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Report from the Editor

by Eric A. Fitzgerald, J.D., CPCU

Eric A. Fitzgerald, J.D, CPCU, is the editor of *The Specialist* and a coverage litigation attorney with the law firm of Marshall Dennehey Warner Coleman & Goggin. The Philadelphia-based firm provides coverage and defense litigation services throughout PA, NJ, DE, OH, WV, and FL through 16 regional offices.

Our feature article this month is a summary of some of the filings in the World Trade Center litigation. Traditionally, the examination of whether a series of criminal acts constituted one or a number of "occurrences" was reserved for small deductible commercial property policy disputes. Now, it is arguably the highest stakes coverage case ever litigated. Despite the unique context, the arguments involved are, for the most part, traditional coverage law arguments. This unlikely joinder of the spectacular and the mundane makes for interesting reading to all of our members.

We are also pleased to bring news of a number of changes to the ASLI designation program. Please feel free to share this issue with any colleagues who are pursuing the CPCU, ASLI, or any portion of these designations. Let's spread the word that obtaining surplus lines credentials has never been more accommodating to our industry.

Finally, an interesting piece on the "language" of our unique industry. As this article goes to print, the Excess/Surplus/Specialty Lines Section committee members will be meeting at the CPCU Society's Leadership Summit in Tampa, FL. We will be discussing how we can continue to strive to bring value to membership in the E/S/SL Section. As always, please forward your ideas to any member of the E/S/SL Section Committee so we can share them throughout the Society. ■

What's in this Issue?

Lloyd's Files Amici Curiae Brief in World Trade Center Coverage Litigation

The Difference Between the Definition of an "Occurrence" in First-Party and Third-Party Coverage Cases

by Richard Wilson, Esq.

Editor's Note: Many of us have heard reports from the ongoing litigation in New York Federal Court regarding whether the World Trade Center destruction will involve one or two occurrences for purposes of insurance recovery. Following, please find a summary prepared by Richard Wilson, Esq., of the Coverage and Bad Faith Litigation Department of Marshall, Dennehey, Warner, Coleman & Goggin.

Lloyd's of London filed an Amici Curiae brief on February 6, 2003, with the United States Court of Appeals for the Second Circuit in the case styled, *World Trade Center Properties, LLC, v The Travelers Indemnity Company,* Civ. A. No. 02-9440 (2nd Cir. 2002).

This case arose out of the terrorist attacks that occurred on September 11, 2001, in New York City. World Trade Center Properties (the "Silverstein parties") filed a declaratory judgment action in a New York District Court against one of its first-party insurers requesting that the court declare that the attack on the World Trade Center on September 11 constituted two "occurrences" and thus, Silverstein parties were entitled to the aggregate policy limits. Silverstein parties' strategy was to move solely against one of its first-party insurers, Travelers Indemnity Company, and then seek to export that result to its other insurers who issued first-party coverage to the World Trade Center. Because Lloyd's also issued first-party insurance to Silverstein parties, it had a substantial interest in this dispute and thus, was allowed to file an Amici Curiae brief addressing the Silverstein parties' failure to accurately acknowledge and apply first-party property insurance law and principles.

The New York Court of Appeals defined first-party insurance as pertaining to loss sustained by an insured to its property, thus, the insured received proceeds when the loss occurs. On the other hand, "if the insurer's duty to defend and pay runs against a third-party claimant who is paid according to a judgment or settlement against the insured then the insurance is classified as 'third-party insurance." *Great Northern Ins. Co. v Mount Vernon Fire Ins. Co.*, 708 N.E.2d 167, 170-71 (N.Y. 1999). Lloyd's stated that Silverstein parties rely primarily on third-party liability decisions thereby attempting to rewrite first-party insurance law so that the number of deductibles and limits turns on how the damage is created by the wrongdoers.

