

MARKET BULLETIN

From	Julian James
Date	3 January 2007
Reference	Y3940
Subject	GAREAT - FRENCH TERRORISM REINSURANCE POOL
Subject areas	To inform syndicates of the procedures for 2007, including the ability to opt-out of the pool.
Attachments	None
Action points	Managing Agents and Underwriters to note and action opt-out procedure if required.
Deadlines	15 January 2007 for the opt-out 31 January 2007 for the Unexpired Exposure Report

Opting out of the pool for 2007

GAREAT participation is compulsory for all members of the French Insurers' Association (FFSA) including Lloyd's. However, individual syndicates were given the option to opt out of the pool for 2006. This option will remain in 2007.

The opting out conditions set in 2006 remain valid for 2007, i.e.:

- a) Syndicates intending to write direct risks subject to the non-exclusion of terrorism legislation must be members of GAREAT to qualify for French Government backstop protection in excess of €2.2 billion industry losses. **Syndicates will therefore automatically be entered into the GAREAT pool unless they specifically opt out. Opt-outs from 2006 will not be carried over. The deadline for opting out is 15 January 2007; after that date, no changes will be allowed.**

(Syndicates wishing to opt out of GAREAT should obtain an opt-out letter template from Zoë Kilminster in Worldwide Markets, ext. 5772, or zoe.kilminster@lloyds.com),

b) Syndicates deciding to opt out of GAREAT must stop underwriting the business to which the legislation applies. These non-GAREAT member syndicates may nonetheless have unexpired exposures and managing agents must therefore submit full details of each syndicate's unexpired risks to include as a minimum:

Assured Name, Premium (EUR), Location (minimum resolution = Departement), Policy Limit (EUR), Policy Attachment Point (EUR), Syndicate Share of Limit (EUR), Incept/Expire date.

This Unexpired Exposure report should be submitted to Paul Nunn, Head, Exposure Management (ext 6402) at Lloyd's by 31 January 2007

Structure of the pool for 2007

In 2006, the GAREAT pool was structured in 5 tranches, with losses up to €400 million retained by the co-reinsurance pool. Above this, three layers of reinsurance were purchased in the commercial reinsurance market protecting against losses up to €2,000 million in the aggregate. Unlimited cover via the CCR (a French State-owned reinsurer) guaranteed by the French State was provided above this level.

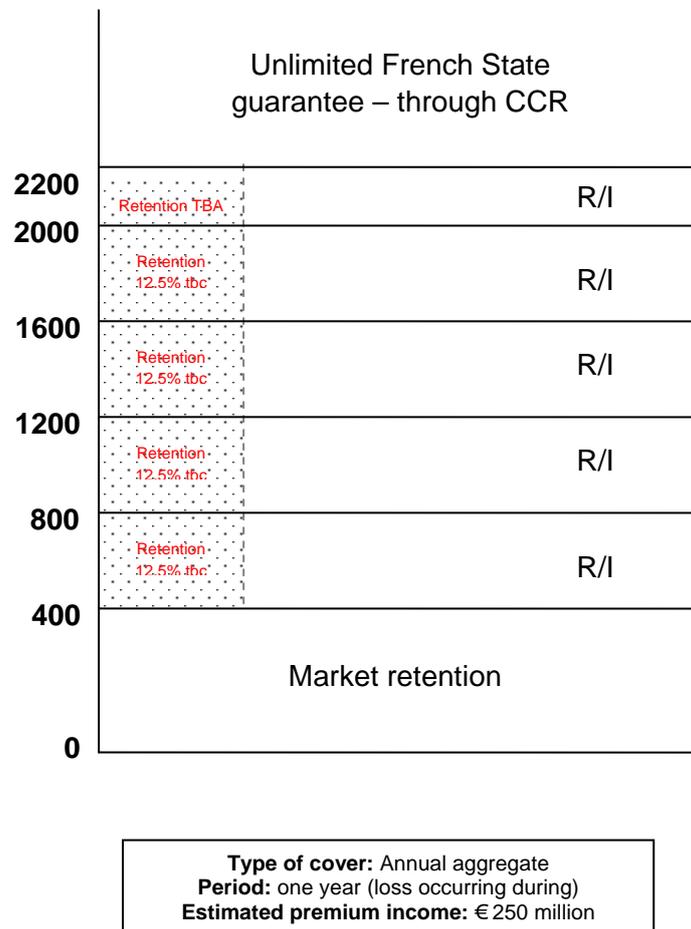
GAREAT has renewed the three-year State agreement for unlimited cover from 2007, with some changes:

For 2007, the second tranche of this structure will be split into two separate layers (from €400 million to €800 million and then from €800 million to €1,200 million) in order to facilitate the placement with reinsurers. **The unlimited cover via the CCR will be provided above €2,200 million instead of €2,000 million.**

The second layer will be led by Swiss Re, the third layer by Scor and the fourth layer by Berkshire Hathaway. The fifth layer will be co-led by Swiss Re and Berkshire Hathaway. Information on the leader of the sixth layer has yet to be released.

