

FAQs

These FAQs are now divided into general sections for ease of use. If you do not find what you are looking for, or would like to contribute, please use the Ask WordingsPLUS page on our website.

We welcome all comments.

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Q1. On reinsurance risks, is an original policy reference sufficient to identify the original wording?

No, without sight of the original wording the underwriter cannot be perfectly clear about conditions contained therein and how they affect the contract that the underwriter is contemplating.

The point of carrying out PBQA checks is to ensure that the contract is clear and unambiguous in its terms and conditions in the expectation of reducing costs from disputed claims or under-priced contracts. A contract where all terms, including those incorporated from an original, underlying or primary policy, are made available and are known to underwriters and reinsureds alike, is less likely to perform poorly in the future.

Current guidance to the effect that an original reference number, often merely the broker slip number or details of the parties/ limits/ interest and situation, is not sufficient in this regard as it merely identifies details of an underlying placement, whereas the whole point is to identify in full the details of an underlying contract document.

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Q2. A slip states that the original policy contains “inter alia”, the following clauses and conditions”. Is this sufficient to identify the original wording?

No. The slip must contain either a copy of the original wording or, if it based on a standard market wording, full details of any amendments made to that wording, together with fully referenced or attached additional clauses. The term “inter alia”, given its literal meaning “amongst others” has the potential to include additional clauses and coverages unknown to the underwriter and broker at the time of placement. Any such contract cannot be regarded as clear and unambiguous or pass any PBQA test.

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Q3. A reinsurance slip contains the condition “War Clause as original.” Is this acceptable, given that on facilities and treaty reinsurances, the underwriter may not have the opportunity to assess every wording that is issued by the original insured during the period of risk?

No. We would advocate that a standard market exclusion wording is applied by the reinsuring underwriter on any such facility in respect of war, radioactive contamination and similar perils. For example, the standard war clause in the London Non-Marine market is NMA 464 which in addition to war excludes invasion, act of foreign enemy, hostilities or war-like operations (whether war be declared or not), civil war, rebellion, revolution, insurrection, civil commotion, martial law, riot or the act of any lawfully constituted authority. However, we have seen clauses on local policies which exclude war and civil war only and in doing so widen underwriters’ exposure. The application of a recognised exclusion will bring the necessary certainty.

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Q4. The underwriter has written “TBE” in his underwriting stamp. Is the risk contract certain?

Yes. Provided that the underwriter has not physically deleted his syndicate number and pseudonym (or member company number in the case of IUA risks), this merely means that his own internal reference has yet to be allocated before appropriate documentation can be issued by the broker

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Q5. The leading underwriter has inserted the comment “DPM 2000 wording to apply until final manuscript wording agreed”. Can this be regarded as contract certain with regard to following underwriters?

No. Whilst the responsibility for the agreement of the wording lies with the leading underwriter, any following underwriter should be aware of the wording to be finally agreed and has the right to request a copy. In this instance, contract certainty is not achieved for the subscribing market unless they reinforce the leader's subjectivity in ascertaining the exact nature and issuance date of the final contract wording.

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Q6. Crystal informs me that certain taxes must be shown under the appropriate heading in the Market Reform Contract as payable by Insurers but the local intermediary has already collected these. Do I therefore still have to show them in the Market Reform Contract?

Yes, but in order to avoid the possibility of the tax being collected a second time by underwriters, the slip should also clearly annotate that these have already been collected locally.

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Q7. Can an expiring wording be used on an insurance or reinsurance placement until a final version is issued for the current period of insurance?

Yes, but the underwriter or broker should impose a condition within the slip making this clear and ideally stating a deadline for agreement of the current year's wording. The expiring wording itself should also be attached to the slip for agreement.

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Q8. When can the term "Amended" be used in the Market Reform Contract in respect of a wording?

If this term is to be used, the precise nature of any amendments made to a given wording or clause must either be specified in full or the amended version of the wording attached to the slip for agreement by underwriters. The only time when the term may otherwise be used is to refer to a lodged wording or wording issued by an approved market body where this word has been used in the title or reference number.

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Q9. A reinsurance slip has been placed where the fronting company has yet to be agreed. Can the reinsured be shown as "To be agreed" until such time as the fronting company is in place?

