

calculating the appropriate DEP can be utilized.

Other Non-Covered Lines

One commenter suggested that Treasury consider extending the commercial/personal allocation to other hybrid contracts containing premiums for excluded lines of coverage such as Medical Malpractice in combination with Hospital General Liability coverage. Such insurance lines are not within the scope of the definition of commercial property and casualty insurance of the Act and are not included in the Program. Therefore, premiums in hybrid policies applicable to those exceptions do not need to be included in an insurer's DEP. Any allocation of premium for such exclusions should be calculated by insurers either using methods suggested by Treasury, or other similar methods in accordance with the insurer's normal business methods and procedures.

Another commenter suggested that Treasury should exclude premiums reported on the specified lines on Statutory Page 14, but earned from retroactive insurance programs such as certain Novations, Adverse Development Cover, or Loss Portfolio Transfer Programs. Retroactive insurance is insurance covering only events that occurred prior to the inception date of the policy, but there appears to be no differentiation in the Statutory Page 14 reporting to indicate that such premiums relate to risks from prior years. Treasury takes the position that such retroactive premiums are not within the time period of the definition of "insured losses" if they are associated with losses that occurred prior to enactment and the effective date of the Act (November 26, 2002). Such premium income may be removed in an insurer's calculation of its DEP. Treasury has modified the language in the final rule (section 50.5(d)(1)(i-iv) of the interim final rule) to clarify the nature of the allocation provisions with regard to hybrid policies and other policies with coverage of losses outside the scope of insured losses under the Program.

Fidelity Insurance

Treasury did not include Line 23 (Fidelity) of Statutory Page 14 in its list of specified lines considered to be commercial "property and casualty insurance" covered under the Act in its initial interim guidance or in its interim final rule. Comments were received from five different commenters, two in support of Treasury's position, and three in opposition.

One of the commenters advocating the inclusion of fidelity insurance argued that it can also have a distinct property component as in cases where coverage is provided for the destruction of money and securities, such as those held in bank or corporate vaults. The commenter pointed out that it had losses associated with fidelity policies arising from the September 11 terrorist attacks totaling some \$20 million due to the destruction of cash on the premises of its insured. Another commenter emphasized that fidelity has always been considered by state regulators, insurers, and policyholders to be a commercial property and casualty line.

Those opposed to the inclusion of fidelity insurance contend that it is a line of insurance that by itself faces low exposure to terrorism losses. One commenter had indicated previously that it had provided terrorism coverage for all of its fidelity policies prior to the Act, but needed to confirm whether fidelity insurance was covered under the Program in order to know how much reinsurance coverage would be needed to cover its deductible exposure. Commenters also pointed out that if Treasury were to reverse itself and now include fidelity insurance as a covered line, problems associated with the timing of the disclosure requirements and other issues would need to be addressed.

After considering the comments, Treasury has determined that fidelity insurance is not covered under the Act, and thus has not inserted Line 23 (Fidelity) in the specified lines on Statutory Page 14 that make up commercial property and casualty insurance covered under the Act. In making the overall determination of what lines of coverage are included and excluded in the definition of property and casualty insurance, Treasury relied on specific guidance provided by Congress in section 102(12) of the Act. Section 102(12)(A) expressly includes excess insurance, workers' compensation insurance, and surety insurance. Traditional surety insurance and fidelity insurance share a similar characteristic in that they guarantee against losses associated with the performance of third parties. Treasury maintains the position that if Congress had intended fidelity insurance to be covered, it would have specifically included it as it did surety insurance. Treasury relied on a similar rationale for excluding group accident coverage, a line of coverage that shares some of the same risk characteristics as workers' compensation coverage, from the list of specified lines on Statutory Page 14 that make up commercial property and

casualty insurance covered under the Act.

Through the comment process, Treasury has been made aware that the traditional fidelity insurance coverage has been expanded in recent years by some insurers to include coverage to non-employee "insiders," as well as to property coverage for loss of firm assets, including cash, due to crime. Although Treasury is making no change to the interim final rule definition with regard to fidelity in the final rule, Treasury will continue to evaluate this wrap-around or hybrid-type coverage which could include other types of coverage that are generally covered by the Act, but not reported as such. In this regard, Treasury will evaluate whether and how the designation of included and excluded lines has affected the availability of coverage for terrorism insurance risk, and whether any further change in the Program might be warranted.

Other DEP-Related Comments

On behalf of county or town mutual insurers that do not report on Statutory Page 14, one commenter suggested that Treasury's suggestion that they convert direct premium or other types of payments such as assessments or contributions into DEP, would lead to inconsistencies in the Program because states have varying reporting requirements. The result would be that DEPs would vary significantly from state to state, which would be "bad from a public policy perspective, but leaves insurers on uncertain ground despite their best good faith efforts at compliance." Treasury has consulted with the NAIC on this issue and we understand that the NAIC plans to develop a recommended conversion method that States in turn could recommend to county or town mutual insurers.

Another commenter requested that Treasury give insurers assurance that "fronted" premiums received by an insurer would not be included in DEP and thus raise its deductible, if the insurer assuming the risk (captive or otherwise) is also an insurer under the Program. The commenter explained that "fronting" is a credit enhancement procedure that is sometimes employed by business customers and their insurers to expand available insurance capacity, and is recognized by state regulators. However, fronting arrangements are not addressed in the Act, and the Act does not appear to provide any basis to exclude "fronted" premiums from DEP. If one insurer "fronts" for another by receiving premiums but passes the risk to another,