Lloyd's began its argument section of its Amici Curiae brief with an in-depth analysis of the definition of "occurrence" in insurance contracts. As stated previously, the Silverstein parties relied almost exclusively on third-party insurance decisions to imply that New York determines occurrence for all purposes by the most immediate physical cause in time. Lloyd's stated that under New York law, the meaning of occurrence varies according to the type of policy at issue and the facts of each case. Moreover, New York recognizes that the unique purposes of first-party insurance yield a distinct occurrence standard. Lloyd's explained that third-party liability insurance indemnifies for the consequences of the insured's own non-intentional conduct injuring others or causing damages to their property. Whereas, Silverstein parties contend that courts should look to the event for which the insured is held liable, regardless whether it is in the physical impact closest in time.

However, Lloyd's pointed out that the Silverstein parties' focus on liability-causing conduct was irrelevant to first-party insurance, because first-party coverage provides insurance against external peril causing damage to the insured's property. Accordingly, the fact that an insured cannot obtain coverage for intentional acts under liability insurance underscores how especially unhelpful third-party precedent was in assessing coverage for intentional damage to first-party property.

With regard to first-party insurance, Lloyd's explained that New York courts focus on time, location, and peril. The Second Circuit in *Newmont Mines v. Hanover Insurance Co.*, 784 F.2d 127 (2nd Cir. 1986) explained that the purpose of first-party insurance is as follows:

> The goal of such a policy, simply stated, is to provide financial protection against damage to property. In accordance with this purpose, the parties here must have intended to provide coverage for property damage each time it occurred unexpectedly and without design, unless the damage occurring at one point in time was merely part of a single, continuous event that already had caused other damage.

Newmont Mines' fact-intensive analysis of the relevant time, location, and peril stands squarely against the Silverstein parties' core claim that "New York law looks only to the immediate physical cause of the loss." The Second Circuit in *Newmont Mines* held that there were two occurrences in a first-party property insurance policy because there were two roof collapses at least three and potentially 17 days apart, the collapses were not connected, the sections of the roof were structurally independent of each other, temperature change may have contributed to the second collapse but not the first, and additional snow may have fallen between the two collapses.

Another case that Lloyd's cited in support of the proposition that in first-party occurrence disputes a court must look to the proximity of location, time, and peril was *Bird v St. Paul Fire & Marine Insurance Co.*, 120 N.E. 86 (N.Y. 1918). In *Bird*, Judge Cardozo held that the proximity of location and time is paramount in assessing the expectations of a reasonable insured. Specifically, Judge Cardozo states:

> In last analysis, therefore, it is something in the minds of men, in the will of contracting parties, and not merely in the physical bond of union between events, which solves, as least for the jurist, this problem of causation. . . . For the physicist, one thing is the cause; for the jurist, another. Even for the jurist, the same cause is alternately proximate and remote as the parties choose to view it. . . . There is nothing absolute in the legal estimate of causation. Proximity and remoteness are relative and changing concepts.

In light of Judge Cardozo's reasoning in *Bird*, Lloyd's stated that the correct test for an "occurrence" is not the immediate physical cause/impact, but "the reasonable expectation and purpose of the ordinary businessman when making an ordinary business contract," an expectation that varies by peril and proximity of space and time. Applying those principles to the present event, Lloyd's stated, "reasonable insureds—in fact, the entire country—understood and said on September 11 that the World Trade Center had been destroyed by a terrorist attack." Contrarily, the Silverstein parties argue that the existence or absence of a terrorist attack is always irrelevant as a matter of New York law in determining causation and occurrence. Lloyd's' responded:

> Through the Silverstein parties' artificial lens, the reasonable expectations of business insureds are unaffected by the fact that the damage done was a part of a terrorist attack, and those insureds' expectations rest solely on the number of physical impacts on the insured location. This view violates

> the principles in *Bird*, (i) against *per se* rules and (ii) for determining reasonable expectations based on "life and experience." To the contrary, *Bird* leaves no doubt that the existence of a coordinated terrorist attack is highly relevant to a reasonable insured's view (as informed here by the experience of the 1993 terrorist bombing) of the cause of damage and the number of occurrences.