No. Almost invariably a fronting company is required because direct insurance is prohibited within the country in question. However, a slip which does not identify the contractual parties cannot be regarded as a valid contract of insurance and can only commence from the date on which the fronting company has agreed its participation in the reinsurance.

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Q10. The wording attached to the Market Reform Contract does not contain a Schedule page. Is it sufficient for the purposes of the contract document?

If the wording itself refers to the inclusion of a Schedule page, it should be attached. If this is not the case, the Market Reform Contract must contain any information referred to as included within the wording itself and should be checked thoroughly to ensure that terminology and coverage match appropriately.

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Q11. Is there any advantage in showing a policy jacket reference on Market Reform Contracts where a policy is subsequently to be issued?

Even though there is no specific check for this in the QA tool, if a policy is required to be signed by Xchanging (Folkestone or Chatham) on a policy wording which does not have its own jacket, then a policy jacket reference must be shown on the slip. This is because there is a choice of policy jackets available. A jacket reference on the slip also assists with compliance with QA Tool Check 9_000265 regarding fraud clauses as the majority of jackets contain a fraud clause.

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Q12. What is an Interlocking Clause?

Interlocking clauses may be applicable to one individual placement or to a series of policies.

On individual placements, in the event of a loss occurrence for which coverage is afforded under more than one section of a multi-section policy, an Interlocking Clause states that the limit of indemnity or liability shall not exceed a certain specified amount, notwithstanding the individual limits stated as being applicable in respect of each section. It also provides for the application of one specified deductible amount in the event of multi-section losses. This type of clause is commonly used within the Financial Institutions market.

An Interlocking Clause may also be used on a placement where a series of other policies are in effect. In this case it will state that where a loss occurrence involves more than one insured, policy or contract period, the total of the loss applicable to that placement will be the amount that its limit (and retention where applicable) bears to the total of all losses under the series of policies.

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Q13. What is the difference between Losses Occurring and Claims Made bases of cover?

Policy Wordings on a *losses occurring* basis cover liabilities arising from the activities of a business which occur during a specified period of insurance, whether notified to insurers during or subsequent to that period. A losses occurring wording effectively provides “open ended” cover for events occurring during the policy period, thus providing the Insured with a measure of comfort inasmuch that they will know that they are covered for a claim falling within the scope of the policy coverage no matter when the notification is made. For this reason, United Kingdom law requires compulsory Employers’ Liability insurance to be on a losses occurring basis.

Policy Wordings, on a *claims made* basis, however, provide cover only for incidents that are notified to insurers during the period of insurance and an insurer may decline to accept new claims notifications after this period. This basis of insurance gives no guarantee of cover in respect of late notification. For example, personal injury claims could be notified years after the incident in question making this type of coverage one where a detailed understanding of the implications of the wording are necessary.

An insured wishing to transfer coverage for this reason from a claims made basis to a losses occurring basis might be advised to include a retroactive extension for the past period in order to address potential claims which have yet to be notified or identified.

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Q14. What is Outside Directorship cover?

Directors today frequently sit on more than one board. Outside Directorship Liability (commonly known as ODL) provides coverage for individual firm members under the terms of a Directors' and Officers' Liability policy whilst holding officer and/or director positions with entities outside the company insured by the policy wording. Coverage is automatically provided for non-profit organisations and for other organisations if specifically scheduled within the policy wording.

Coverage is specifically in excess of any other insurance and/or indemnity available to the individual firm member by reason of their holding the Outside Directorship and applies where the entity outside the company insured or other legal entity is not required or permitted to indemnify the individual firm member.

Additionally, the coverage does not extend indemnity to the outside company or legal entity in which the Outside Directorship is held, or to any other director, officer or employee of that outside company or legal entity but applies as personal coverage of the individual firm member holding the Outside Directorship.

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Q15. Arbitration and Mediation, how do they differ?

An arbitration procedure involves an independent and impartial third party assessing both sides in a dispute privately (rather than publicly) and formulating a method of resolving it. Such arbitration hearings are thus less formal than court hearings with some forms of arbitration being decided upon the basis of documentation only. In many ways, arbitration is an alternative form of court with set procedural rules (such as disclosure of evidence and documentation) governing the issues involved.

The decision of the arbitrator (usually comprising three parties – the chairing party having the casting vote) is usually legally binding on both sides, a more formal subsequent court decision being denied in the event of either party being unhappy with the final decision.

