoline coverages are excluded from the Program as part of the farmowners multiple peril exclusion.

The Extension Act adds a new section 103(e)(1)(B) to TRIA entitled “Program Trigger.” This new provision directs the Secretary not to compensate insurers under the

Program unless the aggregate industry insured losses from a certified act of terrorism exceed certain insured loss or “trigger” amounts.² To implement this provision, the interim final rule adds a new definition for “Program Trigger event”. Such an event is a certified act of terrorism that occurs after March 31, 2006, for which the aggregate industry insured losses resulting from such act exceed \$50 million if occurring in 2006 or \$100 million if occurring in 2007.”

The new Program Trigger provision applies only to acts of terrorism that occur after March 31, 2006. Note that the application of the Program Trigger is based on the date of occurrence and not the date of certification of an act of terrorism. For example, the Program Trigger provision shall *not* apply to an act that occurs prior to March 31, 2006, but which is certified after March 31. After March 31, unless an act of terrorism is a Program Trigger event, insured losses from that act of terrorism will not be considered in any determination of or calculation leading to any Federal share of compensation under the Act. For a further discussion of the Program Trigger, see “*E. Federal Share of Compensation*” below.

B. Interim Guidance Safe Harbors (§50.7)

Section 50.7 of the current regulations provides that “[a]n insurer will be deemed to be in compliance with the requirements of the Act to the extent the insurer reasonably relied on Interim Guidance prior to the effective date of applicable regulations.” The interim final rule adds “Interim Guidance IV issued by Treasury on December 29, 2005, and published at 71 FR 648 (January 5, 2006)” to the list of applicable Interim Guidance.

C. Disclosure (§§50.12 and 50.17)

The interim final rule incorporates guidance on compliance with disclosure requirements and revised safe harbor language with regard to the use of NAIC model disclosure forms.

The Extension Act retains, as a condition for federal payments under the Act, the existing requirements contained in section 103(b) to provide clear and conspicuous disclosure to policyholders of the premium charged for insured losses covered by the Program and of the Federal share of compensation for insured losses under the Program. These disclosures must be made “at the time of offer, purchase, and renewal of the policy”. Treasury is aware of certain operational difficulties some insurers faced with regard to policies processed in the latter part of Program Year 3 (2005) for issuance or renewal effective in 2006. In some cases policies were issued or renewed in 2006 in a form that already included coverage for terrorism risks regardless whether TRIA was

² Section 103(e)(1)(B) states: “In the case of a certified act of terrorism occurring after March 31, 2006, no compensation shall be paid by the Secretary under subsection (a), unless the aggregate industry insured losses resulting from such certified act of terrorism exceed – (i) \$50,000,000, with respect to such insured losses occurring in Program Year 4; or (ii) \$100,000,000, with respect to such insured losses occurring in Program Year 5.”

extended. Because TRIA would have ended on December 31, 2005, disclosures were not provided with these policies.

The Extension Act made no change to the requirement that disclosures are required as a condition for payment of the Federal share of compensation for insured losses. However, given the late date of enactment of the Extension Act, the interim final rule provides in section 50.12(e) that “[i]f an insurer made available coverage for insured losses in a new policy or policy renewal in Program Year 3 for coverage becoming effective in Program Year 4, but did not provide a disclosure at the time of offer, purchase or renewal, then the insurer must be able to demonstrate to Treasury’s satisfaction that it has provided a disclosure as soon as possible following January 1, 2006.” Treasury anticipates that these insurers will already have provided the disclosures by the time this rule is published.

For an insurer to demonstrate to Treasury’s satisfaction that it has provided disclosures as soon as possible following January 1, 2006, Treasury will expect an insurer to have provided disclosures by 30 days after publication of this interim final rule in the **Federal Register**, barring unforeseen or unusual circumstances. If not completed by that time, an insurer will be expected, when submitting a claim for the Federal share of compensation, to clearly demonstrate why such disclosures could not be made by that date and why the insurer should be deemed to be in compliance with the Act’s disclosure requirement.

Pursuant to 31 CFR 50.17, insurers that have used NAIC Model Disclosure Forms that were in existence on April 18, 2003, were deemed to satisfy the disclosure requirements of section 103(b)(2) of the Act. Although the Extension Act made no change to the TRIA disclosure requirements, revisions were made to the Act that required rewording of the NAIC Model Disclosure Forms. The NAIC has since issued revised Model Disclosure Forms, dated January 26, 2006, which if used by insurers, will be deemed to satisfy disclosure requirements of the Act and Treasury regulations. The interim final rule continues the safe harbor approach for use of the most current NAIC Model Disclosure forms deemed by Treasury to meet Program requirements. Insurers may also continue to use other forms to comply with the disclosure requirements.