Other first-party insurance cases involving terrorists attacks underscore Lloyd's position that the tactics of the wrongdoers do not effect the coverage. Lloyd's cites *Pan American World Airways, Inc. v Aetna Casualty & Surety Co.*, 505 F.2d 989 (2nd Cir. 1974), in which the Second Circuit reviewed a non-jury trial resolving the insured peril after Palestinian terrorists hijacked a Boeing 747 passenger jet over England and later blew it up on an airfield in Egypt. The court held that the cause of the first-party loss in Pan American was the terrorist hijacking of the aircraft over England—not the immediate physical impact of the explosion in Egypt or the number of explosives used by the terrorists to destroy sections of the property. The Second Circuit in Pan American reasoned that:

> If the events following a hijacking were permitted to control the insurance nature of the loss, the outcome in any case would vary according to the whim of the hijacker. . . . The parties cannot have intended that the caprice of the hijackers would control the insurance consequences of the loss. Id. at 1008.

The Amici Curiae brief filed by Lloyd's also cited other jurisdictions that have determined that first-party "occurrence" is based on unity of location, time, and peril. The decision that Lloyd's believes is closest to the facts on appeal involved the intentional conversion of 15 Kuwaiti airplanes at one airport by different persons over the course of a day as part of the Iraqi occupation of Kuwait. In *Kuwait Airways Corp. v Kuwait Ins. Co.*, 1 Lloyd's Rep. 664 (Eng. Q.B. 1995), the English Court of Queen's Bench looked to the parties' reasonable expectations and described how occurrence is determined for intentional acts by unities of time, location, and peril. Namely, the English Court held that a reasonable business person would not consider the loss of each aircraft a separate occurrence.

Similarly, the first-party insured in *Peco Energy Co. v Boden*, 64 F.3d 852 (3rd Cir. 1995) was the victim of a series of thefts that took place over a six-year period, but the Third Circuit held that the facts constituted a single "occurrence" under a first-party insurance policy. The court's decision was based on the finding that each theft was part of a larger scheme and that the scheme to steal was the proximate cause behind each theft. A California appellate court in *Eott Energy Corp. v Storebrand Int'l. Ins. Co.*, 52 Cal. Rptr. 2d 894 (Cal Ct. App. 1996) concluded that more than 650 thefts of fuel from the same insured property over a period of 11 months would constitute a single "occurrence" if the thieves acted pursuant to a systematic and organized scheme. Lloyd's concluded that the above principles apply with added force when terrorists intentionally use hijacked aircraft as coordinated weapons to destroy a single location like the World Trade Center.

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Lloyd's Files Amici Curiae Brief in World Trade Center Coverage Litigation

Continued from page 3

Lloyd's further stated that the Silverstein parties' position produces absurd first-party results. To reinforce the argument that the definition of occurrence is inherently different with regard to first- and third-party insurance, Lloyd's gave several examples of first-party coverage results if, as the Silverstein parties request, the definition of "occurrence" in third-party policies was applied to first-party scenarios:

> Assume, for example, that a group of 10 actors carries out a coordinated attack on an insured location by breaking 10 windows, with each individual throwing a separate rock through a separate window at about the same time. A reasonable insured would see the coordinated attack as one occurrence requiring one deductible and providing one limit. But under the Silverstein parties' unprecedented view, each of the 10 rocks striking a window would be a separate "immediate, efficient, physical cause" of the damage, constituting a separate occurrence. An equally absurd result follows where a single actor strikes all 10 blows, causing the insured to absorb 10 deductibles and potentially eliminating any insurance recovery.
>
> The same fault lies when the Silverstein parties' position is applied to terrorist attack. A large gang of terrorists simultaneously setting off bombs on each level of the World Trade Center would impose hundreds of deductibles based on the Silverstein parties' immediate physical impact theory, and dropping bombs from a hijacked aircraft would impose as many deductibles and limits as bomb strikes.

Lloyd's stated that a reasonable first-party insured would view a coordinated attack crashing hijacked planes into the World Trade Center only minutes apart as a continuous event subject to one deductible and one limit. Lloyd's reiterated that the Silverstein parties' strained position on "occurrence" means that the peril of terrorist attack is legally irrelevant to coverage meaning that the only relevant factor in determining whether the event consisted of one event would be the type of immediate physical impact, thus, making the Silverstein parties request for insurance of terrorism unnecessary.