Mediation involves an independent third party working directly with the parties to resolve the disputed issue. The parties decide the terms of the agreement, not the mediator. The most important duty of the mediator is to check and assess that in reality the parties are able to perform the measures decided to resolve the dispute is issue.

Mediation is now very widely recognised in the European Community as the most popular form of alternative dispute resolution as it offers resolutions to a disputed issue quite beyond those within the measure of a court to impose. Its use is increasing in negligence, commercial and personal injury disputes.

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Q16. What is meant by "Day One" Reinstatement?

This method of reinstatement is ultimately concerned with inflation protection.

It may be very difficult to predict the effects of inflation over the timescale needed to rebuild a property. To alleviate this position, a policy may provide cover on a Day One Reinstatement Basis. This allows a given percentage of increase (which must realistically be in line with building costs in order to avoid the possibility of underinsurance) in the declared value of a building which will be available during the period of time from the date of the damage until reinstatement of that building has been completed.

The "Day One" basis is usually applied to commercial buildings and is not the method normally used for the insurance of residential property. Additionally, this basis of insurance will assume that all the necessary works of reinstatement can be performed at the building costs in force at "Day One" of the insurance in force. This is clearly impracticable and such building costs need to be adjusted for applicable rises in prices and other factors such as delays due to obtaining tenders, planning and listed building consents, as well as delays during demolition and rebuilding costs.

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Q17. Subrogation, what is it and how does it work?

Subrogation is the right of an insurer who has indemnified an insured party to take over any legal rights that party may have had in respect of the particular claim, whether already enforced or not.

Under this principle, the insured party is not entitled to receive more than indemnity – their doing so would result in their being in profit and the whole concept of insurance would be undermined. Equally, it would be totally unjust for the Insurer to be in a position where they were able to recover more than the claim payment.

Under subrogation, the insurer acquires the right to use the insured party's name to proceed against any third party who was responsible for causing the loss and to claim from the insured party any sums received by way of compensation from that third party.

Subrogation additionally permits a party who discharges the debt of another to step into the shoes of the party originally entitled to that security. In consequence, the party discharging the debt may be subrogated to any security on which the original debt was secured.

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Q18. What is a Sunset Clause?

A sunset clause is a provision in a liability policy which states that the insurer will respond only to losses reported before a predetermined future date (the "Sunset Date"), being usually a specified time after the expiration of the policy.

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Q19. Extended Reporting Period, what is it and how does it work?

An Extended Reporting Period is the period of time after the expiration of a claims made basis liability coverage policy during which claims may be made.

In order for coverage to be activated under an Extended Reporting Provision, the following conditions must normally be satisfied:

- a) The wrongful act or omission must have occurred during the time the insurance was in force and after the retroactive date. There is no coverage for acts or omissions that occur during the Extended Reporting Period.
- b) The claim must be first made and reported during the Extended Reporting Period.

The Extended Reporting Period applies for a limited and specified period of time. In the case of the majority of professional liability insurances, this period will vary from one to three years and is not renewable and the extended period specifically does not reinstate limits of indemnity, those from the main policy period being those available to the insured party.

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Q20. What is a Contingent Liability?

Contingent liabilities are possible future liabilities that will only become certain on the occurrence of some future event. A contingent liability is less certain than a provision since the latter is quite expected to occur, but a contingent liability only *might* occur.

Examples of contingent liabilities include guarantees and the results of legal disputes, outstanding lawsuits, guarantees and indemnities, environmental cleanup costs, acquisition cost in a merger, with regards to a calculated level of goodwill.

Contingent liabilities may never become actual liabilities. They may, however, be of a significant enough level to have an impact on assets or valuations.

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Q21. “Coinsurance” can have different meanings, what are they?

Internationally, the term may refer to either of the following situations:

- (a) where two or more insurers underwrite the same risk with several liability such that each insurer is not bound to follow the decisions of any co-insurer unless it has specifically agreed to do so.
- (b) where the insured acts as its own insurer for a given proportion of the sum insured.