D. Make Available (§§50.20 and 50.21)

For Program Year 4 (Calendar 2006) and Program Year 5 (Calendar 2007) insurers are required to continue to “make available” coverage for insured losses as required by TRIA and Treasury regulations. Amendments to the “make available” requirement in section 103(c) of the Act are simply conforming amendments that continue the requirements through Program Years 4 and 5. Thus, insurers issuing or renewing commercial property and casualty insurance policies in Program Years 4 and 5 must continue to offer coverage for insured losses resulting from an act of terrorism, as required by section 103(c) of the Act and 31 CFR 50.20 to 50.24 if they wish to have their insured loss claims eligible for the Federal share of compensation in the extended Program Years.

In its Interim Guidance IV issued on December 29, 2005, Treasury addressed “make available” requirements with regard to the transition from Program Year 3, originally the last year of the Program, to the extended Program Years 4 and 5. In that issuance, Treasury noted that the Extension Act made no changes to the “make available” requirement for insurers. Treasury provided guidance on how insurers could comply with Program requirements given operational difficulties arising from the Extension Act passage late in the year.

Treasury clarified that no additional “make available” offer is required if terrorism coverage for the duration of the policy term was offered for policies issued or renewed in 2005. No additional action is required because the “make available” provision of section 103(c) of the Act and 31 CFR 50.20 to 50.24 has been satisfied for coverage periods extending into Program Year 4. For example, policies with “conditional” terrorism coverage exclusions that do not arise or become effective on or after January 1 are policies in which the terrorism coverage portion continues to cover insured losses within the meaning of the Act. In such situations, no additional action is required for insurers to remain in compliance with the Act’s “make available” provision until the time of policy renewal.

Treasury also provided guidance as to how an insurer could comply with “make available” requirements under three scenarios where:

- (1) a policy did not provide terrorism coverage after December 31, 2005, but the policyholder had rejected an offer of terrorism coverage for the portion of the policy term up to December 31,
- (2) a policy’s terrorism coverage expired on December 31, 2005, but the remainder of the policy continued in force in 2006, and
- (3) a policy renewal or application was processed in 2005 for coverage becoming effective in 2006 and the insurer did not “make available” terrorism coverage for Program Year 4 as contemplated by the Extension Act.

In the case of scenario (1) above, Treasury advised that an insurer was not required to make another offer of coverage for the remainder of the policy term. In the other two scenarios, Treasury advised insurers that TRIA as extended requires them to make offers of terrorism coverage for the policy terms continuing or beginning in Program Year 4 (2006). However, Treasury recognized the late date of passage of the Extension Act and the administrative difficulties this posed for some insurers who otherwise had complied with the “make available” provision in 2005. Treasury said it expected all insurers to make a good faith effort to provide policyholders whose terrorism coverage expired as of January 1 with a new offer of terrorism coverage along with the appropriate disclosures by January 1, 2006, or as quickly as possible following that date. In this regard, Treasury stated it considered January 31, 2006, to be the latest reasonable date for offers of coverage to midterm policyholders, barring unforeseen or unusual circumstances. If the January 31 date was not met by an insurer, Treasury indicated it would expect the insurer to explain any delay as well as its good faith efforts when

submitting a claim for the Federal share of compensation under the Program. In its discretion, Treasury would determine whether good faith efforts to comply had been made.

The interim final rule generally incorporates the foregoing guidance into the TRIA “make available” provisions. Section 50.21(b) has been added to address the special Program Year 4 requirements for scenarios (1) and (2) above. For scenarios (2) and (3), where an insurer must make an offer of coverage, section 50.21(d) (formerly 50.21(c)) has been amended to provide that the insurer must be able to demonstrate to Treasury’s satisfaction that it has provided an offer of coverage for insured losses by January 1, 2006, or as soon as possible following that date. In demonstrating to Treasury’s satisfaction that it has provided an offer of coverage for insured losses as soon as possible after January 1, 2006, Treasury considers January 31, 2006, to be the latest reasonable date for offers of coverage, barring unforeseen or unusual circumstances. If not provided by January 31, 2006, Treasury would expect an insurer to demonstrate why the offer could not be made by that date when submitting a claim for Federal compensation under the Program.

The interim final rule incorporates technical amendments to section 50.20 that extend the “make available” requirements into Program Years 4 and 5. Section 50.20(c) also provides that “property and casualty insurance coverage for insured losses does not have to be made available beyond December 31, 2007 (the last day of Program Year 5), even if the policy period of insurance coverage for losses from events other than acts of terrorism extends beyond that date”.