Lloyd's further argued that the Second Circuit should reject the Silverstein parties' attempt to rewrite the law of first-party "occurrence." One of the third-party liability insurance cases that the Silverstein parties rely on in support of their contention that the World Trade Center attack constituted two occurrences is *Arthur A. Johnson Corp. v Indemnity Insurance Co.*, 164 N.E.2d 704 (N.Y. 1959), which involved the failure of two retaining walls during a heavy rain that led to flooding of the sub-basements in two buildings. The New York Court of Appeals found that there were two occurrences for the purposes of triggering liability coverage because the insured had incorrectly constructed the walls and the business purpose of the insurance was served by keying the insured's coverage to the two constructions that generated the liability contractually assumed under a strict liability standard. Lloyd's stated that the Silverstein parties illogically seek to equate the rainfall in *Johnson* with what they term the insurers "remote" cause of loss in this case. However, Lloyd's stated that rainfall was not a risk insured under third-party policies and could not possibly be the conduct for which an insured is held liable. Lloyd's argued that in the present coverage dispute, a terrorist attack is an insured peril under first-party policies and, the terrorist attack on September 11, 2001, was not "remote."

Finally, Lloyd's stated that the Silverstein parties' proposed effort to impose a new "occurrence" standard on insureds and insurers doing business in New York would result in a windfall for the insureds in the present case and would unfairly multiply deductibles and vitiate first-party coverage for other property owners in other intentional damage cases. Lloyd's argues that insurers would become reluctant to provide coverage at the lowest layers out of reciprocal concern that an intentional attack would multiply limits based on the number of weapons used by attackers. Moreover, because the insured has the burden to prove the number of occurrences, the Silverstein parties' standard would disadvantage these insureds by imposing on them the difficult obligation to prove the number of weapons, impacts, and actors causing damage to their property.

However, the most persuasive argument that the Silverstein parties standard would result in an inherently unfair result was that shortly before September 11, Silverstein completed an arm's length transaction and valued the full replacement cost of the World Trade Center at approximately $3.945 billion. At the same time, Silverstein chose to insure the entire property as one insured location for $3.546 billion. Now, Silverstein is arguing a theory designed to create coverage for twice that amount against a single, coordinated terrorist attack that destroyed that single insured location. Lloyd's concluded its brief by stating that Silverstein should be held to the bargain made, and the logical and settled New York law of first-party insurance, not the Silverstein parties' post hoc contentions, should determine the meaning of "occurrence."

It is not often that an insurance coverage dispute has billions of dollars at stake. As such, we will be waiting for a decision from the Second Circuit, which will have some effect on coverage litigation throughout the country for many years to come. Regardless of the outcome, we can anticipate that the parties will be requesting United States Supreme Court review of the issue. We will continue to follow and report on this important litigation. ■

Surplus Lines Certification Program Offers Many New Completion Options

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The Associate in Surplus Lines Insurance (ASLI) program, the only nationally recognized certification program for surplus lines specialists and others seeking expertise in this field, has new completion options that greatly broaden the choices of people who earn the designation. These new options include courses in a number of areas such as claims, underwriting, finance, and insurance production.

Allowing people who want to specialize in surplus lines insurance to tailor the program to their daily responsibilities and career goals is an extremely desirable broadening of the ASLI program.

The ASLI designation is conferred by the Insurance Institute of America (IIA). Earning the ASLI designation requires passing four courses and national examinations. The two foundation courses, ASLI 161—Surplus Lines Insurance Principles and Issues and ASLI 162—Surplus Lines Practices, remain the same. For the other two required courses, however, the student can now select one coverage elective from a list of 10, and one operational elective from a list of 18. In addition, the Registered Professional Liability Underwriter (RPLU) designation granted by the Professional Liability Underwriting Society satisfies both electives.

Arthur L. Flitner, CPCU, assistant vice president at IIA, announced the new completion options. "Allowing people who want to specialize in surplus lines insurance to tailor the program to their daily responsibilities and career goals is an extremely desirable broadening of the ASLI program," Flitner said. "When people make a commitment to increase their knowledge, they want choices to let them align their learning with their educational goals. The timing of these changes is good because it corresponds to a hardening market when insurance practitioners are increasingly looking to surplus lines to meet some of their clients' insurance needs," he added.