In specifically US terms: -

a) in property insurance, coinsurance is a penalty imposed on the insured party by the insurance carrier for under reporting/declaring/insuring the value of tangible property or business income, such penalty being based on a percentage stated within the policy and the amount under-reported.

b) in health insurance, coinsurance determines how the insurer and insured will share the costs of an amount that exceeds the excess or deductible up to the policy's limit of liability. It is usually indicated a percentage amount with the insurer's proportion stated first. The maximum percentage for which the insured will be responsible does not usually exceed fifty percent. Once the insured's out of pocket expenses equal the limit of liability, the insurer will assume responsibility for 100% of any additional costs.

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Q22. What is the difference between a Marine Cargo and a Freight Forwarder's Cover?

A Marine Cargo cover affords coverage arising from physical loss or damage to cargo in an Insured's custody, care or control as it moves from place to place under an approved contract. It can include transit by air, sea or land and can encompass an Insured's own vehicles and transits through the mail services.

In addition to the above, a Freight Forwarder's Cover may typically include legal liability for:-

- loss or damage to customers' equipment.
- consequential loss following loss or damage to customers' equipment.
- mis-delivery of cargo.
- delays in delivery of cargo.
- general average and salvage which cannot be recovered from a customer.
- fines, duties and the like for unintentional breaches of regulations relating to cargo, immigration, pollution or work safety conditions.
- bodily injury or physical loss or damage to third party property resulting from an accident whilst directly performing the insured service.
- sudden & accidental pollution & clean up costs.
- the costs of defending and mitigating claims made under the policy.

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Q23. What is meant by the terms Inward and Outward Reinsurance?

Inwards reinsurance is that accepted by a Lloyd's syndicate or other insurance carrier. Outwards reinsurance is that ceded by an insurer to other insurers or reinsurers.

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Q24. What is meant by the terms Proportional and Non-Proportional Reinsurance?

In Proportional Reinsurance, coverage is provided to the reinsured for only a percentage or portion of the risk or loss from the reinsurer. The proportion of coverage is most commonly based on the percentage of premiums paid to the reinsurer. If, for example, the reinsured pays 75% of such premiums to the reinsurer, then the reinsured recovers 75% of its losses when it reimburses the original policyholder in accordance with the terms of the original policy. The reinsured may accordingly only recover that portion of its total loss and not the entire amount.

Non-Proportional Reinsurance provides coverage for a set amount of loss. A deductible or base amount is specified in the reinsurance policy, and any loss exceeding that amount is paid by the reinsurer, this amount bearing no relationship to the premiums received as in Proportional reinsurance. The reinsured is therefore effectively reimbursed for all payments

made under the original policy that exceed the deductible amount. These coverages can be used in both treaty and facultative contracts.

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Q25. What is meant by the term Quota Share Reinsurance?

Quota Share Reinsurance requires an insurer to transfer, and for the reinsurer to accept, a certain specified percentage of every risk with a defined class of business written by that insurer. If the Quota Share amount is 45%, for instance, the insurer transfers 45% of its liabilities and premium on every written risk to the reinsurer, who is consequently bound to pay 45% of any partial or total loss sustained.

The direct insurer, however, is likely to have greater expenses than the reinsurer, acquisition cost of the business being the most notable of these and it is usual for the reinsurance premium to be offset by an amount of reinsurance commission passing from the reinsurer to the cedant.

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Q26. What is a Cut-Through Clause?

This clause is a provision in a reinsurance agreement which states that, should the original insurer become insolvent, the reinsurer will still be liable for its specified share of any loss but payment will be made directly to the original insured and not, as customarily is the case, to the original insurer.

Cut-Through Clauses are increasingly used in joint public/private partnership ventures (PPPs). For Lenders and Operators, this is intended to act as a comfort factor with regard to a local insurer's credit worthiness, although these clauses do not create privity of contract between reinsurers and Lenders/ Operators and, with regard to local insurers, these clauses may conceivably be in violation of local insolvency rules.

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Q27. Does a facultative reinsurance Market Reform Contract require separate headings for both original and reinsurance conditions?

Whilst it may be deemed acceptable by market bodies for the original policy reference to be specified for contract certainty purposes, (here we would refer you to Question 1 in this

series), it is essential that underwriters know, in the immediate absence of an original wording, the basic terms and conditions applicable to the original insurance. Reinsurance conditions are often at best merely shown under Information and are often missed altogether. The use of headings for both original and reinsurance conditions aids clarity and helps to avoid misunderstandings. They also allow underwriters to assess the scope of their own reinsurance cover and permit differences between the two to be clearly shown i.e. original policy grants Worldwide coverage but that applicable to the reinsurance is limited to Worldwide excluding USA and Canada. Whilst not a requirement, their use is all but essential.