As a result of the Extension Act’s deletion of certain types of insurance from the definition of property and casualty insurance, some uncertainty has arisen regarding the “make available” and disclosure requirements for excess or umbrella liability policies. As a general rule, excess or umbrella liability policies are property and casualty insurance within the meaning of TRIA. Section 102(12)(A) of the Act defines the term “property and casualty insurance” as meaning commercial lines of property and casualty insurance “including excess,” unless otherwise excluded from the definition under Section 102(12)(B). Premiums for commercial excess and umbrella insurance policies are normally reported on Line 17 – Other Liability in the NAIC Annual Statement.³ Nonetheless, excess or umbrella insurance is commercial property and casualty insurance included in the Program only to the extent it provides coverage above primary or underlying coverage that is a type of insurance included in the Program. Thus, if an excess or umbrella policy provides an upper layer of coverage for a type of insurance specifically excluded from the Program (*e.g.*, commercial auto, professional liability, medical malpractice), the excess or umbrella liability policy is also excluded.

Additional uncertainty has arisen with respect to excess or umbrella liability policies to the extent that the underlying policies they cover may include types of insurance that are both included and excluded from the Act’s definition of property and casualty insurance. For example, an excess or umbrella liability policy might cover both

³ See 68 FR 59725 (October 17, 2003).

an underlying professional liability policy (generally excluded from the Program) as well as underlying general liability policy (generally included in the Program). In such cases, the treatment of these hybrid excess and umbrella policies follows the same analysis as the treatment of hybrid policies generally under existing Treasury regulations.⁴

Thus, where the included commercial property and casualty coverage segment of an excess or umbrella liability policy is merely incidental to the remaining excluded coverage under the policy, an insurer may treat the entire policy as not providing property and casualty insurance within the meaning of TRIA and Treasury's regulations.⁵ In such circumstances, the TRIA "make available" and disclosure requirements will not apply and no losses from the commercial coverage segment of the policy will be paid by Treasury.

E. Federal Share of Compensation (§50.50)

The interim final rule adds several provisions to section 50.50 to reflect the addition of the new Program Trigger provision to the Act. Under section 103(a) of TRIA, the Secretary is required to pay the Federal share of compensation for insured losses in accordance with section 103(e) of the Act. The Extension Act amended subsection (e) to provide, in part, that no compensation shall be paid by the Secretary under subsection (a) unless the aggregate industry insured losses from a certified act of terrorism occurring after March 31, 2006, exceed certain amounts. This provision was intended to ensure that there would be no Federal compensation unless the aggregate industry losses from an act of terrorism exceed these amounts.

The interim final rule incorporates a technical amendment to renumbered section 50.50(a) (formerly 50.50(d)) to provide that the Federal share of compensation in Program Year 5 shall be "85 percent of that portion of the insurer's aggregate insured losses that exceed its insurer deductible during Program Year 5," (subject to any adjustments in section 50.51 and the cap of \$100 billion as provided in section 103(e)(2) of the Act). A new provision has also been added to renumbered section 50.50(d) (formerly 50.50(a)) that reiterates, as a condition for Federal compensation for insured losses, a basic insurance principle that, "[t]he insurer offered the coverage for insured losses and the offer was accepted by the insured prior to the occurrence of the loss".

New section 50.50(b) incorporates the Program Trigger limitations on the amount of Federal compensation payable under the Act. To implement these limitations, section 50.50(g) states that Treasury will determine the amount of aggregate industry insured losses, and that if the aggregate industry insured losses exceed the applicable Program Trigger amounts, Treasury will publish notice in the **Federal Register** that the act of terrorism is a Program Trigger event. As noted in the previously issued Interim

⁴ See 31 CFR §50.5(d) (1)(iii) and (iv); 68 FR 41256 – 41258 (July 11, 2003).

⁵ See 31 CFR § 50.5(d)(1)(iii): "For purposes of the Program, commercial coverage combined with coverages that otherwise do not meet the definition of property and casualty insurance is incidental if less than 25 percent of the total direct premium is for such coverage."

Guidance, Treasury also expects to provide notification through press releases and postings on the TRIP web site.

Consistent with Treasury's Interim Guidance, section 50.50(c) clarifies that in the provisions dealing with claims procedures, Subpart F, insured losses or aggregate insured losses for acts of terrorism after March 31, 2006, will be limited to those insured losses resulting from Program Trigger events. This limitation on insured losses controls any determinations of, or calculations leading to, a Federal share of compensation under the Act including any adjustments of the Federal share, and applies to submissions of an insurer in conjunction with Initial Notices of Loss and Certifications of Loss and payments of the Federal share.