The ASLI program was developed by IIA with the assistance of the National Association of Professional Surplus Lines Offices (NAPSLO). Previously, the courses required to earn the ASLI designation consisted of ASLI 161 and ASLI 162 and two courses from the Chartered Property Casualty Underwriter program, CPCU 510—Foundations of Risk Management, Insurance, and Professionalism (formerly CPCU 1), and CPCU 520—Insurance Operations and Regulation (formerly CPCU 5). Under the new completion rules, CPCU 510 is one of the coverage electives, and CPCU 520 is one of the operational electives.

According to Flitner, NAPSLO's ongoing support of the ASLI program has been extremely valuable. "NAPSLO strongly encouraged us to revise the ASLI program rules to broaden its appeal and increase its value to insurance practitioners," Flitner said. ■

ASLI Coverage Electives	ASLI Operational Electives
CPCU 510—Foundations of Risk Management, Insurance, and Professionalism	CPCU 520—Insurance Operations and Regulation
CPCU 551—Commercial Property Risk Management and Insurance	AIS 25—Delivering Insurance Services
CPCU 552—Commercial Liability Risk Management and Insurance	AIC 33—The Claims Environment
CPCU 555—Personal Risk Management and Property-Liability Insurance	AIC 34—Workers Compensation and Managing Bodily Injury Claims
CPCU 557—Survey of Commercial Risk Management and Insurance	AIC 35—Property Loss Adjusting
INS 23—Commercial Insurance	AIC 36—Liability Claim Practices
AAI 81—Foundations of Insurance Production	AU 65—Commercial Underwriting: Principles and Property
AAI 82—Multiple-Lines Insurance Production	AU 66—Commercial Underwriting: Liability and Advanced Techniques
AMIM 121—Ocean Marine Insurance	AAI 83—Agency Operations and Sales Management
AMIM 122—Inland Marine Insurance	APA 91—Principles of Premium Auditing
	APA 92—Premium Auditing Applications
	AIAF 111—Statutory Accounting for Property and Liability Insurers
	AIAF 112—Insurance Information Systems
	AIAF 113—Insurance Company Finance
	AIT 132—Insurance Uses of Technology
	AIT 134—The Strategic Management of Information
	ARe 141—Principles of Reinsurance
	ARe 142—Reinsurance Practices

Surplus Lines in the United States

by David N. Blakesley, CPCU, ARM

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MultiTech Communications, Inc. provides foreign-language translation services to the insurance industry worldwide.

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The United States has 56 insurance jurisdictions: the country's 50 states, plus the District of Columbia, American Samoa, the Commonwealth of the Northern Mariana Islands, Guam, Puerto Rico, and the U.S. Virgin Islands. Insurance laws in American Samoa are written in Samoan and English. In the Commonwealth of the Northern Mariana Islands, despite the use of the Chamorro and Carolinian languages in addition to English, and in Guam, despite the use of Chamorro in addition to English, insurance laws are written solely in English. The insurance laws of Puerto Rico are written solely in Spanish.

Because of the multiplicity of U.S. insurance jurisdictions, each with its own laws and regulations, all statements made about the U.S. market as a whole must of necessity be general.

Admitted versus Non-Admitted

Each of the 56 U.S. jurisdictions regulates all forms of insurance within its borders. Generally, an insurer may operate within a jurisdiction as an admitted or non-admitted carrier. Stated simply, an admitted carrier in a U.S. jurisdiction is subject to the regulatory authority of that same jurisdiction; a non-admitted carrier in a U.S. jurisdiction is subject to the regulatory authority of another jurisdiction, whether a U.S. or a non-U.S. jurisdiction.

If a carrier desires admitted status, it enters into an agreement, often called a "charter," with the jurisdiction's Department of Insurance or equivalent body. Such agreement stipulates how the carrier must operate when it conducts business in the jurisdiction. Typically, among other requirements, the admitted carrier agrees to file certain financial information, undergo inspections, pay premium taxes, maintain an office or offices in the jurisdiction, and contribute to the jurisdiction's solvency or guaranty fund or pool. In consideration of that agreement, an admitted insurer is granted a license or certificate of authority, which allows it to conduct insurance business in the jurisdiction.

