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Department of the Treasury

**31 CFR Part 50
Terrorism Risk Insurance Program;
Claims Procedures; Final Rule**

DEPARTMENT OF THE TREASURY**31 CFR Part 50**

RIN 1505-AB07

**Terrorism Risk Insurance Program;
Claims Procedures****AGENCY:** Departmental Offices, Treasury.**ACTION:** Final rule.

SUMMARY: The Department of the Treasury (Treasury) is issuing this final rule as part of its implementation of title I of the Terrorism Risk Insurance Act of 2002 (Act). The Act established a temporary Terrorism Insurance Program (Program) under which the Federal Government will share the risk of insured loss from certified acts of terrorism with commercial property and casualty insurers until the Program ends on December 31, 2005. This rule was published in proposed form on December 1, 2003, for public comment. The final rule contains certain definitions, requirements, and procedures for insurers filing claims with Treasury for payment of the Federal share of compensation for insured losses under the Program. In particular, the final rule addresses requirements for Federal payment, initial notice of insured loss, loss certifications, the timing and process for payment, associated recordkeeping requirements, and Treasury's audit and investigation authority.

DATES: This final rule is effective July 29, 2004.

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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 in 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, including the issuance of regulations and procedures. The Program will end on December 31, 2005. Thereafter, the Act provides Treasury with certain continuing authority to take actions as necessary to ensure payment, recoupment, adjustments of compensation and reimbursement for insured losses arising out of any act of terrorism (as defined under the Act) occurring during the period between November 26, 2002, and December 31, 2005.

Each entity that meets the 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 to be determined based upon insurance company deductibles and excess loss sharing with the Federal Government, as specified by the Act and the implementing regulations. An insurer's deductible increases each year of the Program, thereby reducing the Federal Government's share prior to expiration of the Program. An insurer's deductible is calculated based on a percentage of the value of direct earned premiums collected over certain statutory periods. Once an insurer has met its deductible, the Federal payments cover 90 percent of insured losses above the deductible, subject to an annual industry-aggregate limit of \$100 billion.

The Program provides a Federal reinsurance backstop for three years. The Act provides Treasury with authority to recoup Federal payments made under the Program through policyholder surcharges, up to a maximum annual limit. The Act also prohibits duplicate payments for insured losses that have been covered under other Federal programs.

The mandatory availability or "make available" provisions in section 103(c) of the Act require that, for Program Year 1, Program Year 2, and, if so determined by the Secretary of the Treasury, for Program Year 3, all entities that meet the definition of insurer under the Program must make available in all of their commercial property and casualty insurance policies coverage for insured losses resulting from an act of terrorism. This coverage cannot differ materially from the terms, amounts and other coverage limitations applicable to losses arising from events other than acts of

terrorism. On June 18, 2004, the Secretary of the Treasury announced his decision to extend the make available requirements through Program Year 3.

As conditions for Federal payment under the Program, insurers must provide clear and conspicuous disclosure to the 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. In addition, the Act requires that insurers make certain certifications to Treasury and process and submit claims for the insured loss in accordance with appropriate business practices and any reasonable procedures Treasury may prescribe.

The Act also contains specific provisions designed to manage litigation arising out of or resulting from a certified act of terrorism. Among other provisions, section 107 creates, upon certification of an act of terrorism by the Secretary, an exclusive Federal cause of action and remedy for property damage, personal injury, or death arising out of or relating to an act of terrorism; preempts certain State causes of action; provides for consolidation of all civil actions in Federal court for any claim (including any claim for loss of property, personal injury, or death) relating to or arising out of an act of terrorism; and provides that amounts awarded in actions for property damage, personal injury, or death that are attributable to punitive damages are not to be counted as "insured losses" and not paid under the Program. The Act also provides the United States with the right of subrogation with respect to any payment or claim paid by the United States under the Program.

In implementing the Program, Treasury is guided by several goals. First, Treasury strives to implement the Act in a transparent and effective manner that treats comparably those insurers required to participate in the Program and provides necessary information to policyholders in a useful and efficient manner. Second, in accord with the Act's stated purposes, Treasury seeks to rely as much as possible on the State insurance regulatory structure. In that regard, Treasury has coordinated the implementation of all aspects of the Program with the National Association of Insurance Commissioners (NAIC). Third, to the extent possible within statutory constraints, Treasury seeks to allow insurers to participate in the Program in a manner consistent with procedures used in their normal course of business. Finally, given the temporary and transitional nature of the Program, Treasury is guided by the Act's

goal that insurers develop their own capacity, resources, and mechanisms for terrorism insurance coverage when the Program expires.

B. Previously Issued Interim Guidance and Regulations

To assist insurers, policyholders, and other interested parties in complying with immediately applicable requirements of the Act prior to the issuance of regulations, Treasury promptly issued interim guidance. The interim guidance addressed certain immediately applicable provisions that required clarification and was to be relied upon by insurers until superseded by regulations or a subsequent notice.

Treasury's first notice of Interim Guidance was published in the **Federal Register** at 67 FR 76206 on December 11, 2002, and addressed, among other matters, statutory disclosure obligations of insurers as conditions for Federal payment under the Program; the requirement that an insurer "make available" terrorism insurance; and how insurers were to calculate the "direct earned premium" received from commercial lines of property and casualty insurance as well as their "insurer deductibles" for purposes of the Program. The second notice of interim guidance was published at 67 FR 78864 on December 26, 2002, and provided guidance concerning which insurance companies were "insurers" for purposes of the Program, including their "affiliates." It also addressed the scope of insured losses covered by the Program and calculation of insurer deductibles. Treasury's third notice of interim guidance was published at 68 FR 4544 on January 29, 2003. It clarified certain disclosure and certification requirements, and addressed issues concerning non-U.S. insurers, and the scope of the term "insured loss" under the Act.¹ These interim guidance notices have now been superseded by a series of interim final and final regulations issued by Treasury.

On February 28, 2003 (68 FR 9804) Treasury published an interim final rule that laid the groundwork for Program implementation, including the scope of the Program and key definitions. This interim final rule was finalized and published in the **Federal Register** at 68 FR 41250 (July 11, 2003) (as amended at

68 FR 48280 (Aug. 13, 2003)) and created subpart A of part 50 in title 31 of the Code of Federal Regulations. Treasury's second interim final regulation created subparts B and C of part 50 and addressed disclosures that insurers must make to policyholders as a condition for Federal payment under the Act, and requirements that insurers make available, in their commercial property and casualty insurance policies, terrorism risk coverage for insured losses under the Program. It was published in the **Federal Register** at 68 FR 19301 (Apr. 18, 2003). After review of comments, this interim final rule was finalized and published at 68 FR 59720 (Oct. 17, 2003).

Treasury has also issued a regulation applying the Act to State residual market insurance entities and State workers' compensation funds. In this regard, Treasury created a subpart D to part 50 of title 31, which was first proposed and published in the **Federal Register** at 68 FR 19309 (Apr. 18, 2003). After review of comments Treasury finalized and published this rule at 68 FR 59715 (Oct. 17, 2003).

C. The Proposed Rule (Claims Procedures)

The proposed rule on which this final rule is based was published in the **Federal Register** at 68 FR 67100 on December 1, 2003. In subpart F to part 50 of title 31, Treasury's proposed rule contained requirements and procedures for insurers that file claims for payment of the Federal share of compensation for insured losses resulting from a certified act of terrorism under the Act. In particular, the proposed rule revised the regulatory definition of "insured loss," provided for an initial notice of insured loss and loss certifications, set forth general requirements for Federal payment under the Program and addressed the timing and process of such payment. Subpart G addressed information to be retained related to the handling and settlement of claims to enable Treasury to perform financial and claim audits.

II. Summary of Comments and Final Rule

In the event that it had been necessary to activate the Program's claims procedures prior to the issuance of this final rule, Treasury was prepared to do so on an expedited basis. Such action, however, was not necessary and Treasury is now issuing this final rule after careful consideration of all comments received on the proposed rule and after consultation with the NAIC. While this final rule largely reflects the proposed rule, Treasury has

made several revisions and a number of clarifications based on the comments received.

Treasury received comments on the proposed rule from four national insurance industry trade associations, collectively, as well as individually, a national risk retention trade association, a national lender trade association, a national surety trade association, a national agent and broker association, a captive insurers association, three insurance companies, a group of London-based insurers, a consulting actuarial firm, a vendor of insurance services, and a legal firm representing captive insurers. As described in detail below, commenters generally agreed with the proposed rule. However, Treasury received many requests to add a process for advance payments and for clarification of specific payment requirements and processes. In response, Treasury has revised the proposed rule to allow advance payments under certain conditions. In addition, Treasury has clarified provisions in the proposed rule that pertain to loss certifications requirements, payments to affiliated groups, prohibitions on duplicative compensation from other Federal programs, and the adjustment and suspension or denial of payments. Several commenters also requested that Treasury add specific references in the claims rule for State residual market insurance entities and Treasury has done so in the final rule. The comments received and Treasury's revisions to the proposed rule are summarized below.