As Treasury indicated in its Interim Guidance, the Program Trigger provision also has a direct bearing on which insured losses count towards satisfaction of the insurer deductible. In Program Year 4, for example, for certified acts of terrorism occurring after March 31, only an insurer's insured losses resulting from Program Trigger events will count towards satisfaction of the insurer deductible for that year. Similarly, in Program Year 5, only an insurer's insured losses resulting from Program Trigger events in that year will count towards satisfaction of the insurer deductible.

F. Determination of Affiliations (§50.55)

Section 50.55 provides that for the purposes of claims procedures and the determination of the Federal share of compensation "an insurer's affiliates for any Program Year shall be determined by the circumstances existing on the date of occurrence of the act of terrorism that is the first act of terrorism in a Program Year to be certified by the Secretary for that Program Year." The purpose of this regulation, when promulgated in 2005, was to clarify the point in time when insurer affiliations would be determined in order to facilitate the calculation of insurer deductibles and the payments of the Federal share of compensation for Program Years in which affiliations could change over time. Since this has meaning only if there is a potential Federal share of compensation, the interim final rule incorporates an amendment clarifying that if the first certified act of terrorism occurs after March 31, 2006, it must also be a Program Trigger event to be used for determining affiliations under the rule.

G. Federal Cause of Action; Approval of Settlements

The Extension Act added section 107(a)(6) to TRIA, which provides that procedures and requirements established by the Secretary under 31 CFR 50.82, as in effect on the date of issuance of that section in final form [July 28, 2004], shall apply to any Federal cause of action described in section 107(a)(1). This provision has been added to new section 50.85.

Section 50.82 of the regulations requires insurers to submit to Treasury for advance approval certain proposed settlements involving an insured loss, any part of the payment of which the insurer intends to submit as part of its claim for federal payment

under the Program. Thus, Treasury would not expect insurers to submit any proposed settlement if the insured losses would not be eligible for payment, as would be the case if the losses resulted from a post-March 31, 2006 certified act that was not a Program Trigger event. However, if there is uncertainty whether or not a certified act will become a Program Trigger event, an insurer may wish to err on the side of caution and submit a proposed settlement for prior approval in order to preserve any subsequent eligibility for Federal compensation for insured losses under the Program. Otherwise the insured losses will be ineligible for later payment if the Program Trigger is reached.

III. Procedural Requirements

The Extension Act extended the TRIA Program, which provides for loss sharing payments by the Federal Government for insured losses resulting from certified acts of terrorism. The Act's extension became effective immediately upon the date of enactment (December 22, 2005). Changes in the Extension Act applied immediately to those entities that come within the Act's definition of "insurer".

The Extension Act revised the definition of property and casualty insurance to exclude certain types of insurance previously covered under the Program. The Extension Act also added a Program Trigger provision limiting the Federal compensation for certified acts of terrorism after March 31, 2006, unless the aggregate industry losses exceed certain amounts. These provisions, which go to the scope of the Program and the conditions for payments by the Federal Government, resulted in the need to provide immediate guidance to insurers, policyholders, and regulators. In addition, extension of the disclosure requirements and the "make available" requirements to policies currently in effect in late December 2005 raised transition issues that need to be addressed immediately. Given the significance of these changes made by the Extension Act, there is a need to issue immediately effective regulations that incorporate and clarify these requirements.

Accordingly, pursuant to 5 U.S.C. 553(b)(B), Treasury has determined that it would be contrary to the public interest to delay issuance of this interim final rule. For the same reasons, pursuant to 5 U.S.C. 553(d)(3), Treasury has determined that there is good cause for this interim final rule to become effective immediately upon publication. While this rule is effective immediately upon publication, Treasury is seeking public comment and will consider all comments in developing a final rule. This interim final rule is a significant regulatory action and has been reviewed by the Office of Management and Budget under the terms of Executive Order 12866. For applicability of the Regulatory Flexibility Act (5 U.S.C. chapter 6), refer to the notice of proposed rulemaking published elsewhere in this issue of the **Federal Register**. However, the Act and the Program are intended to provide benefits to the U.S. economy and all businesses, including small businesses, by providing a federal reinsurance backstop to commercial property and casualty policyholders and spreading the risk of insured loss resulting from an act of terrorism.

List of Subjects in 31 CFR Part 50

Terrorism risk insurance.

