

A GLOBAL DEFINITION OF TERRORISM

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Abstract

Prior to the terrorist attacks of September 11, 2001 in the United States, only a handful of countries maintained a state-supported backstop for losses caused by acts of terrorism. The primary motivation for such state-sponsored coverage is economic: to minimize the harm caused to commercial activities because of the insufficiency of insurance capacity against terrorist acts. The idea is to instill confidence in the financial system as well as in the real economy that significant losses will be covered and, thereby, to encourage continued commerce. We argue that providing such coverage is more likely to lead to greater efficiency if countries follow a consistent approach to defining “acts of terrorism.” At a minimum, inconsistency leads to uncertainty within businesses operating internationally, and possibly to conflict.

Introduction

State-sponsored pools,² or so-called backstops against losses associated with terrorist acts, have evolved in a few countries from a perception of necessity. The IRA bombings in London led to a new mutual reinsurance company, Pool Reinsurance Company Limited (“Pool Re”) in 1993. Riots in South Africa resulted in the South Africa Special Risks Insurance Association (“SASRIA”), which is growing into maturity. In France, the creation of Caisse Centrale de Reassurance (“CCR”) was motivated by natural disasters, but has recently been amended and expanded because of terrorist activity.

Such insurance backstops evolved as a response to a lack of adequate commercial insurance against acts of terrorism. Commercial insurers, perceiving excessive exposure, offered either limited or no coverage. Government intervention in response to such a market failure can be justified because of the negative spillover effects on a country’s commercial activity. When private insurance coverage for the terrorism exposure is withdrawn, society suffers. For example, loans to finance large construction projects with terrorism exposures may be scarce or nonexistent. Commercial airlines with inadequate terrorism insurance limits may be grounded. Numerous other examples can be cited.

Moreover, were commercial insurers voluntarily to offer adequate coverage, they then would face risk of insolvency if losses exceeded their capital and reinsurance resources. In a competitive economy, the insolvency risk in itself is insufficient justification for government intervention into an industry. Indeed, many commercial enterprises fail each year with no one seriously suggesting a role for government in limiting such failures or their effects.

Society, however, faces a systemic risk associated with the simultaneous financial failure of numerous insurers. This systemic risk also creates the possibility of negative effects upon commercial activity and provides further economic justification for government intervention in an effort to rectify this potential market failure. Lawmakers are then motivated to create solutions where such risk is undertaken by society. Such a debate is occurring now in the United States³ and Germany.⁴

This article reviews the current status of state-sponsored pools and other backstops, discusses elements comprising definitions of terrorism for coverage purposes, and compares the various definitions in use today to propose a global definition of terrorism.

Current Status of State-Sponsored Coverage

In 1993, in response to a series of terrorist incidents in Great Britain, the British government led the insurance industry in establishing Pool Reinsurance Company Limited, commonly known as Pool Re. It has been successful in providing reinsurance coverage to the commercial property insurance market in Great Britain for terrorist exposure above a deductible amount. Pool Re does not require that direct insurers offer terrorism coverage; but if they do so, Pool Re provides reinsurance for acts of terrorism.⁵

France has agreed to pay terrorism losses above 1.5 billion euros a year through its state owned reinsurer Caisse Centrale de Reassurance. International reinsurers are forming a pool to pay terrorist claims up to the CCR attachment point.

Spain has had a state-sponsored pool in place since 1941. The Consorcio de Compensacion de Seguros (“CCS – Spanish Insurance Compensation Fund”) covers losses from extraordinary events, including terrorist losses. The South Africa Special Risks Insurance Association established a similar pool. Israel indemnifies losses of life and property from violent acts without a distinction as to whether the loss results from an act of terrorism or an act of war.

Germany is in the process of forming a state-sponsored pool, which will insure up to 13 billion euros, with insurers doing business in Germany responsible for the first 3 billion euros of coverage. Australia just announced that it, too, will provide a short-term limited indemnity for large losses caused by terrorism.

Since 1977, Northern Ireland has had a pool for Criminal Damage (Compensation). The definition of loss is narrow.

Countries currently administering pools for catastrophic events such as earthquakes, blizzards and tidal waves are considering expanding these pools to cover terrorism. Examples are Japan, New Zealand, Norway and Switzerland.