A non-admitted carrier may be "foreign" or "alien." From the point of view of a U.S. insurance jurisdiction, a "foreign non-admitted carrier" is any insurer not regulated by that jurisdiction but by at least one other U.S. jurisdiction. An "alien non-admitted insurer" is an insurer regulated by any non-U.S. jurisdiction.

U.S. jurisdictions allow certain foreign and alien non-admitted carriers to sell insurance within their borders. A foreign or alien non-admitted carrier may be either eligible or ineligible to sell insurance in U.S. jurisdictions, depending on the statutes and regulations of the jurisdiction, which may require proof of financial soundness, among other conditions, before eligibility is granted.

Surplus Lines Carriers—Paradox

In the market, eligible foreign and alien non-admitted carriers are called "surplus lines carriers," or sometimes "excess and surplus lines carriers," reflecting the name given to the coverages they sell. In short, "surplus lines carriers" equal "non-admitted carriers." Non-admitted status is not the only characteristic that distinguishes surplus line carriers. A degree of freedom arising out of their non-admitted status—allowing them to operate, in effect, as deregulated specialty insurers—also distinguishes them. In fact, absent regulatory freedom, a surplus lines carrier would have no special market strengths. Thus, "surplus lines carriers" equal "non-admitted carriers" equal "deregulated specialty carriers."

Therein lies the paradox: to achieve a degree of regulatory freedom as a deregulated specialty carrier, a U.S.-domiciled surplus lines carrier must first be subject to all the same regulations imposed on non-surplus lines (that is, standard) carriers.

However, as stated, to operate in the United States, a U.S.-domiciled surplus lines carrier is always an admitted carrier in at least one U.S. jurisdiction (typically, in its jurisdiction of domicile). In that jurisdiction, the carrier is on the same regulatory footing as all other insurers admitted in the jurisdiction and thus indistinguishable from them.

Therein lies the paradox: to achieve a degree of regulatory freedom as a deregulated specialty carrier, a U.S.-domiciled surplus lines carrier must first be subject to all the same regulations imposed on non-surplus lines (that is, standard) carriers. That's because admitted carriers are treated equally under the laws and regulations of U.S. jurisdictions, irrespective of whether a company's mission is to operate in the marketplace as a surplus lines or standard carrier. Differing legal treatment arises only regarding admitted versus non-admitted insurers.

Let's take, for example, three imaginary U.S.-domiciled carriers—Would-Be Surplus A, In-Fact Surplus B, and Standard C—in California, the country's largest surplus lines market in premium volume. Would-Be Surplus A is domiciled in California and admitted there; In-Fact Surplus B is domiciled and admitted elsewhere in the United States; and Standard C is domiciled elsewhere in the United States and admitted in California. Would-Be Surplus A is not treated under California law and regulations like In-Fact Surplus B with which it shares a mission as a surplus lines carrier, but receives the same treatment as Standard C, a completely different type of operation. As a result, if Would-Be Surplus A were to sell insurance on its own paper in California, it would be bound by the same wording and rating constraints as Standard C. Would-Be Surplus A can fulfill its mission as a surplus carrier outside California only.

This situation occurs throughout the United States. Faced with the paradox imposed by the regulatory system in the United States, surplus carriers, like Would-Be Surplus A in the example, do not sell insurance on their own paper in the jurisdictions where they are admitted. They serve policyholders within their admitted jurisdictions through other insurers that are able to operate as surplus insurers in those jurisdictions.

Surplus Lines—Scope

Although surplus lines, in principle, are not limited to any one type of insurance or buyer, they consist, in practice, almost entirely of specialty commercial property/casualty coverages. Satisfying a variety of specialized needs, surplus lines can respond to demands for:

- Normal coverages, such as property damage or liability insurance, not available from non-surplus lines (standard) carriers because of exposures, loss experience, or limits.
- Unusual or unique coverages, such as broader-than-normal liability insurance or specialty risks not available from standard carriers: event cancellation or fine-art insurance or unique risks, a movie star's legs, for example.