Authority and Issuance

For the reasons set forth above, Subparts A, B, C, F, and I of 31 CFR Part 50 are amended as follows:

PART 50 – TERRORISM RISK INSURANCE PROGRAM

1. The authority citation for 31 CFR Part 50 is revised to read as follows:

Authority: 5 U.S.C. 301; 31 U.S.C. 321; Title I, Pub. L. 107-297, 116 Stat. 2322 (15 U.S.C. 6701 note), as amended by Pub. L. 109-144, 119 Stat. 2660 (15 U.S.C. 6701 note).

2. Section 50.1(a) of Subpart A is revised to read as follows:

Subpart A --- General Provisions

§ 50.1 Authority, purpose and scope.

(a) **Authority.** This Part is issued pursuant to authority in Title I of the Terrorism Risk Insurance Act of 2002, Pub. L. 107–297, 116 Stat. 2322, as amended by the Terrorism Risk Insurance Extension Act of 2005, Pub. L. 109-144, 119 Stat. 2660.

* * * * *

3. Section 50.5 is amended as follows:

- a. Paragraph (g) is revised.
- b. Paragraphs (j) through (p) are redesignated as paragraphs (k), (m), (n), (o), (p), (q), and (r), respectively.
- c. New paragraphs (j) and (l) are added.
- d. Newly designated paragraphs (m) and (n) are revised.

The revisions and additions read as follows:

§ 50.5 Definitions.

* * * * *

(g) *Insurer deductible* means:

(1) For an insurer that has had a full year of operations during the calendar year immediately preceding the applicable Program Year:

(i) For the Transition Period (November 26, 2002 through December 31, 2002), the value of an insurer's direct earned premiums over calendar 2001, multiplied by 1 percent;

(ii) For Program Year 1 (January 1, 2003 through December 31, 2003), the value of an insurer's direct earned premiums over calendar year 2002, multiplied by 7 percent;

(iii) For Program Year 2 (January 1, 2004 through December 31, 2004), the value of an insurer's direct earned premiums over calendar year 2003, multiplied by 10 percent;

(iv) For Program Year 3 (January 1, 2005 through December 31, 2005), the value of an insurer's direct earned premiums over calendar year 2004, multiplied by 15 percent;

(v) For Program Year 4 (January 1, 2006 through December 31, 2006), the value of an insurer's direct earned premiums over calendar year 2005, multiplied by 17.5 percent;

(vi) For Program Year 5 (January 1, 2007 through December 31, 2007), the value of an insurer's direct earned premiums over calendar year 2006, multiplied by 20 percent; and

(2) For an insurer that has not had a full year of operations during the calendar year immediately preceding the applicable Program Year, the insurer deductible will be based on data for direct earned premiums for the applicable Program Year multiplied by the specified percentage for the insurer deductible for the applicable Program Year. If the insurer does not have a full year of operations during the applicable Program Year, the direct earned premiums for the applicable Program Year will be annualized to determine the insurer deductible.

* * * * *

(j) *Professional liability insurance* means insurance coverage for liability arising out of the performance of professional or business duties related to a specific occupation, with coverage being tailored to the needs of the specific occupation. Examples include abstracters, accountants, insurance adjusters, architects, engineers, insurance agents and brokers, lawyers, real estate agents, stockbrokers

and veterinarians. For purposes of this definition, professional liability insurance does not include directors and officers liability insurance.

* * * * *

(l) *Program Trigger event* means a certified act of terrorism that occurs after March 31, 2006, for which the aggregate industry insured losses resulting from such act exceed \$50 million with respect to such insured losses occurring in 2006 or \$100 million with respect to such insured losses occurring in 2007.

(m) *Program Years* means the Transition Period (November 26, 2002 through December 31, 2002), Program Year 1 (January 1, 2003 through December 31, 2003), Program Year 2 (January 1, 2004 through December 31, 2004), Program Year 3 (January 1, 2005 through December 31, 2005), Program Year 4 (January 1, 2006 through December 31, 2006), and Program Year 5 (January 1, 2007 through December 31, 2007).

