Political Violence: When It Gets Serious

Charles Berry

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Today, many multinationals buy political violence insurance programmes from the political risk insurance market. They do so because they have come to realise the limitations of the political violence coverage offered by their property insurance. While general property insurers may, on the face of it, offer cover for such risks as riot, civil commotion or terrorism, in reality that cover is only provided so long as the situation does not get too serious.

In other words, general property insurers cover political violence on the basis that if the level of political violence gets bad, they hand the risk back to the policyholder.

Imagine a property policy that will cover windstorm, but only if the wind speed does not exceed 100 mph. It would not be tolerated. This approach is, nevertheless, routinely accepted when it comes to political violence.

The mechanism for handing back the risk to the policyholder is the standard war risks exclusion. While every risk manager knows he or she has a 'war' exclusion in their policies, few are encouraged to read beyond the word "war" which appears very early in the exclusion and conjures up a picture of conventional war between two sovereign states.

It is the words in the remainder of the exclusion that have most relevance in the modern world. They confirm that the exclusion comes into play much lower down the political violence spectrum than people realise. In fact, calling it a war exclusion is spin; in reality, it is a serious political violence exclusion.

Nor are we simply referring to what is going on in Afghanistan, Iraq or Sudan, events which are clearly deep into the language of the war exclusion. We are talking about the type of political violence that is seen routinely in Nigeria, Sri Lanka, Thailand and many other emerging markets. To verify this, you only have to check the legal history.

One famous example involving a loss in the Lebanon clearly illustrates the point. At the time of the loss, there was no civil war in the Lebanon; the judge said so. He also said that there was no case for arguing that there was even an uprising in the country at the time. So why did the policyholder's cover, which had been specifically extended to cover riot, strike and malicious damage, not respond when rioters ransacked their premises? The answer was that the level of rioting had reached a sufficiently serious level that the war exclusion applied and cover was, therefore, denied.

Many will have looked at the events in Kenya at the beginning of 2008 and seen riots and civil commotion, events usually covered (or not excluded) under a conventional property policy. But the question to be asked about Kenya and other similar events of civil unrest is whether the events amounted to an uprising. When a riot does become an uprising, it is no longer covered by a property policy because the war exclusion clause comes into play.

This should surprise no one. The war exclusion clause did not arrive in the property insurance market by accident. It became fixed in the firmament of property insurance as a result of the War Risks Agreement of 1936. While the immediate motivation for the agreement was the fear of aerial bombardment of the type that first appeared during the Spanish Civil War, the intent of those who framed the agreement was clear: they wanted to protect the property insurance market for land-based risks from the risk of serious political violence.

On the whole, the war risks exclusion has achieved that goal, but not always. The terrorist attacks of September 11 slipped through the industry's defences. However,

the rapidity with which the industry introduced the new terrorism exclusion clause illustrates that while the nature of political violence may have changed in the last 70 years, property insurers continue to want to keep serious political violence out of their general portfolios.

Emerging markets

We have come quite a long way in an article on political violence before getting on to the subject of terrorism. This is very important in the context of the stand-alone terrorism insurance market that developed in the aftermath of 9/11.

The growth of this market has been phenomenal and a testimony to the continuing entrepreneurial and risk-taking skills in the specialist insurance market. Having said that, we at BPL Global are not enthusiasts for the stand-alone terrorism market's basic product, the T3 terrorism wording, (now known as LMA3030).

As political risk insurance brokers, we concentrate on emerging markets where serious political violence mostly occurs, and a lot of political violence is not terrorism, particularly in these markets. Our dislike of the T3 product reflects this focus. In fairness, the policy was originally designed for the type of isolated covert attack more likely to occur in the developed world.

In the popular mind, all types of political violence these days tend to be lumped under the general heading of terrorism. However, it would be a big mistake for any risk manager to believe that stand-alone terrorism insurance will cover his or her company for other contemporary types of political violence, or, indeed, that it will cover all forms of terrorism in emerging markets.

Our long held assertion that terrorism insurance does not cover all forms of terrorism was for some time regarded as controversial. But today market insiders acknowledge that, in reality, the standard T3 terrorism does not cover all types of terrorism. As with other types of cover that carry the standard property insurance market war risks exclusion, cover under the T3 terrorism wording depends on the severity of the event.

Hezbollah in the Lebanon is an example of a serious terrorist organisation. We measure that by its ability to get hundreds of thousands of cheering supporters demonstrating in the streets of Beirut. Nevertheless, it is a terrorist organisation, and some policyholders expected that standard terrorism insurance would cover damage to property by Hezbollah rockets. Happily many of the underwriters in the London market shared this view, and paid a number of small claims.

However, these claims were settled on an *ex gratia* basis, because the lawyers agreed that these terrorist acts were not covered by the standard terrorism policy. It is worth remembering that when the claims get serious, it is the lawyers who count. This did not surprise us, as in our opinion nothing that Hezbollah does is covered by the T3 terrorism wording. But Hezbollah is not alone. There are many other terrorist organisations operating in emerging markets for which the same comment applies. And leading London insurers share this view. Hiscox, for example, has given a clear warning that if a company buys stand-alone terrorism insurance on the T3 wording for assets in emerging markets the buyer "could find itself uninsured".

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A clear picture is, therefore, emerging from the property insurance market: your property policy can cover you for political violence, like riots and civil commotion, provided it does not get too serious. If it becomes too serious, the risk then comes back to you. Likewise your property policy can cover you for terrorism unless, of course, the incident is too severe, at which point the policy excludes the risk.

How serious is serious you may ask? This is easy to answer in theory because the meaning of the words in the war exclusion is fairly clear; but applying these definitions to events as they unfold can be difficult. This is a good time to introduce the CNN conundrum. It says that if political violence has been in the news headlines three nights running in the same country, it is probably a fairly safe bet that events are serious enough for the war risk exclusion to come into play.

The problem is that if the country is in the headlines three nights running, that is the time that the risk management department tends to get the telephone call it dreads from senior management: are we covered?

This in turn leads to a simple rule of thumb for risk managers to use in contemplating the political violence provided by their general property insurance programme. It says that if you are not being asked by your colleagues about your political violence cover, there is probably nothing serious going on, so you are covered. On the other hand, if your colleagues are asking whether you are covered for political violence, the events prompting the question could well be severe enough for you not to be covered. In other words, the political violence cover you have in your general property programme can be as useful as the proverbial chocolate teapot, and especially for emerging markets.

So what do you do if you have assets around the world and you want to take political violence seriously? The answer is that you talk to your political risk insurance broker. The political risk insurance market does take political violence seriously. It does so by taking the words that you find in your war risks exclusion out of the exclusion, and putting them in the causes of loss of their policies. Only this market can do this.

This is why an increasing number of multinational companies are turning to the political risk insurance market for political violence cover. They have done their homework, and decided to take the risk of political violence seriously.

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