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Q28. What is the meaning of the term Constructive Total Loss?

Constructive Total Loss (CTL) is a situation where there is not an actual total loss but where (a) the property insured is damaged to the extent where its restoration is totally beyond economic repair or (b) in the case of perishable goods, an actual total loss looks to be unavoidable. In the case of a CTL, the insured may abandon the property to the insurer by giving them a formal Notice of Abandonment, which entitles the insurer to assume all rights to that property.

The Marine Insurance Act (1906) defines a Constructive Total Loss as one where “the subject matter insured is reasonably abandoned on account of its actual total loss appearing to be unavoidable, or because it could not be preserved from actual total loss without an expenditure which would exceed its value when the expenditure had been incurred.”

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Q29. What is the difference between a Deductible (or Excess) and a Franchise?

A Deductible (or Excess) amount is the monetary amount of the loss that is payable by the insured before the insurer becomes responsible for an indemnity or reimbursement.

A Franchise, whilst not in such common current use, is a specified monetary amount of loss that must be reached before insurers will reimburse any losses and, once losses reach or exceed such amount, insurers will reimburse the insured for the total amount of loss. If, for example, an insurance was subject to a Franchise of £500 in respect of each and every loss, a loss of GBP 450 would be entirely sustained by the insured but a loss of GBP 550 would be entirely reimbursed by insurers.

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Q30. What is a Grace Period?

This is a period of time (usually 30 or 31 days) specified in an insurance contract during which a late payment may be made without the imposition of a specific penalty. Should the payment not be made by the end of the Grace Period, insurers have the right to suspend the contract.

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Q31. What is meant by Non-Vitiation?

A Non –Vitiation (or Multiple Insureds) Clause is used in policies where the Insured comprises more than one insured party, each operating as a separate entity. It provides coverage for each of these parties in the same manner as if individual policies had been issued to each of them. Its main purpose, however, is to protect each of the insured parties against cancellation or avoidance of the policy due to acts of fraud, misrepresentation or non-disclosure by another insured party.

Insurers typically agree under such a clause to waive all rights of subrogation and/or recourse which they may have or acquire against such coinsured or jointly insured party, (together with their employees and agents) except where the rights of subrogation or recourse are acquired in consequence of a vitiating act.

The majority of Non-Vitiation clauses in use within the London Market (including the model wording introduced by the London Engineering Group in January 1998) exclude innocently committed acts of fraud or misrepresentation by any of the insured parties. The LEG model wording additionally excludes indemnity to lenders for or damage sustained by an insured party committing a vitiating act, although this provision may be subject to negotiation in order to protect the interest of funders where the insurance relates to Project Finance.

In the case of Project Finance Insurance, such an amended clause would have the effect of safeguarding the funders' interests by ensuring that claims would still be met if the project company misrepresented or failed to disclose a material fact. Were it not included, the insurers would be fully entitled to void the policy for reasons which might not have been identified by the funders at the time of their entering into the contract. Additionally, the question of innocent acts committed by any of the insured parties and the effect that these might have on the funders rights would need to be taken into account and the clause amended or this provision deleted entirely as may be necessary.

In Commercial Property policies, a non-vitiation clause can also be included to protect the insured's interest should such policy be invalidated by the action of a tenant.

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Q32. What is meant by IBNR Losses?

This term refers to Losses Incurred But Not Reported.

An Incurred But Not Reported (IBNR) reserve represents the amount that must be provided for future payments on insured losses that have occurred but that have not been reported to the insurer. In classes of business with long-tail liabilities (such as asbestos, environmental and other related liabilities), this often includes claims of which the insured is also unaware.

In general, a request from an insurer to an insured for incurred losses would not be interpreted to include IBNR losses.

In order to differentiate, Incurred Losses can be defined as those occurring within a fixed period, whether or not paid or adjusted during that same period.

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Q33. What is Key Person insurance?

Key Person or Key Man insurance is designed to protect a company from the financial loss or impact that it would suffer in the event of the loss of, or the short or long term illness of employees whose skills within their workplace and knowledge of their products are essential to the continued profitability of the company or to individual projects undertaken under their direction.