(n) *Property and casualty insurance* means commercial lines of property and casualty insurance, including excess insurance, workers' compensation insurance, and directors and officers liability insurance, and

(1) Means commercial lines within only the following lines of insurance from the NAIC's Exhibit of Premiums and Losses (commonly known as Statutory Page 14): Line 1—Fire; Line 2.1—Allied Lines; Line 5.1—Commercial Multiple Peril (non-liability portion); Line 5.2—Commercial Multiple Peril (liability portion); Line 8—Ocean Marine; Line 9—Inland Marine; Line 16—Workers' Compensation; Line 17—Other Liability; Line 18—Products Liability; Line 22—Aircraft (all perils); and Line 27—Boiler and Machinery; and

(2) Does not include:

(i) Federal crop insurance issued or reinsured under the Federal Crop Insurance Act (7 U.S.C. 1501 *et seq.*), or any other type of crop or livestock insurance that is privately issued or reinsured (including crop insurance reported under either Line 2.1—Allied Lines or Line 2.2—Multiple Peril (Crop) of the NAIC's Exhibit of Premiums and Losses (commonly known as Statutory Page 14);

(ii) Private mortgage insurance (as defined in section 2 of the Homeowners Protection Act of 1988) (12 U.S.C. 4901) or title insurance;

(iii) Financial guaranty insurance issued by monoline financial guaranty insurance corporations;

- (iv) Insurance for medical malpractice;
- (v) Health or life insurance, including group life insurance;
- (vi) Flood insurance provided under the National Flood Insurance Act of 1968 (42 U.S.C. 4001 *et seq.*) or earthquake insurance reported under Line 12 of the NAIC's Exhibit of Premiums and Losses (commonly known as Statutory Page 14);
- (vii) Reinsurance or retrocessional reinsurance;
- (viii) Commercial automobile insurance, including insurance reported under Lines 19.3 (Commercial Auto No-Fault (personal injury protection)), 19.4 (Other Commercial Auto Liability) and 21.2 (Commercial Auto Physical Damage) of the NAIC's Exhibit of Premiums and Losses (commonly known as Statutory Page 14);
- (ix) Burglary and theft insurance, including insurance reported under Line 26 (Burglary and Theft) of the NAIC's Exhibit of Premiums and Losses (commonly known as Statutory Page 14);
- (x) Surety insurance, including insurance reported under Line 24 (Surety) of the NAIC's Exhibit of Premiums and Losses (commonly known as Statutory Page 14);
- (xi) Professional liability insurance as defined in section 50.5(j); or
- (xii) Farmowners multiple peril insurance, including insurance reported under Line 3 (Farmowners Multiple Peril) of the NAIC's Exhibit of Premiums and Losses (commonly known as Statutory Page 14).

* * * * *

4. Section 50.7 of Subpart A is revised to read as follows:

§ 50.7 Special Rules for Interim Guidance Safe Harbors.

(a) An insurer will be deemed to be in compliance with the requirements of the Act to the extent the insurer reasonably relied on Interim Guidance prior to the effective date of applicable regulations.

(b) For purposes of this section, Interim Guidance means the following documents, which are also available from the Department of the Treasury at <http://www.treasury.gov/trip>:

(1) Interim Guidance I issued by Treasury on December 3, 2002, and published at 67 FR 76206 (December 11, 2002);

(2) Interim Guidance II issued by Treasury on December 18, 2002, and published at 67 FR 78864 (December 26, 2002);

(3) Interim Guidance III issued by Treasury on January 22, 2003, and published at 68 FR 4544 (January 29, 2003); and

(4) Interim Guidance IV issued by Treasury on December 29, 2005, and published at 71 FR 648 (January 5, 2006).

5. Section 50.10(d) of Subpart B is revised to read as follows:

Subpart B—Disclosures as Conditions for Federal Payment

§ 50.10 General disclosure requirements.

* * * * *

(d) *Policies issued more than 90 days after the date of enactment.* For policies issued on or after February 25, 2003, the disclosure required by the Act must be made on a separate line item in the policy, at the time of offer, purchase, and renewal of the policy. For policies issued in late 2005 with coverage extending into 2006, see § 50.12(e)(2).

6. Section 50.12(e) of Subpart B is revised to read as follows

§ 50.12 Clear and conspicuous disclosure.

* * * * *

(e) *Demonstration of compliance.* (1) An insurer may demonstrate that it has satisfied the requirement to provide clear and conspicuous disclosure as described in §50.10 through use of appropriate systems and normal business practices that demonstrate a practice of compliance.

(2) If an insurer made available coverage for insured losses in a new policy or policy renewal in Program Year 3 for coverage becoming effective in Program Year 4, but did not provide a disclosure at the time of offer, purchase or renewal, then the insurer must be able to demonstrate to Treasury’s satisfaction that it has provided a disclosure as soon as possible following January 1, 2006.

* * * * *

7. Section 50.17(e) of Subpart B is revised to read as follows:

§ 50.17 Use of model forms.