For 2007, private reinsurers willing to participate in the GAREAT layers have been asked to provide reinsurance cover for *any* acts of terrorism, as described by the French Code of Insurance and French Code of Defence. This means that all acts of terrorism are covered by GAREAT, including those committed through the use of **nuclear weapons**.

The illustration below describes the 2007 pool reinsurance structure for any acts of terrorism, **including nuclear attacks**.



For the reinsurance layers, the extent of a reinsurer’s participation in the programme will depend on its security rating (based on S&P ratings, with a minimum of BBB- required).

Updates and Reminders:

- **Nuclear risks and new terrorism Act:**

In 2007, GAREAT will cover all acts of terrorism, according to the provisions of new Article L 126-2, i.e. including those involving the use of nuclear weapons. No distinction will be made between nuclear and non-nuclear attacks with regard to GAREAT private reinsurers and French State coverage.

The first layer of €400 million is mutualised between members.

Over €2,200 million, the French State provides unlimited coverage.

Between €400 million and €2,200 million: terrorism is covered by GAREAT except for the **vertical retention. The percentage level of this retention on each of the upper layers will be advised ASAP. However, GAREAT has advised that the total amount vertically retained** by members should be between €200 and €230 million.

To date, GAREAT has not fully completed the reinsurance placement of the pool's upper layers. Should GAREAT not be able to place 100% of the €1,800 million xs €400 million in the private reinsurance market, it has been agreed that losses will be shared among GAREAT members according to the premiums they cede to the pool.

The final reinsurance placement will be advised ASAP.

- **Lloyd's exposure:**

Hypothesis:

- total loss over €2.2bn
- vertical retention: 12.5%
- gap in reinsurance placement: €200m of the sixth layer

1. Lloyd's global maximum exposure in GAREAT: hypothesis – Lloyd's cedes 4% of the total premium ceded by all members to GAREAT

Maximum exposure = (1) + (2) + (3)

- (1) First layer: €400m x 4% = €16m
- (2) Five upper layers: €1600m x 12.5% x 4% = €8m
- (3) Reinsurance gap (sixth layer): €200m x 4% = €8m
- Maximum exposure = (1) + (2) + (3) = 16 + 8 + 8 = €32m

2. Lloyd's exposure Syndicate per Syndicate: hypothesis – Syndicate XXX cedes 5% of the Lloyd's global premium ceded to GAREAT

For a loss over €2.2bn sustained by GAREAT members other than Lloyd's or by a single Lloyd's syndicate:

Rule: losses are mutualised between Lloyd's Syndicates according to the share of the Lloyd's global premium ceded to GAREAT

- Syndicate XXX maximum exposure = 5% x €32 = €1.6m

- **Equalisation reserves:**

The French State has authorised all GAREAT members (this will include all opted-in Lloyd's syndicates) to pay money into equalisation reserves in respect of Attacks and Acts of Terrorism coverage. Therefore if no significant claims occur, GAREAT will refund its members every year with the unused portion of their reinsurance premiums.

Given that UK accounting methods are different from their French equivalent, the money refunded by GAREAT to Lloyd's annually will be repaid into the Premiums Trust Funds where they should be kept as reserves in order to settle future losses relating to acts of terrorism in France. In addition, the portion of GAREAT premiums not called by the pool (about 30%), and therefore kept by Syndicates, should also be considered as reserves.

According to the latest GAREAT co-reinsurance convention, in return for this right to create equalisation reserves, the French State requests that all GAREAT members retain a vertical portion of the upper layers (from second to sixth). The level of this vertical retention will be advised ASAP but should be between €200m and €230m.

- **MAT risks:**

The decree excluding MAT risks from the scope of the new article L 126-2 was published on 30 September 2006, as a result of significant lobbying and negotiation with the French government.