The coverage provided can take the form of short term death or illness cover in respect of an employee essential to the fruition of an individual project to long term coverage in respect of directors and managerial level employees.

If an owner-director is critically ill, necessitating his or her being unable to continue work or if that person dies, succession costs might be incurred or guaranteed loans might have to be addressed

Additionally, Key Person insurance can be effected to cushion the financial impact of a person with unique skills terminating his employment to join a rival enterprise. This might lead to projects being abandoned or having to be substantially revised as a result of the loss of that person/skill set.

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Q34. What is Stop Loss reinsurance?

Stop loss reinsurance protects a cedant against losses exceeding an aggregate amount of claims over a period of insurance, normally stated as a percentage of the premium income earned during the period. This type of reinsurance does not apply to individual claims. Reinsurers' liability is limited to a stated percentage of the loss and a maximum monetary amount.

The stop loss method protects the cedant against the possibility that the aggregate value of an accumulation of small losses will exceed a specified percentage of earned premium income of a particular class. Stop loss reinsurance is the exact opposite of quota share reinsurance and surplus reinsurance.

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Q35. What is Surplus reinsurance?

Surplus reinsurance requires an insurer to transfer or cede and the reinsurer to accept the part or proportion of every risk that exceeds the insurer's predetermined retention limit. The reinsurer shares in the premium and losses in the same proportion as its share in the total limits pertaining to the risk.

This type of reinsurance allows the insurer to keep small insurance on its own account and to transfer the risk on larger insurances in excess of its retention limit

To illustrate simply how this type of reinsurance works, suppose an insurer issues a policy for USD 20,000,000, retains USD 5,000,000 (25%) and transfers the remaining USD 15,000,000 (75%) to its reinsurer. This type of surplus reinsurance is known as a "three line surplus" since the amount transferred amounts to three times the amount retained by the insurer. Should a total loss occur, the settlements between the two parties would be made on that same 25%/75% basis. Should a partial loss occur, the reinsurer reimburses the insurer in the same proportion as the amount of premium received by them.

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Q36. A wording contains the following exclusion. Does this policy cover flood and/or fire following earthquake?

"This policy does not cover: Loss or damage (including loss or damage by fire or theft) directly or indirectly resulting from typhoon, hurricane, cyclone, volcanic eruption, earthquake, subterranean fire or other convulsion of nature."

Answer: The word "indirectly" is present to expressly exclude any kind of consequential loss. Therefore we would not expect any perils to be covered as a result of earthquake.

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Q37. What prompted the need for specialised terrorism coverage within the United Kingdom?

In the United Kingdom, incidents such as the Iranian Embassy Siege of 1980, the IRA bombing of Manchester (1996), the Lockerbie bombing (1988) and St Mary Axe (1992), all prompted a recognition that a special class of insurance was needed to deal with eventualities which looked destined to become more frequent and commonplace.

The losses from these incidents caused insurers to re-examine the way in which coverage could be provided. The major problem lay in estimating the scale and frequency of future losses and the locations in which they might occur. Calculation of premiums was therefore rendered unreliable and haphazard, in consequence of which reinsurance could not be relied upon to provide adequate protection, potentially leaving insurers exposed to unforeseen, massive losses.

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Q38. What steps were taken to institute a scheme that would provide adequate coverage for terrorism losses within the United Kingdom?

Negotiations between the insurance industry and the government led to the formation of the Pool Re scheme in 1992. Its scope was initially limited to terrorist damage by fire and explosion.

In 2002, the government announced that the remit of the scheme would extend to full All Risks coverage, enabling it to provide coverage for contamination, impact by aircraft and flood damage in exchange for a doubling in premium for the period of risk. Membership of Pool Re continues to be optional but a property insurer joining it must, under the terms of its membership, insure a policyholder's entire portfolio of property risks under the scheme.

The Pool Re scheme sets industry-wide retentions. Where these have been met, losses arising from acts of terrorism are covered by the funds in the pool and when these have been exhausted, by the United Kingdom government.

In addition, Pool Re can provide reinsurance coverage in excess of the first £75 million of loss.

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Q39. What is an insurance pool?