* * * * *

(e) *Definitions.* For purposes of this section, references to NAIC Model Disclosure Form No. 1 and NAIC Model Disclosure Form No. 2 refer to such forms as were in existence on April 18, 2003, or as subsequently modified by the NAIC, provided Treasury has stated that usage by insurers of the subsequently modified forms is deemed to satisfy the disclosure requirements of the Act and the insurer uses the most current forms that are available at the time of disclosure. These forms may be found on the Treasury Web site at <http://www.treasury.gov/trip>.

8. Sections 50.20 and 50.21 of Subpart C are revised to read as follows:

Subpart C—Mandatory Availability

§ 50.20 General mandatory availability requirements.

(a) *Transition Period and Program Years 1 and 2—period ending December 31, 2004.* Under section 103(c) of the Act (unless the time is extended by the Secretary as provided in that section) during the period beginning on November 26, 2002 and ending on December 31, 2004 (the last day of Program Year 2), an insurer must:

(1) Make available, in all of its property and casualty insurance policies, coverage for insured losses; and

(2) Make available property and casualty insurance coverage for insured losses that does not differ materially from the terms, amounts, and other coverage limitations applicable to losses arising from events other than acts of terrorism.

(b) *Program Year 3—calendar year 2005.* In accordance with the determination of the Secretary announced June 18, 2004, an insurer must comply with paragraphs (a)(1) and (a)(2) of this section during Program Year 3.

(c) *Program Years 4 and 5 – calendar years 2006 and 2007.* Under section 103(c) of the Act, an insurer must comply with paragraphs (a)(1) and (a)(2) of this section during Program Years 4 and 5. Notwithstanding paragraph (a)(2) of this section and §50.23(a), property and casualty insurance coverage for insured losses does not have to be made available beyond December 31, 2007 (the last day of Program Year 5) even if the policy period of insurance coverage for losses from events other than acts of terrorism extends beyond that date.

§ 50.21 Make available.

(a) *General.* The requirement to make available coverage as provided in §50.20 applies to policies in existence on November 26, 2002, new policies issued and renewals of existing policies during the period beginning on November 26, 2002 and ending on December 31, 2004 (the last day of Program Year 2), and to new policies issued and renewals of existing policies in Program Years 3 through 5 (calendar years 2005 through 2007). Except as provided in paragraph (b) of this section, the requirement applies at the time an insurer makes the initial offer of coverage as well as at the time an insurer makes an initial offer of renewal of an existing policy.

(b) *Special Program Year 4 requirement for certain new policies issued and renewals of existing policies in Program Year 3.* If coverage for insured losses under a policy of property and casualty insurance (as defined by the Act, as amended) expired as of December 31, 2005, but the remainder of coverage under the policy continued in force in Program Year 4, then an insurer must make available coverage as provided in §50.20 for insured losses for the remaining portion of the policy term in the manner specified in paragraphs (d)(1) and (d)(2) of this section. This requirement does not apply if during Program Year 3 a policyholder declined an offer of coverage for insured losses made at the time of the initial offer of coverage or offer of renewal of the existing policy.

(c) *Changes negotiated subsequent to initial offer.* If an insurer satisfies the requirement to “make available” coverage as described in §50.20 by first making an offer with coverage for insured losses that does not differ materially from the terms, amounts, and other coverage limitations applicable to losses arising from events other than acts of terrorism, which the policyholder declines, the insurer may negotiate with the policyholder an option of partial coverage for insured losses at a lower amount of coverage if permitted by any applicable State law. An insurer is not required by the Act to offer partial coverage if the policyholder declines full coverage. See §50.24.

(d) *Demonstrations of compliance.*

(1) If an insurer makes an offer of insurance but no contract of insurance is concluded, the insurer may demonstrate that it has satisfied the requirement to make available coverage as described in §50.20 through use of appropriate systems and normal business practices that demonstrate a practice of compliance.

(2) If an insurer must make available coverage for insured losses as required by paragraph (b) of this section for a policy whose coverage period began in Program Year 3 but extends into Program Year 4, then the insurer must be able to demonstrate to Treasury’s satisfaction that it has offered such coverage by January 1, 2006, or as soon as possible following that date.

(3) If an insurer processed a new policy or policy renewal in Program Year 3 for coverage becoming effective in Program Year 4, but did not make available coverage for insured losses as required by §50.20 by January 1, 2006, then the insurer must be able to demonstrate to Treasury’s satisfaction that it has provided an offer of coverage for insured losses as soon as possible following that date.

* * * * *

9. Section 50.50 of Subpart F is revised to read as follows:

Subpart F—Claims Procedures

§ 50.50 Federal share of compensation.

