

# Counter Terrorism & Political Risk



**Propeller Club**

**2005**

**AON**

# General Overview

## What are Political Risks ?

Political Risks are the inherent, intangible risks that arise in dealings with foreign countries and are caused by the actions or inactions of

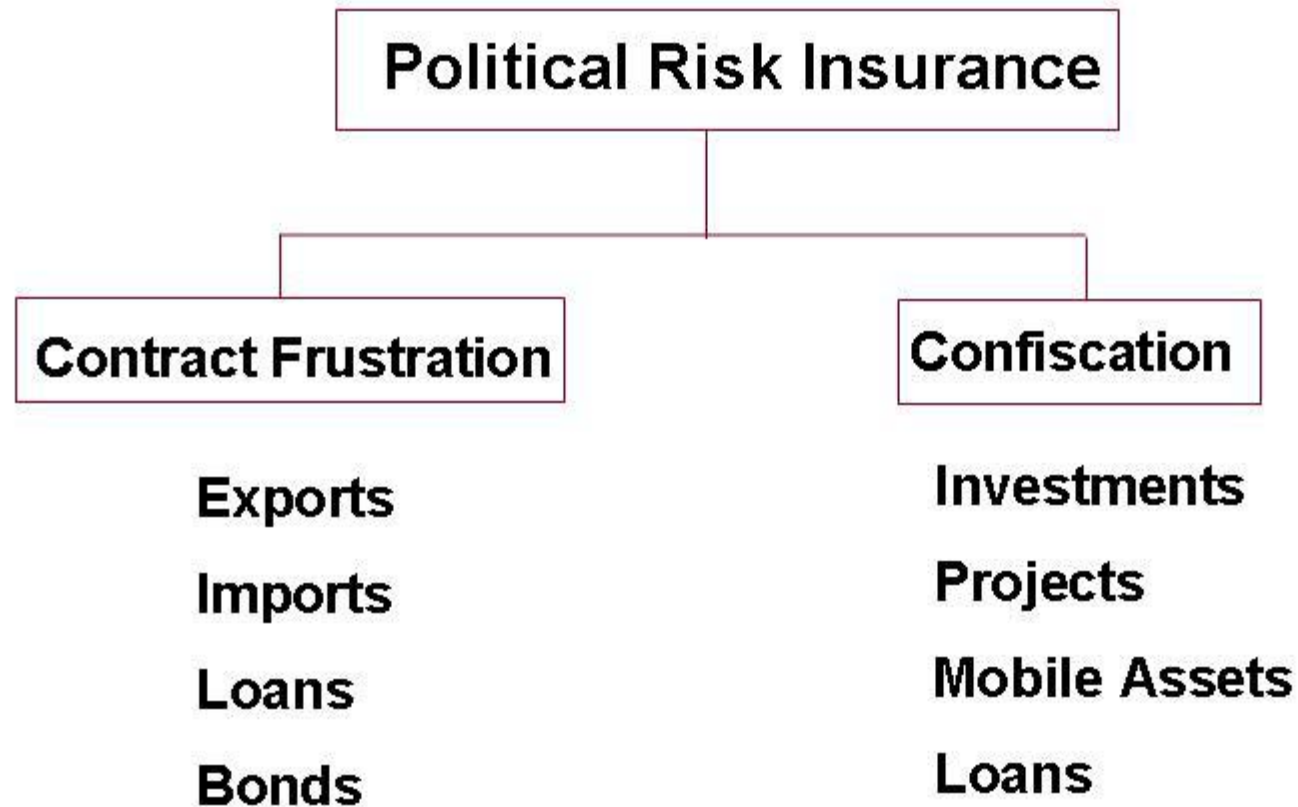
- ▶ a foreign government, or
- ▶ the insured's government, or
- ▶ a third party country government,
- ▶ war and unrest (political violence)

which

- ▶ prevent or restrict the performance of a contract, or
- ▶ deprive a corporation of all or part of its assets.

**Political Risk insurance does not make a bad contract better !!**

# General Overview



# Confiscation – Permanent Assets

*For Joint Ventures, Subsidiaries, permanent investment abroad*

## Cover:

- Confiscation, Expropriation & Nationalisation
- Forced Abandonment &/or Divestiture
- Cancellation of Concession/Licence
- Selective Discrimination
- Political Violence (war, terrorism, SRCC etc.)
- Currency Inconvertibility / Exchange Transfer



## Insureds:

### Investors

Value of equity and/or  
Inter-company loans, and/or  
Guaranteed bank loans

### Lenders

Value of the scheduled loan  
repayments

# Terrorism stand-alone cover

- **Covers:**

- ▶ Foreign terrorism
- ▶ Domestic terrorism
- ▶ Special Interest Groups
- ▶ Organised crime (subject to definition)