In other countries, insurers are banding together to form voluntary pools to provide terrorism coverage. Examples of these efforts can be found in Russia and Luxembourg. In some countries, i.e. Malaysia, the government is appealing to the banking community to establish a pool.

The United States Congress has considered four proposals to establish a state-sponsored backstop for terrorism coverage,⁶ and is currently debating a fifth proposal.⁷ None has been adopted. These proposals, however, provide informative insight into legislative thinking as to the definition of terrorism for state coverage and the terms.

In summary, there is much activity in state-supported pools. Never before has the need for a coordinated coverage definition been as great.

Definitions of Terrorism

Implicit in the creation of these pools is the question of what should be covered. What is the definition of an act of terrorism? Some pools require that insurers provide underlying coverage using a coverage definition at least as broad as the state-sponsored backstop.⁸ Others make such underlying coverage optional.⁹ Interestingly, of the five legislative proposals in the U.S., three would make coverage by traditional insurers mandatory and two would make coverage optional.¹⁰

No common definition of terrorism exists. In the U.S., the Insurance Services Office, Inc. (“ISO”), an insurance trade organization routinely providing standard policy language for use in the 50 states, published a definition of terrorism as an exclusion from coverage which was rejected by several leading states.¹¹

On May 20, 2002, the Association of Southeast Asian Nations (“ASEAN”) meeting in Kuala Lumpur discussed the need for a definition of terrorism. No conclusion was reached. The definition sought was not for the purpose of underwriting of risks, however.

Some have suggested that the United Nations address the issue.¹² Others have suggested the Organization for Economic Cooperation and Development (“OECD”) address the issue.¹³ We examine several definitions of terrorism for the purpose of comparisons and identifying patterns.

The Reinsurance (“Acts of Terrorism”) Act 1993 in the UK defined Acts of Terrorism as “acts of persons acting on behalf of, or in connection with, any organisation which carries out activities directed towards the overthrowing or influencing, by force or violence, of Her Majesty’s government in the United Kingdom or any other government de jure or de facto.”

Pool Re relied on this definition and produced a model definition as follows: “...an act of any person acting on

behalf of or in connection with any organisation with activities directed towards the overthrowing or influencing of any government de jure or de facto by force or violence.”¹⁴ This is in line with the standard pre-September 11th definition used by the International Underwriting Association (“IUA”) and the Lloyd’s Underwriters Non-Marine Association (“NMA”) in London.¹⁵

After September 11th, the definition used by the IUA was expanded to read as follows: “An act or acts (whether threatened or actual) of any person or persons involving the causing or occasioning or threatening of harm of whatever nature and by whatever means made or claimed to be made in whole or in part for political, religious, ideological or similar purposes.”¹⁶

After September 11th, the NMA also circulated four terrorism exclusion endorsements which defined terrorism as “...an act, including but not limited to the use of force or violence and/or the threat thereof, of any person or group(s) of persons, whether acting alone or on behalf of or in connection with any organisation(s) or government(s), committed for political, religious, ideological or similar purposes including the intention to influence any government and/or to put the public, or any section of the public, in fear.”¹⁷

South Africa, Spain and Israel do not have coverage limitations as to terrorism. Rather, they have broad coverage for losses from extraordinary events, including terrorism.

Hong Kong is currently debating its response to U.N. Resolution 1373. Terms of the proposed ordinance follow a definition of terrorism requiring that there be “the use or threat of action to influence a government or intimidate the public, and that the use or threat is made for the purpose of advancing a political, religious or ideological cause. In addition, the action must involve serious violence against a person or serious damage to property or create a serious risk to the health or safety of the public or seriously interfere with or disrupt an electronic system.”¹⁸

In Northern Ireland, a claimant must show that the damage incurred was unlawfully, maliciously or wantonly caused to property either by a riotous assembly or as a result of an act committed maliciously by a person acting on behalf of or in connection with an unlawful association.¹⁹

As of mid-July 2002, no U.S. federal legislation on terrorism insurance had been enacted. A Conference Committee of the Senate and House of Representatives has been named to consider a compromise. Deliberations are expected to continue in early September 2002.

Elements of a Definition of Terrorism

What follows is a discussion of the possible elements for definitions of acts of terrorism, drawing on those definitions discussed above.