The following will, however, remain subject to the provisions of article L.126-2:

- insurance contracts covering damage to the hulls of aircraft used for non commercial activities or for non-lucrative purposes, where the unit value of each hull declared in the contract is less than €1 million;
- insurance contracts covering damage to the hulls of marine, lake and inland waterway vessels used for pleasure sailing / yachting, where the unit value of each hull declared in the contract is less than €1 million.

In both of these cases, protection is afforded by the stop loss reinsurance purchased from CCR by Lloyd's, on behalf all syndicates.

For more detailed information on this topic, please refer to Market Bulletins Y3882 and Y3921.

GAREAT coverage of MAT risks:

- The storage portion of hybrid contracts “Stocks & Transit” can be ceded to GAREAT. However, the CCR will not offer the State cover over €2.2bn.
- Non-MAT contracts covering satellites can be ceded to GAREAT. Such contracts must be submitted to GAREAT on a case by case basis prior to cession to the pool.
- Contracts covering the construction of aviation hulls can be ceded to GAREAT, since they are not regarded as MAT risks in France.

- **Business Interruption standalone policies:**

The FFSA has provided the French market with additional information on standalone BI contracts. It appears that if the BI contract covers Fire, the terrorism cover becomes compulsory. Consequently:

- These contracts must include the clause LMA 5061
- These contracts must be ceded to GAREAT when the sum insured exceeds €6m.

- **“Shortage from suppliers” contracts:**

Further to discussions, it has been decided that such contracts can still be ceded to GAREAT.

- **Transition for 2007:**

The new Terrorism Act has affected the scope of GAREAT. Prior to the Act, **all** property contracts were to include terrorism cover. Following the Act, only contracts with a Fire guarantee must cover terrorism.

Therefore, in order to comply with the new legal requirements, **GAREAT will no longer accept risks where there is no Fire guarantee.**

Contracts already ceded by members before the publication of the new Article L 126-2 can continue to be ceded until the next renewal date of the risk.

GAREAT has also confirmed that the following contracts are to be ceded to GAREAT should they cover the consequences of fire damage:

- Construction All Risks
- Construction risks
- Standalone Business Interruption

• **GAREAT territorial limits:**

GAREAT's territorial reach will change in 2007 to comply with the new Act. **GAREAT will no longer accept risks located in territories where the new article L 126-2 does not apply.**

Contracts already ceded by members before the publication of the new Article L 126-2 can continue to be ceded until the next renewal date of the risk (such as Polynesian risks).

2007 GAREAT territorial scope	
French Guiana (La Guyane)	Yes
French Polynesia	No
French Southern and Antarctic Lands, including the Kerguelen Islands	No
Guadeloupe	Yes
Martinique	Yes
Mayotte	Yes
Metropolitan France	Yes
New Caledonia	No
Reunion Island	Yes
Saint Barthelemy	Yes
Saint Martin	Yes
Saint-Pierre & Miquelon	Yes
Wallis & Futuna	Yes
Andorra	No
Monaco	No

• **Claims declarations:**

GAREAT has designed a new claim declaration online system for its members. Any member with a claim to cede to GAREAT should contact the Lloyd's French office to obtain access to this system.

Members must declare losses no later than 6 months after the date of occurrence (date at which the act of terrorism was committed). However, when a member is advised of a claim during the sixth month, the member has one clear month to declare the loss to GAREAT.

All co-insurers on a contract must declare their portion of a loss.

• **French coverholders' GAREAT returns:**

Syndicates declare in their returns:

- Open-market risks
- Risks written by their Lloyd's Brokers holding lineslips on their behalf
- Risks written by their coverholders **other than French coverholders.**

French coverholders holding binders on behalf of Lloyd's Syndicates also submit separate GAREAT returns direct to the Lloyd's French office. These returns include all risks written through the binders they hold.

However, please note that:

- The onus is on the Syndicates to ensure that French coverholders make a return to the Lloyd's French office if they write risks falling under GAREAT
- The onus is on the Syndicates to ensure that French coverholders submit timely and accurate data to the Lloyd's French office.
- Syndicates are charged on the basis of these returns made by French coverholders

For these reasons, Syndicates should contact their French coverholders regularly to check they do make GAREAT returns to the Lloyd's French office. Syndicates should also set up procedures to control the data submitted by their coverholders, if such procedures are not already in place.

Further information

Further information regarding GAREAT can be obtained as follows:

In France, from Lloyd's Paris office:

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