Surplus Lines—Policies and Pricing

A surplus lines policy wording may be the same as found in the non-surplus lines market (for example, if the surplus lines market is tapped simply to obtain higher limits), a modified form of a similar wording found in the non-surplus lines market (for example, through the insertion of special exclusions or added insured perils), or unique (for example, kidnap and ransom insurance). Because of the focus on greater-than-normal exposures and specialty and unique risks, it is not surprising that rates in the surplus lines market may be substantially higher than those in the non-surplus lines market.

Surplus Lines—Distribution

Surplus lines insurance is sold through intermediaries, called either an agent or a broker, depending on the U.S. jurisdiction. Generally, distribution of surplus lines products is wholesale, that is, from a surplus line agent or broker to a policyholder's independent agent or broker, rather than retail, that is, from a surplus line agent or broker directly to a policyholder. Generally, U.S. jurisdictions require that a policyholder's broker or independent agent exert some form of diligent effort to place the policyholder's coverage with an admitted carrier before placing it with a non-admitted carrier.

Surplus Lines—Example of Policyholder Benefits

XYZ Corporation manufactures sports clothing and football helmets, an unusual combination of exposures. Let's assume that all non-surplus lines liability carriers in the jurisdiction where XYZ is located are willing to insure product liability arising out of manufacture of sports clothing, but none wants to insure the liability arising out of manufacture of football helmets because of exposure to head trauma claims. Eligible surplus lines carriers are willing to insure the combined exposure, but their rates are substantially higher than those of admitted carriers.

Faced with these circumstances, XYZ's broker or independent agent might obtain:

- Football helmet coverage from a surplus lines carrier through a surplus lines broker.
- Sports clothing coverage from a non-surplus lines carrier.

By tapping the surplus lines market, XYZ's broker or agent obtains insurance for the otherwise uninsurable helmet exposure. By placing the minimum-risk sports clothing exposure in the lower-priced admitted, non-surplus lines market, the broker or agent reduces XYZ's overall premium expense.

Surplus Lines—Terminology in Puerto Rico

Basic surplus lines expressions used in the Insurance Code of Puerto Rico—the one market in the United States in which insurance laws are not written in English—are:

- asegurador autorizado—admitted carrier
- asegurador elegible de lÌneas excedentes—eligible surplus lines carrier
- asegurador no autorizado—non-admitted carrier
- corredor de seguros de lÌneas excedentes—surplus lines broker
- seguros de lÌneas excedentes—surplus lines insurance

Surplus Lines—Statistics and Future

In its annual review of the excess and surplus lines industry, issued in September 2001, A.M. Best reported that surplus lines premiums in the United States reached $11.7 billion, or 7.2 percent of the total commercial property and casualty premium in the country, in 2000. According to a survey conducted by *Business Insurance* magazine, published in its September 10, 2001, issue, the top

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Surplus Lines in the United States

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three surplus lines markets in 2000, in order of premium volume, were California, Texas, and Florida.

. . . the U.S. insurance market is daunting, but policyholders of all types generally are well served.

In its January 14, 2002, issue, *Business Insurance* reported a surge in surplus lines business in 2001, particularly following the terrorist attacks in the United States on September 11, 2001, reflecting withdrawal of a number of standard carriers from a variety of property and casualty lines.

To be sure, encompassing 56 jurisdictions—each with its own mix of laws and regulations written in more than one language—the U.S. insurance market is daunting, but policyholders of all types generally are well served. Speaking in broad terms, the principal concern of individual and small-business insurance buyers is consumer protection, while that of larger businesses and professional institutions is availability of reasonably priced, effective coverage. The U.S. regulatory environment addresses both: it provides consumer protection at the local level and, through its surplus lines market, a deregulated global specialty market. Debate over federalization of insurance regulation is as old as regulation of the industry. Everyone expects the debate to continue; no one expects that federalization will occur. The surplus lines industry is here to stay. ■

Editor's note: Additional information on U.S. regulatory environment and surplus lines can be found at:

- Florida Surplus Lines Association
- Florida Surplus Lines Service Office
- National Association of Insurance Commissioners
- National Association of Professional Surplus Lines Offices, Ltd.
- Surplus Lines Association of California
- Surplus Lines Stamping Office of Texas
- Texas Surplus Lines Association, Inc.

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