A. Definition of Insured Loss (Section 50.5)

The final rule amends the previously issued definition of "insured loss" at § 50.5(e) to clarify that certain loss adjustment expenses allocable to a specific underlying loss are part of an insurer's insured losses and will be included in the Federal share of compensation under the Program. This clarification follows customary practices of the insurance industry with regard to reinsured losses. The definition has also been amended by the final rule to clarify that an insurer's payments in excess of policy limits or payments due to an insurer's extra-contractual obligations will not be considered as an insurer's insured loss. In addition, because section 107(a)(5) of the Act explicitly states that punitive damages are not to be considered as insured losses, the definition has been further amended to exclude compensation to an insurer for any payments attributable to punitive damages.

¹ Treasury's fourth interim guidance, published at 68 FR 15039 on March 27, 2003, provided insurers a procedure by which they could seek to rebut a presumption of control established in Treasury's interim final regulations. The Interim Guidance has subsequently been superseded by a provision in the final rule for subpart A of part 50, title 31 published at 68 FR 41250 (July 11, 2003).

1. Allocated Loss Adjustment Expense

In § 50.5(e)(3) of the proposed rule, Treasury proposed to revise the definition of the term “insured loss” to include certain loss adjustment expenses incurred by an insurer in connection with insured losses, specifically those expenses “that are allocated and identified by claim file in insurer records, including expenses incurred in the investigation, adjustment and defense of claims, but excluding staff adjuster salaries and any allocations of other internal insurer expenses.” In the preamble to the proposed rule, Treasury noted that this was consistent with customary insurance industry business practices.

Three comments addressed the proposed rule’s treatment of these allocated loss adjustment expenses (commonly known in the insurance industry as ALAE) within the definition of insured loss. An insurance industry trade association commended Treasury noting that, “this is consistent with industry practices and certainly appropriate.” However, an individual insurance company commented that this description of ALAE would not provide equal indemnification to insurers employing staff adjusters versus those using outside, or independent, adjusters. Another insurer expressed concern that certain expenses would be excluded under § 50.5(e)(3) of the proposed rule. Expenses cited were, “traveling to investigate the site of a loss, attend an examination, or perform some other function related to a specific claim” if incurred by insurer staff adjusters.

Treasury has considered the comments presented and believes that the proposed rule generally reflected its intention to follow the Act’s objectives of a system of shared public and private compensation for insured losses, including the unpredictable adjustment expenses directly associated with such losses. In particular, Treasury believes that the treatment of staff salaries in the proposed rule remains consistent with the Congressional findings and purposes of the Act and treats insurers participating in the Program comparably. Expenses such as staff salaries and other internal insurer expenses that are known and incurred regardless of the occurrence of any certified act of terrorism are not suitable to be shared with the general taxpayers and thus are not included in the definition of insured loss.

The specific approach taken toward staff adjuster and other expenses in § 50.5(e)(3) of the proposed rule is consistent with accepted practices in

the reinsurance industry and with the broader objectives for the Act. However, for added clarity, Treasury has modified § 50.5(e)(3) in the final rule to specifically exclude “staff salaries, overhead, and other insurer expenses that would have been incurred notwithstanding the insured loss” from the definition of insured loss. Consistent with this approach, reasonable, allocated expenses for travel to investigate the site of a loss, attend an examination, or perform some other function related to the investigation, adjustment and defense of a specific claim, even if incurred by insurer staff adjusters, are included in the definition of insured loss.

2. Extra-Contractual Obligations

The proposed rule also revised the definition of “insured loss” to clarify that the Federal Government would not share in an insurer’s payment of extra-contractual damages. Extra-contractual obligations describe an insurer’s liability to pay damages to its insured or a third party due to the insurer’s breach of the insurance policy and/or negligent or bad-faith claims-handling conduct, including liability for punitive, exemplary, or special damages awarded or paid as a result of such conduct.

Several insurance industry trade groups commented that Treasury’s proposed rule should be revised to allow for the federal payment of extra-contractual obligations paid by an insurer. Extra-contractual obligations paid by an insurer are the result of an insurer’s conduct and are not part of “insured loss” or directly associated with adjusting the loss as is the case with ALAE. Accordingly, such losses are not to be paid under the Program. The final rule adopts § 50.5(4) of the rule as proposed, with some minor modifications to the language.

In commenting on extra-contractual obligations, one trade group stated that in the light of unique situations following an act of terrorism, insurers “may go beyond the contract language to indemnify an insured.” Such payments by an insurer would not be an “insured loss” because the paid loss is not covered by the terms and conditions of the insurance policy. Treasury considered the comment and has determined to adopt § 50.5(a)(6) of the proposed rule without change in the final rule.

3. Excess Policy Limits Payments

The definition of “insured loss” in the proposed rule did not include losses in excess of policy limits (known commonly in the insurance industry as XPL). XPL losses occur when the

liability of the insured to a third party is in excess of that policy limit but otherwise within the scope of the insurance coverage. Under certain circumstances, an insurer will pay XPL losses to or on behalf of its insured (*e.g.*, when an insurer fails to accept a settlement offer within policy limits and a jury later finds the policyholder liable in an amount in excess of policy limits). In the preamble to the proposed rule, Treasury specifically invited comments on whether Treasury should include XPL losses within the definition of “insured loss.”

One commenter who addressed the issue of XPL losses pointed out that excess of loss reinsurance treaties usually include clauses providing reinsurance coverage for XPL claims. Treasury recognizes that such clauses are sometimes negotiated into reinsurance treaties. However, Treasury had determined not to include such losses in the definition of “insured loss” because such excess losses are not part of “insured loss” or directly associated with adjusting the loss. Given the lack of additional reasons to include XPL, the final rule adopts Treasury’s proposed language, with a technical correction at § 50.5(e)(4)(iii).

4. Losses by State Residual Market Mechanisms

Three comments were received from insurance trade associations, submitted individually and collectively, concerning the proposed rule not specifically addressing losses by State residual market insurance entities and State workers’ compensation funds (hereafter referenced as State residual market mechanisms). The commenters offered language to explicitly include, in the definition of insured losses, those losses allocated on a proportionate share basis from a State residual market mechanism to a participating insurer. Treasury has determined that it is not necessary to amend the definition of insured loss for this purpose, but has addressed this issue through clarifications to §§ 50.50 and 50.53 regarding the treatment of residual market losses. These changes are discussed below.

B. Federal Share of Compensation (Section 50.50)

The final rule provides that the Federal share of compensation under the Program is 90 percent of that portion of the insurer’s insured losses that exceed its insurer deductible during a Program Year, subject to specified adjustments and the annual industry aggregate limit of \$100 billion as provided in the Act. This section also

addresses requirements for federal payment and situations under which Treasury may deny or suspend payment.

1. General Clarifications

In § 50.50(a), Treasury has revised the proposed rule to clarify that the Federal share of compensation will be paid once a Certification of Loss required by § 50.53 of the final rule is deemed sufficient. Section 50.50(a)(1) was changed slightly to make clear that the insurer, including all affiliates of the insurer, must meet the requirements of § 50.5(f). Also, § 50.50(a)(4) has been revised to clarify that Treasury will pay so long as the underlying insured loss—as well as the insurer's claim for Federal payment—is not fraudulent, collusive, made in bad faith, or dishonest. In addition, under § 50.50(4) of the final rule, neither the underlying claim for insured loss nor the insurer's claim will be paid if Treasury determines that the claim is designed to circumvent the purposes of the Act and regulations. This is intended to discourage those who may attempt to "game" the Program.

Section 50.50(a) of the proposed rule provided that payment of the Federal share of compensation would occur upon Treasury making a determination as to the factors listed therein. This section of the proposed rule provided that Treasury may make a payment without this determination, subject to a "reservation of rights." As that term is commonly understood in the insurance industry, payment subject to a "reservation of rights" facilitates prompt payment because the payment is not construed as a waiver by the payee of any preconditions to payment. Although Treasury has eliminated the "reservation of rights" language in the final rule, Federal payment is still subject to Treasury's statutory authority as administrator of the Program to examine, or re-examine the factors listed in § 50.50(a) as part of a claims review or audit. This is now reflected in § 50.50(b) of the final rule. Treasury has statutory authority to subsequently adjust, or require repayment of any federal payment under the Act.

2. State Residual Market Mechanisms

As previously noted in the discussion of § 50.5, Treasury received comments with regard to the distribution of losses to participating insurers from State residual market mechanisms described in section 103(d)(2)(B) of the Act. A comment jointly provided by four insurance industry trade associations suggested that the proposed rule be revised to recognize losses paid by

participating insurers as their share of residual market losses. Treasury concurs with the need to clarify the treatment of losses paid as a share of residual market losses. Section 50.50(a)(2) has been revised to make clear that the insurer's insured losses include "the allocated dollar value of the insurer's proportionate share of losses from a State residual market entity or State workers' compensation fund."

3. Advance Payments

Section 50.50(a) of the proposed rule provided that the amount of payment of the Federal share of compensation would be based, in part, upon a Treasury determination that, the "insurer has made payment of an underlying insured loss to a person who had suffered the insured loss, or to a person acting on behalf of such person * * *." This proposed an approach whereby Treasury would pay the Federal share of compensation strictly as a reimbursement for amounts actually paid by insurers for underlying insured losses, whether fully or partially settled. This approach was also followed in § 50.53 of the proposed rule (Loss Certifications), which required, in part, a certification that the insurer had paid all underlying claims comprising the insured losses submitted for payment, as listed in the bordereau provided pursuant to § 50.53(b)(1).