An insurance pool is a group of insurers that pool assets to share both premiums and losses. By this means, they can provide a far greater amount of insurance coverage than that

available to an individual insurer and are able to insure much larger risks. By becoming a member of a pool, an insurer with limited resources is able to compete with larger and potentially more prestigious companies.

Pools can not only be set up on a basis of voluntary participation but may also be mandated by the state or government to cover risks where insurance may be unavailable within the standard markets. They enable insurers to easily compare loss and premium ratings whilst establishing an increased control over the particular class of business.

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Q40. What is TRIA, and how does it operate?

The Terrorism Risk Insurance Act (TRIA) is a United States Federal Law introduced by President George W. Bush in 2002 and was set up as a purely temporary measure to allow the insurance industry “breathing space” to develop its own solutions for the provision of property and casualty terrorism insurance in the wake of the 9/11 catastrophe.

The Act originally expired on 31 December 2005 and was subsequently extended for a further two years. It was then further extended under the Terrorism Risk Insurance Program Reauthorization Act (TRIPRA) to expire on 31 December 2014.

The TRIPRA extension to the TRIA Act refines Terrorism as being “any act certified by the Secretary of Treasury, in conjunction with the Secretary of State and the Attorney General, to be an act that is dangerous to human life, property or infrastructure and to have resulted in damage within the US (or outside the US in the case of a US -flagged vessel) or on the premises of a US mission”. The TRIPRA extension excludes the previous provision defining acts of terrorism as being those “committed by individual(s) acting on behalf of a foreign person or foreign interest as part of an effort to coerce the US population or government.”

The Act established the Federal Terrorism Insurance Program, overseen by the Secretary of the Treasury. The Program is triggered by his determination of an event as an Act of Terrorism, the deductible for an individual company being 20 per cent of premiums as at 2007 with limits set at USD 27.5bn of losses before federal assistance via the Program is available and losses from the Program must exceed USD 10 million.

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Q41. How does terrorism coverage operate in Spain?

In Spain, terrorism is classed as one of a number of “extraordinary risks” for which coverage is available from the Consorcio de Compensación de Seguros (CCS), which is managed by the state to provide compensation denied by the private reinsurance market. Coverage is mandatory in respect of property and business interruption, motor vehicle damage, machinery breakdown, theft, information technology, construction and personal accident.

Premium is charged by CCS at specified rates for individual classes. No insurer retentions apply under the Scheme , although an insurer is entitled to deduct a five per cent administration charge before passing the premium on to CCS.

CCS additionally acts as a warranty fund in the event that a private insurer is unable to fulfil its obligations with a state warranty with unlimited funds being in place as a safety net in the event that losses are in excess of CCS's capacity.

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Q42. How does terrorism coverage operate in Austria?

On 1 October 2002, the Verband der Versicherungsunternehmen Österreichs (the insurance association of Austria) formed the Österreichischer Versicherungspool zur Deckung von Terrorrisiken in order to cover purely private co-reinsurance risks.

Protection is provided on property and business interruption risks for industrial, commercial and private lines with a sum insured of up to EUR 5 million each location, policyholder and calendar year. Risks with total limits exceeding this amount need to be covered facultatively.

The Pool holds reinsurance of EUR 150 million in the annual aggregate in excess of a retention of EUR 5 million. Participation is voluntary but includes the vast majority of members of the Verband der Versicherungsunternehmen Österreichs.

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Q43. How does terrorism coverage operate in Germany?

Extremus Versicherungs-AG was established in 2002 following the 9/11 attacks in the US and operates as a specialist insurance company solely underwriting large scale property terrorism risks. The German government participates in a limited capacity and membership is optional.

Extremus only participate where the sum insured is in excess of EUR 25 million with the scheme providing a total of EUR 10 billion per annum. The German government has extended its guarantee to Extremus until the end of 2009 with USD 11.6 billion of funding and has said that its support is likely to continue thereafter, but at a lower funding level.

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Q44. How does terrorism coverage operate in the Netherlands ?

Nederlandse Herverzekeringsmaatschappij voor Terrorismeschaden N.V is a reinsurance company incorporated by the Association of Insurers in the Netherlands, writing property and business interruption risks with a sub-limit for all participating insurers of EUR 75 million per policyholder or location per annum.