Perpetrators. Definitions of terrorism uniformly categorize the perpetrators of such acts. Some definitions define perpetrators as a person or organization acting on behalf of a terrorist group or on behalf of foreign interests. Although some definitions do not require persons committing acts of terrorism be connected to an organization, most do require a connection. Most do not define such persons as operatives of a foreign government, which would bring the definition closer to that of war.

State-Sponsored. State sponsorship generally is not a prerequisite. None of the U.S. proposals defines terrorism as being state sponsored; neither do the IUA and NMA definitions nor the Pool Re definition.

Motive. Definitions of terrorism routinely require motives for the actions. The U.S. proposals vary. Two proposals include destabilization of the government as one motivation. Three of the proposals add a motive to coerce the civilian population. The Lloyd’s definition calls for overthrowing or influencing of any government. The current Hong Kong proposed ordinance broadens the motive to intimidate the public and to require that the use of threat is made for the purpose of advancing a political, religious or ideological cause. A post-September 11 NMA definition adds as a motive to put the public, or any section of the public, in fear.²⁰

Method. Definitions also include reference to the method of harm. The major distinction in this element is whether the method must be violent. The Pool Re definition requires an act by force or violence. There is some discussion

of expanding this definition.

The U.S. versions call for an act to be unlawful which causes harm or is a violent act. The Hong Kong proposal encompasses a broad definition of method which involves serious violence against a person or serious damage to property or creation of a serious risk to the health or safety of the public or serious interference with or disruption of an electronic system or essential service, facility or system. Post-September 11 IUA and NMA definitions call for an act or a threat of an act.²¹

Loss Threshold Most definitions do not set amounts of loss in absolute terms, rather calling for serious loss of life and property. Two U.S. proposals are exceptions as they require property losses in excess of US\$5 million before an act can be certified as an act of terrorism. The ISO definition, which has been used in the U.S. to define the exclusion from coverage, sets human loss at 50 or more persons killed or seriously injured and property loss at greater than US\$25 million, with either threshold qualifying as an act of terrorism.

The loss threshold for a definition of terrorism should not be confused with the point at which state-sponsored coverage begins. For example the attachment points for France and Germany are 1.5 billion and 3.0 billion euros, respectively.

Certified and By Whom. To be considered an act of terrorism, some definitions require government certification. Both France and the U.K. require certification of an event as an act of terrorism by government ministers. All U. S. proposals require certification, either by the Secretary of the Treasury or the Secretary of Commerce. Most certifications are non-appealable. In Northern Ireland, the claim must be certified by the Chief Constable of the Royal Ulster Constabulary.

A Global Definition of Acts of Terrorism

Drawing from the above discussion, we offer the following as a global definition of terrorism:

An act, including, but not limited to, the use of force or violence, committed by any person or persons acting on behalf of or in connection with any organization creating serious violence against a person or serious damage to property or a serious risk to the health or safety of the public undertaken to influence a government for the purpose of advancing a political, religious or ideological cause. Such act shall be certified as an "Act of Terrorism" by the senior judicial or administrative official designated by the adopting government and shall not be subject to appeal.

In some ways, more notable than the proposed definition itself is that which is omitted from it. There must be an act, not merely a threat of an act. While some definitions embrace threats, and certainly threats can cause real loss, in our opinion actual losses paid by society should require terrorist acts. Moreover, while a single person can carry out a harmful act, we would require that the person be connected with an organization for the act to be considered an act of terrorism.

We have rejected the notion of quantifying serious loss of life or property, opting instead to allow each jurisdiction to make that determination on an incident-by-incident basis. We have not specifically set out as a loss the interruption or interference with an electronic system or essential service, believing it to be covered generally in our definition.

Finally, we believe that each jurisdiction should provide an arbiter to determine whether an incident is an act of terrorism. To provide finality, this decision should not be subject to appeal.

As more countries adopt state-sponsored pools, the patchwork of definitions could multiply. If this occurs, the potential for confusion and conflict similarly multiply, with commercial enterprises operating cross-border finding risk management increasingly complex. One can envision coverage gaps between primary insurance and state pools because of disparate definitions of acts of terrorism.