Treasury received six comments on the timing of Federal payments. With some variation, the common theme was the issue of whether an insurer would receive the Federal share of compensation before or after the insurer's payment of underlying insured losses. The commenters, one insurer, three trade associations and one law firm on behalf of a trade association, contended that adherence to the pure reimbursement approach is not required by the Act. It was asserted that insurers may need to receive the Federal share of compensation for an insured loss in advance of their actual payment because of liquidity problems, particularly in the financial environment following a certified act of terrorism. The commenters explained that reinsurance industry practice permits advance or simultaneous payments subject to certain controls.

Treasury carefully considered these comments and determined that there may be some circumstances in which it would be appropriate for Treasury to advance payment for the Federal share of compensation for insured losses. Section 104(b)(2) of the Act authorizes the issuance of rules or procedures specifying the manner in which payments of the Federal share of

compensation may be made based on estimates of insured losses. In the final rule, Treasury has revised § 50.50 of the proposed rule to permit insurers to include on their bordereau requests for payment of the Federal share of compensation for both (1) claim payments already made, and (2) claim payments about to be made. This applies to partial as well as final settlements of underlying claims that comprise an insurer's insured losses.

Under the final rule, insurers are required to certify that any advances for underlying insured losses that have been requested will be paid within five business days of receipt of funds from Treasury. In addition, any interest earned on such funds will be remitted to the Treasury. Treasury believes that this provides an appropriate balance between meeting the cash flow needs of participating insurers and the proper stewardship over public funds.

To permit advanced payments, § 50.50(a)(3) of the proposed rule has been revised in the final rule to recognize that an insurer "has paid or is prepared to pay an underlying insured loss." Section 50.53(b)(2)(i) also has been revised to provide that underlying losses on the insurer's bordereau "either: Have been paid by the insurer; or will be paid by the insurer upon receipt of an advance payment of the Federal share of compensation as soon as possible, consistent with the insurer's normal business practices, but not longer than five business days after receipt of the Federal share of compensation." Also, a new subsection (d) has been added to § 50.54 Payment of the Federal Share of Compensation, that requires insurers seeking advanced payments to establish segregated interest-bearing accounts for the receipt of such payments and for the disbursement of those payments to insureds and claimants.

4. Full Payment for All Insured Losses

One comment was received from a trade association that understood the proposed rule as requiring insurers to make payment in full of all insured losses before becoming eligible for the Federal share of compensation. This is a misreading of the proposed rule and no change to the rule is required.

5. Denial or Suspension of Payment

Section 50.62 of the proposed rule provided generally that an insurer may be ineligible to receive payment of the Federal share of compensation for insured losses upon a determination by Treasury that the insurer intentionally concealed or misrepresented any material fact or circumstance, engaged

in fraudulent conduct, or made false statements relating to participation under the Act.

A national insurance trade association commented on § 50.62. This commenter noted that section 103(b) of the Act sets forth the grounds under which an insurer may be ineligible to receive Federal payments and that section 104(e) of the Act provides Treasury with civil money penalty authority. If any of the conditions for payment of the Federal share in section 103(b) have not been met with respect to a particular insured loss, the commenter suggested that the appropriate response of Treasury would be to deny payment for that insured loss. Similarly, the commenter suggested that if there is wrongdoing, such as fraud or misrepresentation, Treasury could assess civil money penalties under section 104(e) of the Act. The commenter concluded that these provisions "cover the landscape of potential offenses" and thus viewed the provisions of § 50.62 to be overbroad. The commenter recommended that § 50.62 be deleted or revised.

Treasury concurs that sections 103(b) and 104(e) provide Treasury with broad authority to deny or suspend payment and/or to assess civil money penalties in connection with insurer requests for payment of the Federal share of compensation under the Act. Treasury has determined to delete § 50.62 as the commenter requested and to address certain issues through revisions to § 50.50.

Treasury believes there may be circumstances where failure to meet one of the requirements for payment of the Federal share of compensation with respect to one insured loss may be an indication of a broader pattern or practice of malfeasance or wrongdoing on the part of the insurer with regard to its other claims for insured losses. To address this, Treasury has added a new subsection (c) to § 50.50 that provides, in Treasury's discretion, for suspension of payment for other insured losses of an insurer if the insurer fails to meet one of the requirements in § 50.50(a). In such cases, Treasury may decide to conduct additional review and investigation of the insurer's Loss Certification submissions before paying the Federal share of compensation.

C. Adjustments to the Federal Share of Compensation (Section 50.51)

The final rule specifies several adjustments in calculating the Federal share of compensation. First, the rule reduces aggregate insured losses by amounts recovered by insurers for salvage and subrogation. Second, the

rule provides that, should the amount of an insurer's Federal share of compensation from the Program and the amount of recoveries from other sources exceed the aggregate amount of its insured losses in a Program Year, then any excess recovery must be returned to Treasury. Excluded from this requirement are recoveries from a reinsurer pursuant to an agreement whereby an insurer's obligation to repay its reinsurer takes priority over its obligation to repay Treasury. Third, the rule in § 50.51 follows the Act's requirement that the Federal share of compensation for insured losses be reduced by any duplicate amount of compensation otherwise provided by the Federal government for those insured losses.

1. Salvage and Subrogation

Treasury received three comments on the salvage and subrogation provisions of 50.51(a). One commenter, an insurer, noted that the preamble to the proposed rule expressed Treasury's expectation that, "as normal good business practice, insurers will pursue salvage and subrogation." The commenter was concerned that this language and the proposed rule did not explicitly address the flexibility of the insurer to use its own business discretion to pursue, abandon or forego salvage and/or subrogation efforts. Treasury believes that normal business practice requires the use of discretion in determining salvage and/or subrogation efforts. Treasury does not believe a change to the proposed rule is required and expects insurers to use the appropriate discretion in pursuing salvage and/or subrogation opportunities.

This same commenter requested clarification regarding the cost of pursuing salvage and/or subrogation. The rule states that the insurer's aggregate insured losses used to calculate the Federal share of compensation shall be reduced by any salvage or subrogation recoveries. Treasury agrees that insurers should be able to recover the costs of pursuing salvage and subrogation actions. It is expected that these expenses will be included by insurers in Allocated Loss Adjustment Expenses. Because such reasonable expenses are included in the definition of insured loss, Treasury sees no need to further change the rule to resolve this issue. Additional guidance on the treatment and netting of expenses will be included in the definitions for the fields reported on the bordereau form submitted with the Certifications of Loss.

A trade association commented that some insurers do not currently capture

salvage and subrogation recoveries independent of one another and sought relaxed reporting requirements. Treasury prefers to receive this information separately, but in the interest of minimizing changes to insurers' existing processes Treasury will accept reports with salvage and subrogation recoveries combined or separate. This accommodation will be accomplished in the bordereau format and instructions which are soon to be published (along with other forms) for public comment.

2. No Excess Recoveries

Section 50.51(b)(1) of the proposed rule provided that in any Program Year the sum of the Federal share of compensation paid to an insurer and the insurer's recoveries for insured losses from other sources shall not be greater than the insurer's aggregate losses for acts of terrorism in that Program Year. This is consistent with section 103(g)(2) of the Act.

One commenter suggested that ceding commissions received by an insurer in reinsuring its deductible and retentions under the Act could be considered part of an insurer's recovery. Ceding commissions are compensation from a reinsurer to a ceding insurer for the costs of writing underlying policies and are paid regardless of whether claims are ever submitted. It is Treasury's view that ceding commissions are not recoveries from other sources for insured losses and, therefore, the Federal share of compensation shall not be reduced by such commissions. No change has been made to the proposed rule in this regard.

Section 50.51(b)(1) of the proposed rule also provided that amounts recovered for insured losses in excess of an insurer's aggregate amount of insured losses in a Program Year be repaid to Treasury within 45 days after the end of the month when such amounts are received by the insurer. A trade association commented that it may take a long time after actual receipt of recoveries before an insurer is able to determine whether a recovery is excess. The commenter suggested that repayment be required 45 days after the insurer becomes aware that the recovery is excess.

Treasury recognizes that the determination of a recovery being excess may occur some time after the actual receipt of that recovery. However, Treasury believes that the commenter's alternative, based on when the insurer becomes "aware" of any excess recovery, is too vague to establish a definitive schedule for the repayment of funds. The final rule has been clarified

in § 50.51(b)(1) so that amounts recovered for insured losses in excess of an insurer's aggregate amount of insured losses in a Program Year are to be repaid to Treasury based on when total recoveries of the insurer, from all sources, become excess.

3. Compensation From Other Federal Programs

Section 103(e)(1)(B) of the Act states, "The Federal share of compensation for insured losses under the Program shall be reduced by the amount of compensation provided by the Federal Government to any person under any other Federal program for those insured losses." To implement this statutory provision, § 50.51(b)(2) of the proposed rule stated, "The Federal share of compensation due an insurer for insured losses shall be reduced by any amounts received by the insurer or an insured or a third party suffering the underlying loss from any other Federal programs as compensation for those insured losses, including, but not limited to, insurance, assistance, grants or disaster relief from the Federal Government." Nine comments addressed § 50.51(b)(2). After consideration of the comments and upon further analysis, Treasury has made several revisions in the final rule and is providing additional explanation in this preamble for greater guidance.