(a) *General.* The Treasury will pay the Federal share of compensation for insured losses as provided in section 103 of the Act once a Certification of Loss required by §50.53 is deemed sufficient. The Federal share of compensation under the Program shall be:

(1) 90 percent of that portion of the insurer's aggregate insured losses that exceed its insurer deductible during each Program Year through Program Year 4, and

(2) 85 percent of that portion of the insurer's aggregate insured losses that exceed its insurer deductible during Program Year 5,

both subject to any adjustments in §50.51 and the cap of \$100 billion as provided in section 103(e)(2) of the Act.

(b) *Program Trigger amounts.* Notwithstanding paragraph (a) or anything in this Subpart to the contrary, no Federal share of compensation will be paid by Treasury unless the aggregate industry insured losses resulting from a certified act of terrorism occurring after March 31, 2006 exceed the following amounts:

(1) For a certified act of terrorism occurring after March 31, 2006 and before January 1, 2007: \$50 million;

(2) For a certified act of terrorism occurring in calendar year 2007: \$100 million.

(c) *Insured losses after March 31, 2006.* For all purposes of subpart F, insured loss or insured losses or aggregate insured losses resulting from acts of terrorism after March 31, 2006 shall be limited to those insured losses resulting from Program Trigger events.

(d) *Conditions for payment of Federal share.* Subject to paragraph (e) of this section, Treasury shall pay the appropriate amount of the Federal share of compensation to an insurer upon a determination that:

(1) The insurer is an entity, including an affiliate thereof, that meets the requirements of §50.5(f);

(2) The insurer's insured losses, as defined in §50.5(e) and limited by §50.50(c) (including the allocated dollar value of the insurer's proportionate share of insured losses from a State residual market insurance entity or State workers'

compensation fund as described in §50.35), have exceeded its insurer deductible as defined in §50.5(g);

(3) The insurer has paid or is prepared to pay an underlying insured loss, based on a filed claim for the insured loss;

(4) Neither the insurer's claim for Federal payment nor any underlying claim for an insured loss is fraudulent, collusive, made in bad faith, dishonest or otherwise designed to circumvent the purposes of the Act and regulations;

(5) The insurer had provided a clear and conspicuous disclosure as required by §§50.10 through 50.19;

(6) The insurer offered coverage for insured losses and the offer was accepted by the insured prior to the occurrence of the loss;

(7) The insurer took all steps reasonably necessary to properly and carefully investigate the underlying insured loss and otherwise processed the underlying insured loss using appropriate insurance business practices;

(8) The insured losses submitted for payment are within the scope of coverage issued by the insurer under the terms and conditions of the policies for commercial property and casualty insurance as defined in §50.5(n); and

(9) The procedures specified in this Subpart have been followed and all conditions for payment have been met.

(e) *Adjustments.* Treasury may subsequently adjust, including requiring repayment of, any payment made under paragraph (d) of this section in accordance with its authority under the Act.

(f) *Suspension of payment for other insured losses.* Upon a determination by Treasury that an insurer has failed to meet any of the requirements for payment specified in paragraph (d) of this section for a particular insured loss, Treasury may suspend payment of the Federal share of compensation for all other insured losses of the insurer pending investigation and audit of the insurer's insured losses.

(g) *Aggregate industry losses.* Treasury will determine the amount of aggregate industry insured losses resulting from a certified act of terrorism. If such aggregate industry insured losses exceed the applicable Program Trigger amounts specified in paragraph (b) of this section, Treasury will publish notice in the Federal Register that the act of terrorism is a Program Trigger event.

10. Section 50.55 of Subpart F is revised to read as follows:

§ 50.55 Determination of Affiliations.

For the purposes of subpart F, an insurer's affiliates for any Program Year shall be determined by the circumstances existing on the date of occurrence of the act of terrorism that is the first act of terrorism in a Program Year to be certified by the Secretary for that Program Year. Provided, however, if such act of terrorism occurs after March 31, 2006, the act of terrorism must also be a Program Trigger event to determine affiliations as provided in this section.

11. A new section 50.85 is added to Subpart I as follows:

§ 50.85 Amendment related to settlement approval.

Section 107(a)(6) of the Act, added December 22, 2005, provides that procedures and requirements established by the Secretary under section 50.82 of part 50 of title 31 of the Code of Federal Regulations (as in effect on the date of issuance of that section in final form) shall apply to any cause of action described in section 107(a)(1) of the Act.

Dated: May 4, 2006.

Emil W. Henry, Jr.

Assistant Secretary of the Treasury.