STATE OF NEW YORK
INSURANCE DEPARTMENT
25 BEAVER STREET
NEW YORK, NEW YORK 10004

OGC Op. No. 03-01-37

The Office of General Counsel issued the following opinion on January 16, 2003, representing the position of the New York State Insurance Department.

Re: Political Risk Insurance

Questions Presented:

1. With regard to the regulation of excess line insurance, what is the situs of the risk for political risk insurance?

2. Under what circumstances could political risk insurance be placed with an unauthorized insurer?

Conclusions:

1. The situs of the risk depends upon the particular facts of the situation for which coverage is sought. The inquiry in this matter was made to ascertain the permissibility of procuring a political risk coverage policy directly from an unauthorized insurer without having to use the excess line market. In light of the nature of political risk insurance, however, this would not be permissible.

2. Where political risk insurance coverage is considered to constitute one or more of the types of coverage referenced in N.Y. Ins. Law § 2105(a), then the coverage could be placed by an excess line broker with an unauthorized insurer that is in compliance with the requirements contained in N.Y. Insurance Law § 2118 (McKinney Supp. 2003) and Regulation 41, N.Y. Comp. Codes R. & Regs. tit. 11 § 27 (2001).

Facts:

The issue of this inquiry concerns the availability of obtaining political risk insurance from unauthorized insurers in the excess line market. The inquiry described political risk insurance as insurance that is designed to protect an insured against losses caused by an act of a specifically defined foreign government or governments. In most cases, political risk insurance is purchased to cover risks where the level of political or economic volatility is beyond the client's comfort zone. As such, while it is common to see insureds purchase political risk insurance for countries like Brazil, Turkey, Indonesia and Argentina, political risk insurance is seldom used for stable foreign risks like the United Kingdom or Canada, and are not used to cover one's own domestic political risk. Political risk insurance is available for the full range of exposures related to cross-border corporate, commodity, trade, structured trade and project activities, and the financing thereof. The inquiry states that the risks include but are not limited to:

(a) Foreign government frustration of contracts (including export/import embargoes or license cancellation);

(b) Political force majeure, i.e., frustration of contracts due to war, terrorism, or political violence;

(c) Currency inconvertibility and inability to transfer currency;

(d) Expropriation, nationalization and confiscation of overseas assets or companies; and

(e) Lenders' interest (covering a financial institution) against non- repayment of a loan due to political risks as detailed above.

Analysis:

1. Situs of Risk

In regard to unauthorized insurers, the situs of risk is an issue when ascertaining whether the excess line market must be utilized or whether a licensed broker may procure the policy directly without using the excess line market. [1] Under N.Y. Ins. Law § 2117(b)(2), an insurance broker may place insurance with an unauthorized insurer without using the excess line market in certain circumstances, such as where the situs of the property insured is permanently outside of New York. That section provides as follows:

Notwithstanding the provisions of subsection (a) hereof, any insurance broker licensed under subparagraph (B) of paragraph one of subsection (b) of section two thousand one hundred four of this article may negotiate a contract of insurance, or place insurance, in an insurer not authorized to do business in this state, as follows:

. . . .

(2) insurance against loss of or damage to property having a permanent situs outside of this state . . . .

N.Y. Ins. Law § 2117(b)(2) (McKinney Supp. 2003).

This provision is regarded by the Department as applying only to tangible property that is permanently located outside of this State. For example, were a person simply seeking fire or theft coverage for property located outside of New York, the section would operate to allow a licensed broker to procure such coverage from an unauthorized insurer without using the excess line laws. Political risk insurance, as discussed below, is viewed as a type of insurance that is a combination of several kinds of coverage. Therefore, the "situs" exception of N.Y. Ins. Law § 2117(b)(2) is not applicable to political risk insurance.

2. Placement of Political Risk Insurance With an Unauthorized Insurer

The New York Insurance Law does not contain a definition of "political risk insurance." Such coverage, however, is recognized by the Department. For example, Regulation 86, N.Y. Comp. Codes. R. & Regs. tit. 11, § 16 (1998), which implements Article 63 of the Insurance Law (the rate and policy form filing exemption for special risk insurance), includes political risk insurance as a type of special risk insurance and describes it as follows:

Coverage for losses arising out of the actions of a foreign government. This includes:

(1) loss of use or destruction of property located in a foreign country;

(2) loss of income from operations or uncompleted contracts in a foreign country;

(3) nonpayment on a contract due to the inability to convert foreign currency into "contract" currency;

(4) termination of contracts due to license cancellations and embargoes;

(5)war civil war, revolution, rebellion, insurrection within a foreign country or along the route of shipment which prevents completion of contracts; or

(6) expropriation, confiscation, nationalization, seizure, requisition or arbitrary and selective intervention by a foreign government preventing completion of contracts or otherwise affecting business operations of the insured in such country.