As a preliminary matter, Treasury has made a few technical corrections to the final rule. The proposed rule explained that any reduction would be based on the amount of compensation received by the insurer or an insured or a third party suffering the underlying loss. This provision in the final rule no longer makes reference to amounts received or compensation provided to insurers. This is because amounts received by insurers are covered in § 50.51(b)(1), which addresses recoveries by insurers from all other sources, including compensation received by the Federal Government. Second, the language of 50.51(b) is being revised from "any amounts received by" to "compensation provided by other Federal programs to" an insured or a third party to parallel the statutory language found in section 103(e)(1)(B) of the Act.

a. *Types of Compensation Used To Reduce the Federal Share.* In its proposed rule, Treasury described the type of compensation provided by other Federal programs in reducing the Federal share of compensation to insurers as "insurance, assistance, grants, or disaster relief." In its final rule, Treasury is providing clearer guidance on what constitutes compensation provided by other Federal

programs for insured losses. Section 50.51(b)(2)(i) of the Final Rule provides that compensation provided by other Federal programs for insured losses means compensation that is provided by Federal programs established for the purpose of compensating persons for losses in the event of emergencies, disasters, acts of terrorism, or similar events. Compensation provided by other Federal programs that could be considered duplicate compensation include, but are not limited to, compensation provided under Federal programs such as:

- Federal Emergency Management Agency (FEMA) disaster relief and emergency assistance;
- Department of Housing and Urban Development block grant assistance; and
- Federal programs specially established to compensate victims for losses resulting from the certified act of terrorism (similar to the September 11th Victim Compensation Fund of 2001 (Pub. L. 107-42, 115 Stat. 237, § 401 *et seq.*)).

However, it is Treasury's view that Congress did not intend to reduce the Federal share of compensation due to receipt of Social Security disability payments and other similar benefits. Accordingly, § 50.51(b)(2)(i) of the final rule provides that compensation provided by Federal programs for insured losses excludes benefit or entitlement payments such as those made under the Social Security Act, those made under laws administered by the Secretary of Veteran Affairs, railroad retirement benefit payments, and other types of similar benefit payments. These types of Federal entitlement or benefit payments to individuals are the result of services performed and are paid irrespective of whether the loss occurs as a result of an act of terrorism. Under the final rule they are not treated as duplicate compensation for insured losses arising from an act of terrorism and shall not be used by Treasury to reduce the Federal share of compensation due an insurer.

b. *Statutory Requirement That the Federal Share Be Reduced.* Several commenters criticized the Act's requirement that the Federal share of compensation be reduced by compensation provided by the Federal Government under other Federal programs for insured losses. Several commenters acknowledged that it is a legitimate goal that no one should receive a double recovery for a loss. In developing this rule, Treasury understands that its reduction of the Federal share of compensation does not, in turn, reduce the amount insurers are obligated to pay under the terms and

conditions of their insurance policies. This was pointed out by several commenters. Nevertheless, Treasury must follow the Act.

Based upon a review of how several other Federal programs would likely treat proceeds from "property and casualty insurance," under the Act or otherwise, Treasury expects that duplicative compensation situations will be rare. This is because the most likely Federal programs identified by Treasury as potential sources of duplicate payments already guard against duplicate compensation.

For example, HUD and FEMA programs offset their payments by insurance proceeds received or expected to be received by their applicants. These programs also have procedures to recoup their payments from recipients of assistance to the extent those recipients later receive insurance proceeds. Further, it is expected that Congress will include mechanisms to prevent double Federal recovery in programs designed to help victims of future acts of terrorism, much in the same way the September 11th Compensation Fund of 2001 treats collateral source payments. Moreover, any payments from other Federal insurance programs should be offset by operation of the "other insurance" clauses in insurers' standard policy forms for commercial property and casualty insurance. Finally, insurers themselves can discount settlement offers to reflect payments received from other Federal programs and in that way avoid the problem of compensation being duplicative. For claims that do not settle and proceed to award, some states allow or require reductions based on collateral source payments.

One commenter acknowledged that the proposed rule generally follows section 103 of the Act, but nevertheless concluded that section presents a "serious contractual problem" for insurers because insurance contracts do not allow for any reduction of amounts paid to insureds, other than for payments made under other insurance policies. Also, the commenter explained that because insurers cannot forecast the amount by which their payment will be reduced, insurers cannot factor the reduction into the price of their premiums. The commenter suggested that § 50.53(b)(1) of the proposed rule be revised by deleting the words "or insured or third party suffering the underlying loss" or if that is not possible, that the Federal Government require that the insured reduce the amount of its claim presented to the insurer.

Treasury has considered the comment but has determined not to accept either suggestion. The language in section 103 requires that Treasury reduce its payment to insurers by the amount of compensation provided "to any person" for those insured losses. Insureds or third party claimants who suffer the underlying insured loss are included in the definition of "person[s]," in section 102 of the Act. However, nothing in the Act or Treasury's regulations would prevent an insurer from pursuing changes to its policies (including obtaining any necessary State regulatory approval) in order to address this reduction and allow for possible offset.

Another commenter asserted that the proposed rule "is neither logical nor equitable, and does not serve the underlying purpose of 103(e)(1)(B)." According to the commenter, it was not the intent of Congress to transfer the risk of double recovery to insurers. The commenter does not believe there should be any reduction of the insurer's Federal payment but that insurers are willing to assist Treasury in identifying those persons that have received double Federal recovery for insured losses. Treasury does not share the commenter's view. The statutory language requires Treasury to reduce the Federal share of compensation by the amount of compensation provided by the Federal Government to any person under any other Federal program for insured losses.

This same commenter also suggested that the subrogation provisions of the Act are available to prevent double recoveries. Section 107(c) of the Act provides that the United States shall have the right of subrogation with respect to any payment or claims paid by the United States under title I of the Act. Upon payment to an insurer, the United States becomes subrogated to the rights of the insurer (to the extent of the payment). Yet, as many of the commenters pointed out, the terms and conditions of standard commercial property and casualty policies do not provide the insurer with any right of offset or recoupment of amounts paid by other Federal programs. Therefore, section 107(c) may not be effective in guarding against double Federal payment. Furthermore, even if the exercise of the United States' subrogation rights could avoid the Federal Government paying twice for the same loss, the commenter's approach shifts the responsibility to pursue subrogation to the United States. Under § 50.50(a)(6), insurers are to process claims in a manner consistent with appropriate business practices, which include pursuing subrogation

recoveries when appropriate. The responsibility to pursue recoveries though subrogation lies with the insurer in the first instance. The United States retains the ability to pursue such recoveries in the event the insurer does not.

c. Other Federal Compensation Already Offset in the Underlying Claim for Insured Loss. A trade association commented that the Federal share of compensation should not be reduced if in fact the payments by the other Federal program are already offset in the insurance claim to the insurer. If the insurance claim is already reduced, there is no duplicate compensation. The commenter is concerned that the proposed rule could be read to require the reduction of the payment to the insurer even though the insured or third party did not claim, and the insurer did not pay, for that part of the insured loss. To address this, the association recommended that Treasury clarify the proposed rule to make clear that there will be no reduction in Federal payments if the losses compensated for by the other Federal program are not also paid by the insurer. Based on the commenter's suggestion, language has been added to the final rule that clarifies the Federal share of compensation shall be reduced only "to the extent such other compensation duplicates the insurance indemnification for those insured losses." When the insurer's payment has not been offset, the Federal share shall only be reduced by the amount, if any, that the aggregate of the insurer's payment and the compensation from the other Federal program exceed the total loss. This is because the other compensation is not duplicating the payment for insured losses until there is an excess recovery.

The commenter also questioned what would happen in the situation where other Federal programs require their claimants to pursue other recoveries (such as insurance proceeds) and then to repay the other program. Would the insurer be credited for any repayment to the other Federal program? In such a situation, the Federal share of compensation would be reduced pending the claimant's repayment to the other Federal program. Once the claimant repays the other Federal program, presumably out of the insurance proceeds, the Program will pay the insurer the amount of the reduction. This will occur after the other Federal program notifies Treasury that the recipient of the insurance proceeds has repaid the other Federal program.

d. Insurer Due Diligence. Section 50.51(b)(2) of the proposed rule stated,

"Each insurer shall inquire of each of its claimants whether or not duplicate payments for insured losses have been paid from other Federal sources. Such amounts shall be reported with each underlying claim on the bordereau specified in § 50.53(b)(1) and the total amount subtracted from the aggregate amount claimed as the Federal share of compensation for insured losses." Generally, all of the commenters viewed this information collection requirement as reasonable. Three commenters addressed the information insurers would need to obtain from claimants and suggested various approaches and forms to be used by insurers to collect information about duplicate compensation from other Federal sources. Treasury will be issuing a notice and publishing forms for public comment at a later date.