A global definition is not immune from political influence in certifying an act of terrorism. A global definition, however, is more likely to result in consistent application and more predictable certifications of acts of terrorism. At

the same time, we acknowledge that any negative consequences from a failure to agree on a global definition could be mitigated somewhat to the extent that national drafters explicitly and clearly address elements in their definition which are included and those which are excluded, thus rendering greater clarity and providing less opportunity for misinterpretation.

Endnotes

1. This paper was co-authored by Mr. Player, Chairman of the Insurance and Reinsurance Group of Morris, Manning & Martin, L.L.P, Harold D. Skipper, Chairman, Professor, and C.V. Starr Chair of International Insurance, Georgia State University, and Janet Lambert, Partner, Reinsurance & International Risk Team, Barlow Lyde & Gilbert, London. It was presented by Mr. Player at the Annual Conference of the Asia-Pacific Risk and Insurance Association in Shanghai, China on July 22, 2002.
2. The term “pool” is used to describe a pool of funds and does not connote traditional pooling of risk by insurers.
3. The U.S. Congress is considering several pieces of legislation that call for a temporary federal backstop to maintain a market for terrorism risk insurance and is currently debating S. 2600 in the Senate. In November 2001, the House of Representatives passed H.R. 3210, the Terrorism Risk Protection Act, which includes a federal risk-sharing program. Although H.R. 3210 has not passed the Senate, four similar bills have been introduced in the Senate. These bills include S. 1743, S. 1744, S. 1748 and S. 1751 (S. 1748 and S. 1751 are identical bills.) S. 1743 would create a three-year reinsurance fund administered by the Secretary of Commerce. As part of this fund, participating commercial insurers would pay assessments and receive federal reinsurance protection against losses related to acts of terrorism. S. 1744 provides for a two-year industry risk-sharing commercial insurance program under the Secretary of Commerce. S. 1748/1751 would create a temporary public/private federal reinsurance program under the Secretary of Treasury. There is currently no consensus on any of these proposals.
4. Germany is currently in the process of creating a large state pool to support terrorism coverage.
5. Acts of Terrorism are defined in the Reinsurance (Acts of Terrorism) Act of 1993.
6. *See supra* note 3.
7. Terrorism Risk Insurance Act of 2002, S. 2600, 107th Cong. (2002).
8. Coverage of these risks has been compulsory in France since 1986. *See* Articles R-126-1, R-126-2 and L-126-2 of the French Insurance Code.
9. *For example*, Pool Re.
10. S. 2600, the Terrorism Risk Insurance Act of 2002, S. 1751, the Terrorism Risk Insurance Act of 2001, and S. 1743, the National Terrorism Reinsurance Fund Act, mandate that participating insurers offer terrorism coverage. However, H.R. 3210, the Terrorism Risk Protection Act, and S. 1744, the Terrorism Insurance Act, make such coverage optional.
11. The states of California, Florida, Georgia, New York and Texas rejected the ISO terrorism exclusion and insisted on a modification of the definition or that some form of terrorism coverage be mandated.
12. The Security Council of the United Nations passed Resolution 1373 on 28 September 2001 relating to measures for the prevention of terrorist acts. The last published United Nations treatise on the subject was in a September 1995 paper presented to the U.N. Conference on Trade and Development entitled, “Comparative Examples of Existing Catastrophe Insurance Schemes,” GE.95-53326.
13. At its Ministerial Meeting in Paris during mid-May 2002, the OECD formally stated, “We recognize the adverse effects of the shrinkage of affordable insurance cover for terrorism risks. We would welcome

OECD policy analysis and recommendations on how to define and cover terrorism risks and to assess the respective roles of the insurance industry, financial markets and governments, including for the coverage of 'mega-terrorism' risks."

14. Just after this paper was delivered, Pool Re's commercial terrorism coverage was modified to a wider "all-risks" basis, broadening the current coverage — which requires an act of force or violence—to terrorism damage caused by biological contamination, flood, and beginning Jan. 1, 2003, nuclear contamination.
15. IRMA/IUA – G55 and NMA2751.
16. IUA – G51A and G57.
17. NMA (2918-2921).
18. United Nations (Anti-Terrorism Measures) Ordinance.
19. Alan J. Fleming, "An Explosive Topic: Terrorism Cover in the United Kingdom," Risk Management, 41:14 et seq., August 1991.
20. NMA (2918-2921).
21. IUA – G51A and G57; NMA (2918-2921).