N.Y. Comp. Codes Rules & Regs. tit. 11, § 16.12(e)(2002).

Under N.Y. Ins. Law § 2105(a), an excess line broker may place insurance risks with non-licensed insurers only for the kinds of insurance specified in N.Y. Ins. Law § 1113(a)(4)-(14), (16), (17), (19), (20), (22), (27) and (28) (McKinney Supp. 2003).2 Different aspects of political risk insurance are viewed by the Department as coming within a number of the aforementioned kinds of insurance. Therefore, political risk coverage conforming to the description contained in Regulation 86 may be placed with an unauthorized insurer in the excess line market.

When an excess line broker desires to place coverage with an unauthorized insurer, it must generally comply with the provisions of N.Y. Ins. Law § 2118 (McKinney Supp. 2003) and Regulation 41, N.Y. Comp. Codes R. & Regs. tit. 11 § 27 (2001). These provisions require, inter alia, that the broker first obtain declinations from authorized New York insurers prior to placing the coverage with an unauthorized insurer, and would be applicable in the instant case.

Finally, it is noted that Item 5 in the inquiry’ s description proposes to protect a lender from the nonpayment of a debt obligation. This item has no analogous provision in the description of political risk insurance contained in Regulation 86. Where the nonpayment was due to the financial default or insolvency of the obligor (whether or not proximately caused by occurrences constituting "political risks"), such coverage would constitute financial guaranty insurance as set forth in N.Y. Ins. Law § 6901(a)(1)(A) (McKinney 2000). This coverage comes within financial guaranty insurance (§ 1113(a)(25)), which is defined under N. Y. Ins. Law § 6901 (McKinney 2000), in pertinent part, as follows:

(a)(1) "Financial guaranty insurance" means a surety bond, insurance policy or, when issued by an insurer or any person doing an insurance business as defined in paragraph one of subsection (b) of section one thousand one hundred one of this chapter, an indemnity contract, and any guaranty similar to the foregoing types, under which loss is payable, upon proof of occurrence of financial loss, to an insured claimant, obligee or indemnitee as a result of any of the following events:

(A) failure of any obligor on or issuer of any debt instrument or other monetary obligation (including equity securities guarantied under a surety bond, insurance policy or indemnity contract) to pay when due to be paid by the obligor or scheduled at the time insured to be received by the holder of the obligation, principal, interest, premium, dividend or purchase price of or on, or other amounts due or payable with respect to, such instrument or obligation, when such failure is the result of a financial default or insolvency or, provided that such payment source is investment grade, any other failure to make payment, regardless of whether such obligation is incurred directly or as guarantor by or on behalf of another obligor that has also defaulted;

(B) changes in the levels of interest rates, whether short or long term or the differential in interest rates between various markets or products;

(C) changes in the rate of exchange of currency;

(D) changes in the value of specific assets or commodities, financial or commodity indices, or price levels in general; or

(E) other events which the superintendent determines are substantially similar to any of the foregoing.

The coverage sought in Item 5 of the inquiry’ s description constitutes financial guaranty insurance, which is enumerated at N.Y. Ins. Law § 1113(a)(25). Financial guaranty insurance is not among the kinds of insurance designated under N.Y. Ins. Law § 2105(a). Therefore, it may not be placed by an excess line broker.

For further information you may contact Supervising Attorney Michael Campanelli at the New York City Office.

---

1 The situs of the risk is also relevant for tax allocation purposes, but the inquiry does not pertain to tax issues.

2 The types of coverage listed in those sections are as follows:

(4) Fire insurance;
(5) Miscellaneous property insurance;
(6) Water damage insurance;
(7) Burglary and theft insurance;
(8) Glass insurance;
(9) Boiler and machinery insurance;
(10) Elevator insurance;
(11) Animal insurance;
(12) Collision insurance;
(13) Personal injury liability insurance;
(14) Property damage liability insurance;
(16) Fidelity and surety insurance;
(17) Credit insurance;
(19) Motor vehicle and aircraft physical damage insurance;
(20) Marine and inland marine insurance;
(22) Residual value insurance;
(27) Prize indemnification insurance; and
(28) Service contract reimbursement insurance.