Another commenter pointed out that the proposed rule did not address the situation where an insurer pays a claim before the person receives compensation from another Federal program. This may occur when the person has not yet applied for such compensation from the other program despite being eligible or the person later becomes entitled to compensation (e.g., a program set up at a later date). Having considered this comment, Treasury has modified the rule to require insurers to inquire of their policyholders, insureds, and claimants not only whether the person receiving the insurance proceeds has received compensation from another Federal program but also whether it expects to receive, or is entitled to receive compensation from another Federal program for the insured loss, and if so, the source and amount of the compensation received or expected. An insurer will be expected to collect this information at the time of claims settlement. Consistent with the insurance industry's business practice, Treasury will not require the insurer to re-open its closed claim file simply to collect this information, which can be obtained from the other Federal programs.

Although § 50.51(b)(2)(ii) of the final rule requires insurers to inquire about duplicate compensation—expected, as well as received—the Federal share of compensation will be reduced only by those amounts actually provided by the other Federal program. If a person informs an insurer that it has not yet received but expects to, or is entitled to receive compensation for another Federal program for the insured losses, Treasury will notify the other Program.

Another commenter, a "federally approved" insurer, commented that it would not have to inquire about

duplicate Federal compensation because awards under the Longshore and Harbor Workers' Compensation Act ("LHWCA") (33 U.S.C. 901, *et seq.*) already take such payments into account. In such a situation, however, the final rule will still require the insurer to inquire about possible duplicate compensation since there may be sources of Federal payments for LHWCA claimants that are not taken into account under that Act.

e. *False Information Submitted to the Insurer.* Another commenter asserted that insurers have no way of ensuring that its policyholders, insureds, or claimants will reveal information concerning duplicative payments. The comment suggested that Treasury add penalties or warn persons attempting to collect twice. The final rule only requires that insurers inquire concerning duplicate compensation and report the response received. If Treasury learns that a person who has received an insurance payment shared by the Program has also received compensation for those insured losses from another Federal program, the insurer's Federal share of compensation shall be reduced.

4. Claims Handling

A commenter referenced § 50.51(b)(2) as well as § 50.51(a) and asserted that the regulations should "make it clear that the Treasury does not wish to exercise any authority over claims handling." The commenter's observation is incorrect. Treasury is responsible for the financial integrity of the Program. Section 50.50, which provides the basis for Treasury to determine the amount of the Federal share of compensation to insurers, is designed to allow Treasury to review the insurer's handling of underlying claims for insured losses. For example, § 50.50(a)(6) provides that Treasury will examine whether the insurer took all steps reasonably necessary to properly and carefully investigate the underlying insured loss and otherwise processed the underlying loss using appropriate insurance business practices. Section 50.50(a)(7) indicates that Treasury will review whether the insured losses submitted for payment are within the scope of coverage issued by the insurer. In order for it to properly carry out its financial responsibilities, Treasury will, as needed, audit insurer requests for compensation, including the handling of underlying claims, as provided in subpart G of the rule.

D. Initial Notice of Insured Loss (Section 50.52)

The final rule includes an early notification requirement when an

insurer obtains information indicating its insured losses will exceed 50 percent of its insurer deductible as defined by the Act. At that time, the insurer is required to submit, on a form prescribed by Treasury, estimates of aggregate losses for the Program Year, its insurer deductible and the Federal share of aggregate losses, as well as the name of the person designated to make required certifications and receive Federal payments. Such information will assist in estimating funding levels for certified acts of terrorism and otherwise facilitate operations of the Program. Because the insurer deductible applies collectively to all insurers in an affiliated group, the notice must include the designation of a single insurance entity to coordinate the submission of required reports and documentation (including the Initial Notice of Insured Loss), make required certifications and receive Federal payments on behalf of the affiliated group.

No comments were received specific to this section of the proposed regulation. However, as a result of changes made to § 50.54 in response to comments regarding the designated single payee in an affiliated group, this section has also been revised. The Initial Notice of Insured Loss is to include a "designated insurer" as a single point of contact in an affiliated group for "receiving, disbursing, and distributing" payments of the Federal share. This issue is more fully addressed in the discussion of § 50.54 below.

E. Loss Certifications (Section 50.53)

The final rule specifies the type of loss information that an insurer is required to submit in documenting insured losses eligible for payment of the Federal share of compensation. An Initial Certification of Loss, on a form prescribed by Treasury, is required when insured losses first exceed the insurer's deductible. If the insurer sustains ongoing, additional insured losses, periodic Supplementary Certifications of Loss, on a form prescribed by Treasury, must be submitted. These Certifications of Loss will be used by Treasury to assess payment eligibility for the Federal share of compensation and compliance with the Act's prerequisites for payment. The rule also addresses various written certifications the Act requires as a condition for payment of the Federal share. Specific statements certifying actions by the insurer as required by the Act, and by Treasury in administering and implementing the Act, are to be included as part of each Certification of Loss.

One revision to the proposed rule has been made to this section solely to add clarity. The definition of a bordereau, formerly § 50.53(e), has now been included in § 50.53(b)(1).

1. Timing of Submission of Initial Certification of Loss

In § 50.53(b) of the proposed rule, Treasury proposed that an insurer "use its best efforts to file the Initial Certification of Loss with Treasury within 45 days following the last calendar day of the month when an insurer's aggregate insured losses exceed its insurer deductible." One insurer trade organization commented that an insurer may not be able to file the initial certification of loss within that time period and that a time requirement is not really necessary. Alternatively, it suggested that Treasury modify the rule to allow insurers to request an extension of time to submit the Initial Certification of Loss.

The proposed rule provided for insurers to use their "best efforts" to submit the Initial Certification of Loss within 45 days. The proposed rule did not establish a fixed deadline that would serve as the basis to deny a claim for federal payment. Thus, a special request for an extension of time is not necessary so long as the insurer has used its best efforts to meet the requirement. Treasury believes this is reasonable. The objective of the rule is to encourage timely reporting of losses so that Treasury remains as current as possible with its potential liabilities. Generally, it will be in the insurer's interest to report losses as soon as possible. Accordingly, Treasury has made no change to the proposed rule.

The trade group also recommended that the loss certification process should specifically recognize special circumstances associated with large deductible policies. The commenter noted that with large deductible policies, particularly in workers compensation, insurers will typically first pay the entire claim to the insured worker and then recover the deductible from the insured employer. Treasury agrees that this comment regarding large deductible policies merits attention and will address the concern in the development of the actual loss certification reporting forms.

2. Certification Language

Two insurance trade associations and an insurer commented on the certification required in proposed rule § 50.53(b)(2)(iv) dealing with the clear and conspicuous disclosures that insurers are required to provide to policyholders. The commenters noted

that the certification requirement appeared to impose a more stringent standard than was promulgated in previously issued regulations, in that insurers are required to certify they have “complied with the disclosure requirements * * * for each underlying loss.” They suggested the use of less demanding certification language that would allow insurers to rely on “systems and normal business practices that demonstrate a practice of compliance” with the mandatory disclosure requirement as referenced in § 50.12(e).

Treasury does not believe that the compliance language of § 50.53(b)(2)(iv) is inconsistent or more stringent than the “normal business practices” approach in § 50.12(e). The compliance language of § 50.53(b)(2)(iv) means that for each underlying loss an insurer would be able to demonstrate it made an individual disclosure because it had a reliable system in its normal business practice that generated disclosures. For this reason, Treasury has decided to not change the certification language of § 50.53(b)(2)(iv).

One insurance trade association suggested deletion of the requirement in § 50.53(b)(2)(v) of the proposed rule to certify compliance with the Act’s mandatory availability requirements because, in the commenter’s view, there is no specific statutory requirement for the certification as a condition for payment. The mandatory availability or “make available” provisions in section 103(c) of the Act require that, for Program Years 1 and 2, and if so determined by Treasury for Program Year 3, all insurers must make available in all of their property and casualty insurance policies coverage for insured losses resulting from an act of terrorism. This coverage cannot differ materially from the terms, amounts, and other coverage limitations applicable to losses arising from events other than acts of terrorism. Under its authority in section 104(a)(2) of the Act to effectively administer and implement the Program, Treasury believes it is appropriate to include the certification requirement in § 50.53(b)(2)(iv). The “make available” requirement is, as the commenter also acknowledged, an “important predicate to the proper functioning of [the Act].” For this reason, Treasury has made no change in making the rule final.

3. State Residual Market Mechanisms

As described earlier, Treasury revised § 50.50(a)(2) of the proposed rule to clarify that the proportionate share of insured losses from State residual market insurance entities or State workers’ compensation funds described

in § 50.35 (those that share profit and losses) are treated as the insured losses of the individual insurer participants of those State residual market mechanisms. Joint comments from the four insurer trade associations also raised issues regarding the certification of loss requirements for these entities in § 50.53(b)(2) of the proposed rule. The joint comments observed that the flow of information pertaining to insured losses of State residual market mechanisms was different than that of individual insurers. For example, commenters noted that knowledge about processing claims in accordance with “appropriate business practices” as required by section 103(b)(3) of the Act lies with State residual market mechanism servicing carriers and administrators, not the participating insurers who are assessed a proportionate share of insured losses of the State residual market mechanism. Consequently, the joint trade association comment recommended special treatment for the loss certification requirements of § 50.53(b)(2) for State residual market insurance entities and State workers’ compensation funds.