Insurers bear a combined retention of EUR 7.5 million or 2.5 per cent of the gross premium per annum, subject to a minimum retention of EUR 50,000 per participant. Should claims exceed

EUR 1bn per annum, they may be reduced proportionately by the government so that the limit is not exceeded.

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Q45. How does terrorism coverage operate in Australia?

The Terrorism Insurance Act (TIA) came into effect on 1 July 2003. This Act declares that, should the Australian Government declare the occurrence of a terrorist incident within Australia, the terrorism exclusion in an applicable property or public liability policy is rendered inoperative and cover is provided thereunder for terrorism losses in accordance with all other terms and conditions contained therein.

A non-compulsory reinsurance pool - the Australian Reinsurance Pool Corporation – was established to work alongside TIA but is only available to participants who exclude terrorism under their policies. As with TIA, should a terrorist incident be declared, the pool indemnifies up to the limits contained within the applicable policies, with a retention not exceeding AUD 1 million per insurer per annum and an overall cap of AUD 10 billion per incident.

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Q46. How does terrorism coverage operate in South Africa ?

SASRIA (the South African Special Risks Insurance Association) was formed by the South African Government in 1979 to specifically provide coverage for political unrest, violence and defined terrorist risks. A coupon is issued to the insured party through the insurer on policies covering motor, mining, construction and plant, money, computer insurance, property damage and business interruption (restricted to standing charges and insured working expenses only) up to a maximum limit of ZAR 300 million in respect of any one insured .

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Q47. How does terrorism coverage operate in Namibia ?

NASRIA (the National Special Risks Association) was set up by the Namibian government in 1987 and offers coverage on property, business interruption, crime and motor risks up to a limit of NAD 100 million.

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Q48. How does terrorism coverage operate in France?

The purchase of terrorism coverage is obligatory in France. Property damage and motor vehicle policies have been required to include this coverage since 1986. Membership of the French reinsurance pool GAREAT is compulsory for members of the French Insurers Association FFSA including Lloyd's. It offers protection to direct insurers if they cede the terrorism part of all qualifying policies within their portfolio together with the respective premium, provided that the sum insured exceeds EUR 6 million.

Should the sum insured lie between this amount and EUR 20 million, the insurer is required to cede 6 per cent of the premium to GAREAT with further rates of 12 per cent applicable to sums insured up to EUR 50 million and 18 per cent on sum insured above this amount.

The pool operates through four layers:

The first EUR 400 million being covered by a co-reinsurance pool, through which coverage is mandatory.

The second layer of up to EUR 1,600 million is purchased through commercial insurers and reinsurers.

The third layer, up to a limit of EUR 2,200 million is led by Hannover Re.

The fourth and final layer is provided by the French government, offering unlimited indemnity through Caisse Centrale de Reassurance, a state-owned reinsurer.

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Q49. What is Stand Alone Terrorism cover and how does it operate?

Stand alone terrorism coverage may be defined as a policy covering Terrorism risks only rather than an extension to an existing property or casualty policy and one specifically effected to provide coverage outside any applicable terrorism pool or where pool coverage is not available. The market for such policies has developed considerably since the 9/11 events. Many insureds prefer the degree of certainty that such cover offers compared to that of TRIA and terrorism pools whose future life span might be uncertain..

The most commonly used policy form within the London market for the provision of coverage for domestic and foreign acts of terrorism committed for religious, political and ideological purposes is the T3 form together with its companion Business Interruption Extension T3A, which as standard provides indemnity on a Gross earnings basis with other variants being developed and registered within the market. The policy can be extended to include sabotage i.e. acts of deliberate subversion causing damage or destruction and arising out of acts covered by the policy.

The T3 form uses a standard terrorism definition which does not include the use of biological or chemical weapons, nuclear detonation or explosion or bio-chemical weapons. This has made it a form more suitable for use within Western Europe and the US than in Iraq, India, Sri Lanka and other areas which are emerging as terrorism hotspots.

These areas call for the development of specialist wordings which may well prompt radical alterations to the standard London market forms.

A companion wording, the T3L form, provides indemnity for bodily injury and property damage arising out of similar acts of terrorism but additionally includes acts of intimidation or coercion, disruption of the economy or Government, overthrow of the Government by intimidation or coercion and acts mass destruction, assassination, kidnap or hostage-taking intended to affect the conduct of the Government.

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