After considering the joint comments, as well as its own concerns with the mechanisms of information flow and content in connection with reconciling and auditing insured loss information of State residual market mechanisms, Treasury has added a new § 50.53(e) to the final rule to deal with loss certifications of State residual market mechanisms. Essentially, Treasury has sought to accommodate the special circumstances of State residual market mechanisms by separating the entity receiving payment (insurers participating in a residual market mechanism) from the entity with responsibility for providing certifications under section 103(b) of the Act (the residual market mechanism based on its own servicing or that of a servicing carrier).

In order to receive payment of the Federal share of compensation for residual market losses, an insurer participating in a State residual market mechanism will submit to Treasury, as an underlying loss on its bordereau, the amount of losses allocated to it by the State residual market mechanism. The State residual market mechanism will provide to its participating insurers the detailed underlying loss information that supports the total amount of insured losses from which the proportionate share of insured losses was calculated for each participating insurer. The State residual market mechanism will also provide to its participating insurers and to Treasury

the certifications required by §§ 50.53(b)(2) and 50.53(c)(2). To facilitate any needed review or audit pursuant to §§ 50.60 and 50.61, State residual market mechanisms and their individual participating insurers are both required to maintain insured loss information they received or provided, as well as any supporting documentation for certifications.

F. Payment of Federal Share of Compensation (Section 50.54)

The final rule establishes the process for making payment as provided by the Act. It also addresses the making of payments before the total amount of insured losses are known, providing for later adjustment based on any overpayment or underpayment. The rule specifies the types of insurer accounts required for Treasury to electronically transfer funds in making payments of the Federal share of compensation and, in the case of advance payments of the Federal share, establishes that interest earned on those funds must be remitted to Treasury. Because the Act requires insurance entities within an affiliated group to be treated as a single entity in determining the insurer deductible, the rule requires that all payments be made to a single insurance entity within an affiliated group. This entity is to be identified by the affiliated group and designated on the Initial Notice of Insured Loss. Applicable payment process procedures are to be posted at www.treasury.gov/trip or otherwise made publicly available.

1. Prompt Payment

Section 50.54(a) of the proposed rule provided that Treasury would “promptly” pay to an insurer the Federal share of compensation due the insurer for its insured losses and that any overpayments by Treasury of the Federal share will be offset from future payments to the insurer or returned to Treasury within 45 days. Three comments were received on the issue of prompt payment. One commenter was pleased with the rule as written. Two commenters asked that prompt payment be better defined. One of these commenters suggested that Treasury set a goal of processing and paying claims within 45 days of receipt of an Initial Certification of Loss or any Supplemental Certification if the losses being claimed are not in dispute. After considering these comments, Treasury does not believe a regulatory time limit for payment is necessary. Treasury intends to pay the Federal share of compensation due insurers as promptly as possible and believes this commitment in the provision of public

funds is sufficient. In seeking contractor support for the management of Program claims, Treasury has made this intention clear. Treasury has also clarified this section to specify that the payment process incorporates the use of electronic funds transfer through the Automated Clearinghouse (ACH) network. This provides a mechanism for the prompt disbursement of funds from Treasury to an insurer.

2. Advance Payments

As stated in the discussion of § 50.50, Treasury has revised this section in order to permit advance payments of the Federal share. Section 50.54 of the final rule describes the types of accounts required to be established by insurers to receive the Federal share of compensation. Treasury's control over the payment process is facilitated by having only one account per insurer into which payments will be made. If an insurer is only seeking reimbursement for insured losses it has already paid, then the only requirement for the account is the capability to receive electronic funds transfers over the ACH network. If an insurer seeks advance payments of the Federal share, or a combination of advance payments and reimbursement, then the account must be segregated from other insurer accounts. A "segregated account" is defined in section 50.54(d) of the final rule as an interest bearing, separate account at an institution eligible to receive payments through the ACH network and limited to the purposes of (i) receiving payments of the Federal share of compensation (ii) disbursing payments to insureds and claimants and (iii) transferring payments to the insurer or affiliated insurers for insured losses reported on the bordereau as already paid.

Payments to insureds and claimants that are made using funds advanced by Treasury are to be made directly from the segregated account. All interest earned on these advanced funds is to accrue through such time that payments from the account clear and is to be entirely remitted to Treasury. If it is determined that an insurer has not properly disbursed advances of the Federal share or otherwise not complied with these regulatory claims procedures, then Treasury may deny or withhold making advance payments of the Federal share of compensation.

3. Affiliated Group

Because the Act requires insurance entities within an affiliated group to be treated as a single entity in determining the insurer deductible, the proposed rule required that all payments be made

to a single insurance entity within an affiliated group. The proposed rule required this entity to be identified by the affiliated group and designated on the Initial Notice of Insured Loss. The proposed rule further required insurers within an affiliated group to assign their rights to receive payments of their Federal share of compensation to this designated single insurance entity, while requiring the single insurance entity to distribute such payments "as appropriate" among affiliated insurers in the group.

Four commenters addressed issues involving Treasury's payment of the Federal share of compensation to a single insurance entity on behalf of an affiliated group of insurers. One commenter expressed the view that it preferred that Federal payments go to the individual insurer making the underlying claim payment. In the alternative, the commenter recommended that, in order to prevent a designated insurer from withholding distribution to affiliates, at a minimum, the rule be revised to require the single insurance entity to distribute payments of the Federal share of compensation to affiliated insurers in the group or to hold those funds in trust for distribution to affiliated insurers in the group. This suggestion was echoed by a second commenter.

Another commenter criticized the assignment requirement in § 50.54(c) of the proposed rule. Because of the potential shift in statutory rights or corporate asset values resulting from this "compulsory assignment of rights," the commenter suggested a better approach would be to require each entity within an affiliated group to appoint a common agent within the group for submission of claims while retaining legal title in its own name to all proceeds. The commenter further suggested that the common agent be required to act in a fiduciary capacity on behalf of other affiliates.

A fourth commenter noted that the execution of assignment agreements will trigger holding company filing requirements pursuant to state insurance laws. The commenter observed that such filing requirements have been brought to the attention of the NAIC and expressed interest in working with both NAIC and Treasury "to craft an appropriate solution that will be convenient for all parties." As a result of this comment, Treasury consulted with the NAIC and devised a more flexible approach to the single payee/affiliated group provision than what was proposed.

In the final rule, Treasury has deleted the requirement that affiliated insurers

assign their rights to be paid under the Program to the single insurance entity in their affiliated group. Treasury has concluded that the proposed requirement of an assignment of rights may be an overly restrictive approach and that different mechanisms may be used among affiliate groups to assure proper distribution of the Federal share of compensation.

In addition, in § 50.54 of the final rule Treasury has clarified that the designated insurer receiving payments of the Federal share of compensation on behalf of an affiliated group must distribute payments in a manner that assures that other insurers in the group are compensated for their insured losses taking into account a reasonable and fair allocation of the group's insurer deductible. Because the insurer deductible for a group is an aggregate calculation based on the collective property and casualty insurance premium of all insurers in the group, Treasury recognizes there may be complexities and difficulties in determining individual insurer deductibles within the group. Treasury has thus provided guidance in requiring that the group deductible be allocated in a "reasonable and fair" manner among affiliated insurers. If necessary, Treasury will review the deductible allocation of an affiliated group, looking to the totality of the circumstances in determining what is "reasonable" and "fair." The final rule also clarifies that Treasury's obligation to pay the Federal share of compensation to affiliated insurers in a group is discharged upon its payment to the designated insurer, to the extent of the payment for insured losses of the group as reported on the group's bordereau. This provision does not prevent Treasury from subsequently adjusting payments, for example, as a result of an audit.

G. Audit Authority and Recordkeeping (Sections 50.60 and 50.61)

Sections 50.60 and 50.61 of the final rule require insurers to retain all records and files pertaining to the processing, handling, and settlement of insured losses, including electronic documents and data, and allow Treasury access in order to conduct subsequent financial, claims, and performance reviews and audits. Treasury and/or its appointed designee(s) will need access to pertinent books, files, agreements and records that support the insurer's Certifications of Loss previously submitted.

Three comments were received regarding the proposed §§ 50.60 Audit authority and 50.61 Recordkeeping. One commenter recommended that § 50.60 explicitly require the retention of

reinsurance and other relevant agreements and that they be available during audit. Treasury believes that the proposed language already required such information to be maintained and accessible. Thus, no change to the proposed rule was required. A second commenter requested that access to the records be provided "upon reasonable notice" to the insurer by Treasury. Treasury has added this language to the final rule. This commenter also recommended that the audit authority of § 50.60 be expressly limited to the records required to be kept under § 50.61. Treasury disagrees and declines to limit the records it may need to access during investigation, audit and examination.

A third commenter was concerned with the type and form of claims records to be maintained. The commenter observed that § 50.61 of the proposed rule only required that "records" of material matters pertinent to insured losses be retained, not actual claim files containing activities relative to the handling and adjustment of claims. The commenter further suggested that any records required to be retained beyond actual claim files be permitted to be stored in a limited form such as electronic data storage. Treasury is concerned with the availability of information needed for investigation, confirmation, audit and examination for the time periods specified in § 50.61, not the medium in which information is retained. Information that is material needs to be retained in whatever form that can provide reasonable access by Treasury. Treasury believes that insurers' normal claims and other record keeping methods, technology, and systems can be used to meet this requirement and the proposed rule does not need to be changed.

H. Other Issues

1. Future Issues

As Treasury explained in the preamble to the proposed rule, its strategy has been to give priority to regulations needed in the event of an act of terrorism. In addition to comments on the proposed claims rule, Treasury received several comments regarding aspects of insured losses resulting from certified acts of terrorism that were not included in the proposed rule. Comments were received concerning insurer insolvency, dispute resolution, commutation of losses, and the impact of losses exceeding the annual aggregate cap of \$100 billion specified by the Act. These are the types of secondary issues that Treasury intends to address as necessary through guidance or

supplementary rulemaking. Treasury will consider all the comments that have already been submitted in its development of pertinent future regulations.

2. Confidential or Privileged Information

A trade association commented that the proposed rule did not protect confidential or privileged information submitted to Treasury as part of the TRIA claim process. Any issues relating to the disclosure of confidential or privileged information will be addressed through the procedures and exceptions applicable under the Freedom of Information Act, 5 U.S.C. 552.

3. Longshore and Harbor Workers' Compensation Act Assessments

A comment, received from an insurer, dealt specifically with the insurer's situation regarding assessments under the Longshore and Harbor Workers' Compensation Act. This comment was not pertinent to the proposed rule and therefore has not been addressed. Insurers can request interpretations from Treasury pursuant to 31 CFR 50.9.

III. Procedural Requirements

Executive Order 12866, "Regulatory Planning and Review." This rule is a significant regulatory action for purposes of Executive Order 12866, "Regulatory Planning and Review," and has been reviewed by the Office of Management and Budget (OMB).

Regulatory Flexibility Act. Pursuant to the Regulatory Flexibility Act, 5 U.S.C. 601 *et seq.*, it is hereby certified that this rule will not have a significant economic impact on a substantial number of small entities. Treasury is required to pay the Federal share of compensation to insurers for insured losses in accordance with the Act. A condition of Federal payment is that the insurer must submit to Treasury, in accordance with procedures established by Treasury, a claim for payment and certain certifications. The rule seeks to emulate loss reporting practices in the reinsurance industry, which insurers already follow in order to get payment for reinsurance, thus minimizing the impact on all insurers. The Act itself requires all insurers receiving direct earned premium for any type of property and casualty insurance, as defined in the Act, to participate in the Program. This includes all insurers regardless of size or sophistication. The Act also defines property and casualty insurance to mean commercial lines insurance without any reference to the size or scope of the insurer or the

insured. Accordingly, any economic impact associated with the rule flows from the Act and not the rule. A regulatory flexibility analysis is thus not required.

Paperwork Reduction Act. The collection of information (recordkeeping requirement) contained in this rule has been approved by the OMB in accordance with the requirements of the Paperwork Reduction Act, 44 U.S.C. 3507(d) and assigned OMB Control Number 1505-0197. The forms to be prescribed by Treasury will be the subject of a separate submission to OMB on which the public will be provided an opportunity to comment. An agency may not conduct or sponsor, and a person is not required to respond to, a collection of information unless it displays a valid control number assigned by OMB.

The collection of information is the recordkeeping requirement in § 50.61. The information will be used by Treasury (or its designees) to audit or examine claims for Federal payments submitted by insurers. The recordkeeping requirement is mandatory for any insurer that seeks payment of a Federal share of compensation.

The estimated number of record keepers is 100 insurers sustaining insured losses. The estimated average annual burden per recordkeeper is 8.33 hours. The estimated total annual recordkeeping burden is 833 hours.

Comments regarding the accuracy of this burden estimate should be directed to the Terrorism Risk Insurance Program, Suite 2100, Department of the Treasury, 1425 New York Ave., NW., Washington, DC 20220 and to the Office of Management and Budget, Attn: Desk Officer for the Department of the Treasury, Office of Information and Regulatory Affairs, New Executive Office Building, Room 3208, Washington, DC 20503.

List of Subjects in 31 CFR Part 50

Terrorism risk insurance.

■ For the reasons stated above, 31 CFR part 50 is amended as follows:

PART 50—TERRORISM RISK INSURANCE PROGRAM

■ 1. The authority citation for part 50 continues 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).

■ 2. Revise § 50.5(e) to read as follows:

§ 50.5 Definitions.

* * * * *

(e) *Insured loss.* (1) The term insured loss means any loss resulting from an act of terrorism (including an act of war, in the case of workers' compensation) that is covered by primary or excess property and casualty insurance issued by an insurer if the loss:

(i) Occurs within the United States;

(ii) Occurs to an air carrier (as defined in 49 U.S.C. 40102), to a United States flag vessel (or a vessel based principally in the United States, on which United States income tax is paid and whose insurance coverage is subject to regulation in the United States), regardless of where the loss occurs; or

(iii) Occurs at the premises of any United States mission.

(2)(i) A loss that occurs to an air carrier (as defined in 49 U.S.C. 40102), to a United States flag vessel, or a vessel based principally in the United States, on which United States income tax is paid and whose insurance coverage is subject to regulation in the United States, is not an insured loss under section 102(5)(B) of the Act unless it is incurred by the air carrier or vessel outside the United States.

(ii) An insured loss to an air carrier or vessel outside the United States under section 102(5)(B) of the Act does not include losses covered by third party insurance contracts that are separate from the insurance coverage provided to the air carrier or vessel.

(3) The term insured loss includes reasonable loss adjustment expenses, incurred by an insurer in connection with insured losses, that are allocated and identified by claim file in insurer records, including expenses incurred in the investigation, adjustment and defense of claims, but excluding staff salaries, overhead, and other insurer expenses that would have been incurred notwithstanding the insured loss.

(4) The term insured loss does not include:

(i) Punitive or exemplary damages awarded or paid in connection with the Federal cause of action specified in section 107(a)(1) of the Act. The term "punitive or exemplary damages" means damages that are not compensatory but are an award of money made to a claimant solely to punish or deter; or

(ii) Extra contractual damages awarded against, or paid by, an insurer; or

(iii) Payments by an insurer in excess of policy limits.

* * * * *

■ 3. New Subparts F and G of Part 50 are added as follows:

Subpart F—Claims Procedures
Sec.

50.50 Federal share of compensation.

50.51 Adjustments to the Federal share of compensation.

50.52 Initial Notice of Insured Loss.

50.53 Loss certifications.

50.54 Payment of Federal share of compensation.

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. Subject to paragraph (b) of this section, Treasury shall pay the appropriate amount of the Federal share of compensation 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), 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 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;

(7) 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(l); and

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

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

(c) *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 (a) 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.

(d) *Amount payable.* The Federal share of compensation under the Program shall be 90 percent of that portion of the insurer's aggregate insured losses that exceed its insurer deductible during a Program Year, subject to any adjustments in § 50.51 and the cap of \$100 billion as provided in section 103(e)(2) of the Act.

§ 50.51 Adjustments to the Federal share of compensation.

(a) *Aggregate amount of insured losses.* The aggregate amount of insured losses of an insurer in a Program Year used to calculate the Federal share of compensation shall be reduced by any amounts recovered by the insurer as salvage or subrogation for its insured losses in the Program Year.

(b) *Amount of Federal share of compensation.* The Federal share of compensation shall be adjusted as follows:

(1) *No excess recoveries.* For any Program Year, the sum of the Federal share of compensation paid by Treasury to an insurer and the insurer's recoveries for insured losses from other sources shall not be greater than the insurer's aggregate amount of insured losses for acts of terrorism in that Program Year. Amounts recovered for insured losses in excess of an insurer's aggregate amount of insured losses in a Program Year shall be repaid to Treasury within 45 days after the end of the month in which total recoveries of the insurer, from all sources, become excess. For purposes of this paragraph, amounts recovered from a reinsurer pursuant to an agreement whereby the reinsurer's right to any excess recovery has priority over the rights of Treasury shall not be considered a recovery subject to repayment to Treasury.

(2) *Reduction of amount payable.* The Federal share of compensation for insured losses under the Program shall be reduced by the amount of other compensation provided by other Federal programs to an insured or a third party to the extent such other compensation duplicates the insurance indemnification for those insured losses.

(i) *Other Federal program compensation.* For purposes of this section, compensation provided by other Federal programs for insured losses means compensation that is

provided by Federal programs established for the purpose of compensating persons for losses in the event of emergencies, disasters, acts of terrorism, or similar events.

Compensation provided by Federal programs for insured losses excludes benefit or entitlement payments, such as those made under the Social Security Act, under laws administered by the Secretary of Veteran Affairs, railroad retirement benefit payments, and other similar types of benefit payments.

(ii) *Insurer due diligence.* Each insurer shall inquire of each of its policyholders, insureds, and claimants whether the person receiving insurance proceeds for an insured loss has received, expects to receive, or is entitled to receive compensation from another Federal program for the insured loss, and if so, the source and the amount of the compensation received or expected. The response, source, and such amounts shall be reported with each underlying claim on the bordereau specified in § 50.53(b)(1).

§ 50.52 Initial Notice of Insured Loss.

Each insurer shall submit to Treasury an Initial Notice of Insured Loss, on a form prescribed by Treasury, whenever the insurer's aggregate insured losses (including reserves for "incurred but not reported" losses) within a Program Year exceed an amount equal to 50 percent of the insurer's deductible as specified in § 50.5(g). Insurers are advised the form for the Initial Notice of Insured Loss will include an initial estimate of aggregate losses for the Program Year, the amount of the insurer deductible and an estimate of the Federal share of compensation for the insurer's aggregate insured losses. In the case of an affiliated group of insurers, the form for the Initial Notice of Insured Loss will include the name and address of a single designated insurer within the affiliated group that will serve as the single point of contact for the purpose of providing loss and compliance certifications as required in § 50.53 and for receiving, disbursing, and distributing payments of the Federal share of compensation in accordance with § 50.54. An insurer, at its option, may elect to include with its Initial Notice of Insured Loss the certification of direct earned premium required by § 50.53(b)(3).

§ 50.53 Loss certifications.

(a) *General.* When an insurer has paid aggregate insured losses that exceed its insurer deductible, the insurer may make claim upon Treasury for the payment of the Federal share of compensation for its insured losses. The

insurer shall file an Initial Certification of Loss, on a form prescribed by Treasury, and thereafter such Supplementary Certifications of Loss, on a form prescribed by Treasury, as may be necessary to receive payment for the Federal share of compensation for its insured losses.

(b) *Initial Certification of Loss.* An insurer shall use its best efforts to file with the Program the Initial Certification of Loss within 45 days following the last calendar day of the month when an insurer has paid aggregate insured losses that exceed its insurer deductible. The Initial Certification of Loss will include the following:

(1) A bordereau, on a form prescribed by Treasury, that includes basic information about each underlying insured loss. For purposes of this section, a "bordereau" is a report of basic information about an insurer's underlying claims that, in the aggregate, constitute the insured losses of the insurer. The bordereau will include, but may not be limited to:

(i) A listing of each underlying insured loss by catastrophe code and line of business;

(ii) The total amount of reinsurance recovered from other sources;

(iii) A calculation of the aggregate insured losses sustained by the insurer above its insurer deductible for the Program Year; and

(iv) The amount the insurer claims as the Federal share of compensation for its aggregate insured losses.

(2) A certification that the insurer is in compliance with the provisions of section 103(b) of the Act and this part, including certifications that:

(i) The underlying insured losses listed on the bordereau filed pursuant to § 50.53(b)(1) either: Have been paid by the insurer; or will be paid by the insurer upon receipt of an advance payment of the Federal share of compensation as soon as possible, consistent with the insurer's normal business practices, but not longer than five business days after receipt of the Federal share of compensation;

(ii) The underlying claims for insured losses were filed by persons who suffered an insured loss, or by persons acting on behalf of such persons;

(iii) The underlying claims for insured losses were processed in accordance with appropriate business practices and the procedures specified in this subpart;

(iv) The insurer has complied with the disclosure requirements of §§ 50.10 through 50.19 for each underlying insured loss that is included in the amount of the insurer's aggregate insured losses; and

(v) The insurer has complied with the mandatory availability requirements of §§ 50.20 through 50.24.

(3) A certification of the amount of the insurer's "direct earned premium" as defined in § 50.5(d), together with the calculation of its "insurer deductible" as defined in § 50.5(g) (provided this certification was not submitted previously with the Initial Notice of Insured Loss specified in § 50.52).

(4) A certification that the insurer will disburse payment of the Federal share of compensation in accordance with this subpart.

(c) *Supplementary Certification of Loss.* If the total amount of the Federal share of compensation due an insurer for insured losses under the Act has not been determined at the time an Initial Certification of Loss has been filed, the insurer shall file monthly, or on a schedule otherwise determined by Treasury, Supplementary Certifications of Loss updating the amount of the Federal share of compensation owed for the insurer's insured losses. Supplementary Certifications of Loss will include the following:

(1) A bordereau described in § 50.53(b)(1); and

(2) A certification as described in § 50.53(b)(2).

(d) *Supplementary information.* In addition to the information required in paragraphs (b) and (c) of this section, Treasury may require such additional supporting documentation as required to ascertain the Federal share of compensation for the insured losses of any insurer.

(e) *State Residual Market Insurance Entities and State Workers' Compensation Funds.* A State residual market insurance entity or State workers' compensation fund described in § 50.35 shall provide the Certifications of Loss described in §§ 50.53(b) and 50.53(c) for all its insured losses to each participating insurer at the time it provides the allocated dollar value of the participating insurer's proportionate share of insured losses. In addition, at such time the State residual market insurance entity or State workers' compensation fund shall provide the certification described in § 50.53(b)(2) to Treasury. Participating insurers shall treat the allocated dollar value of their proportionate share of insured losses from a State residual market insurance entity or State workers' compensation fund as an insured loss for the purpose of their own reporting to Treasury in seeking the Federal share of compensation.

§ 50.54 Payment of Federal share of compensation.

(a) *Timing.* Treasury will promptly pay to an insurer the Federal share of compensation due the insurer for its insured losses. Payment shall be made in such installments and on such conditions as determined by the Treasury to be appropriate. Any overpayments by Treasury of the Federal share of compensation will be offset from future payments to the insurer or returned to Treasury within 45 days.

(b) *Payment process.* Payment of the Federal share of compensation for insured losses will be made to the insurer designated on the Initial Notice of Loss required by § 50.52. An insurer that requests payment of the Federal share of compensation for insured losses must receive payment through electronic funds transfer. The insurer must establish either an account for reimbursement as described in paragraph (c) of this section (if the insurer only seeks reimbursement) or a segregated account as described in paragraph (d) of this section (if the insurer seeks advance payments or a combination of advance payments and reimbursement). Applicable procedures will be posted at www.treasury.gov/trip or otherwise will be made publicly available.

(c) *Account for reimbursement.* An insurer shall designate an account for the receipt of reimbursement of the Federal share of compensation at an institution eligible to receive payments through the Automated Clearing House (ACH) network.

(d) *Segregated account for advance payments.* An insurer that seeks advance payments of the Federal share of compensation as certified according to § 50.53(b)(2)(i)(B) shall establish an interest-bearing segregated account into which Treasury will make advance payments as well as reimbursements to the insurer.

(1) *Definition of segregated account.* For purposes of this section, a

segregated account is an interest-bearing separate account established by an insurer at a financial institution eligible to receive payments through the ACH network. Such an account is limited to the purposes of:

(i) Receiving payments of the Federal share of compensation;

(ii) Disbursing payments to insureds and claimants; and

(iii) Transferring payments to the insurer or affiliated insurers for insured losses reported on the bordereau as already paid.

(2) *Remittance of interest.* All interest earned on advance payments in the segregated account must be remitted at least quarterly to Treasury's Office of Financial Management or as otherwise prescribed in applicable procedures.

(e) *Denial or withholding of advance payment.* Treasury may deny or withhold advance payments of the Federal share of compensation to an insurer if Treasury determines that the insurer has not properly disbursed previous advances of the Federal share of compensation or otherwise has not complied with the requirements for advance payment as provided in this subpart.

(f) *Affiliated group.* In the case of an affiliated group of insurers, Treasury will make payment of the Federal share of compensation for the insured losses of the affiliated group to the insurer designated in the Initial Notice of Insured Loss to receive payment on behalf of the affiliated group. The designated insurer receiving payment from Treasury must distribute payment to affiliated insurers in a manner that ensures that each insurer in the affiliated group is compensated for its share of insured losses, taking into account a reasonable and fair allocation of the group deductible among affiliated insurers. Upon payment of the Federal share of compensation to the designated insurer, Treasury's payment obligation to the insurers in the affiliated group with respect to any insured losses

covered on the applicable bordereau is discharged to the extent of the payment.

Subpart G—Audit and Investigative Procedures**§ 50.60 Audit authority.**

The Secretary of the Treasury, or an authorized representative, shall have, upon reasonable notice, access to all books, documents, papers and records of an insurer that are pertinent to amounts paid to the insurer as the Federal share of compensation for insured losses for the purpose of investigation, confirmation, audit and examination.

§ 50.61 Recordkeeping.

Each insurer that seeks payment of a Federal share of compensation under subpart F of this part shall retain such records as are necessary to fully disclose all material matters pertinent to insured losses and the Federal share of compensation sought under the Program, including, but not limited to, records regarding premiums and insured losses for all commercial property and casualty insurance issued by the insurer and information relating to any adjustment in the amount of the Federal share of compensation payable. Insurers shall maintain detailed records for not less than 5 years from the termination dates of all reinsurance agreements involving commercial property and casualty insurance subject to the Act. Records relating to premiums shall be retained and available for review for not less than 3 years following the conclusion of the policy year. Records relating to underlying claims shall be retained for not less than 5 years following the final adjustment of the claim.

Dated: June 21, 2004.

Wayne A. Abernathy,

Assistant Secretary of the Treasury.

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