- **Excludes:**

- ▶ Crime
- ▶ Chemical / Biological / Nuclear
- ▶ War
- ▶ Strikes, Labour disputes, civil commotion

# Confiscation – Mobile Assets

## What do we mean by mobile assets?

- Can be owned assets such as
  - ▶ **stocks of parts, components, commodities**
  - ▶ **Ships**
  - ▶ **goods in transit**
  - ▶ **temporary imports**
- Or leased assets such as
  - ▶ **ships**
  - ▶ **plant & equipment**
  - ▶ **other mobile equipment**



# Confiscation – Mobile Assets

## Features of cover – Owned Assets

- market capacity available is usually quite large
- period of cover may range from days to 3 years
- 100% indemnity
- deductible for physical damage perils
- basis of valuation can be market value, replacement value, invoice value or repair value
- theft is not confiscation!
- non-delivery is a contractual risk



# Confiscation – Mobile Assets

## Case example

Insured:	Commodity trader
Country of risk:	Indonesia + Ivory Coast
Insured Goods:	Beans, grains, pulses etc... stored in port warehouse prior to export
Risks insured:	Confiscation, deprivation, political violence (Mobile assets + PV)
Sum Insured:	USD 30,000,000
Deductible:	PV only - USD 50,000 each and every loss
Period:	12 months
Rate:	Indonesia @ 1.2% p.a. Ivory Coast @ 1.5% p.a.



# Contract - Non payment

## How is Political Risk different from Credit Insurance ?

**Political risk arises from the action (or inaction) of a government exercising its authority.**

**Non-payment by a Public Buyer is a political risk.**

**Credit insurance protects a seller against not being paid by a Private Buyer**

# Contract - Non payment

## Lloyd's Public Buyer definition

- i. a central government or a ministry, department or agency thereof (hereinafter referred to as "Government"), or
- ii. a regional or local authority or a department or agency thereof (hereinafter referred to as "Local Authority"), or
- iii. a nationalised undertaking (including a public corporation) or a state trading organisation or an entity in which the Government or Local Authority retains a controlling interest and/or a majority shareholding.

## Contract - Non payment

**A Private Buyer is a buyer who does not meet the Public Buyer definition and is therefore is a commercial or private entity that can become insolvent and bankrupt.**

**Examples: Aon, Ford Motor Company, GE, Marconi, Enron, WorldCom**

# Contract - Non payment

## Insured Events

### Buyer Non-Payment

the failure and/or refusal by the Buyer to pay sums due and payable in accordance with the Insured Contract, including any sums which become payable in accordance with the Insured Contract following the termination of the Insured Contract



# Contract - Non payment

## Insured Events

### Non-honouring of Debt Instrument

the failure and/or refusal of the Issuing Bank and/or Guarantor to honour its obligations under the Debt Instrument of the Insured Contract

- ▶ **can be Letter of Credit, Bill of Exchange or Promissory Notes etc.**

# Contract - Non payment

## Example

Insured:	Oil Trader
Risk Country:	Nigeria
Contract:	Sale of oil to NNPC (Public Buyer)
Payment:	45 day open account
Limit:	USD 30m excess of USD 5m deductible
Cover:	Non-payment
Period:	12 months
Premium:	0.5% per month
Cover expected to revolve every 30 days	

# Import pre-financing

## Structure

- buyer is required to pay in advance of delivery of goods
- usually prompted by the supplier's poor cash flow or lack of credit
- may be in the form of a simple Advanced-payment (lower risk), or full pre-production finance (higher risk)
- balance of purchase price usually paid on quality / quantity check
- buyer often encouraged to prefinance to secure priority deliveries

# Import pre-financing

## Structure



**Metals Trader  
Switzerland**

USD 2m Pre-payment →

← USD 2m steel  
slabs (90 days  
later)



**Steel Producer  
Romania**

# Import pre-financing

## Cover : Non-delivery – Non repayment

### Insured Events:

#### **A. Country risks (Public and Private Suppliers)**

- ◆ Import / export embargo
- ◆ Cancellation / non-renewal of licences
- ◆ Termination through war / civil war / government interference
- ◆ Currency inconvertibility/non-transfer on repayments
- ◆ Confiscation

#### **B. Supplier risks (Public suppliers only)**

- ◆ Contract Termination
- ◆ Failure to repay advance payment / honour the guarantee
- ◆ Failure / refusal to comply with contractual obligations  
(Non Delivery)
- ◆ Failure / refusal to honour arbitration award



# Unfair Calling Cover (UCC)



## On-Demand and Unconditional Bonds and Guarantees

- Bid/Tender Bonds
- Advance Payment / Progress Payment Bonds
- Performance Bonds
- Retention/Maintenance/Warranty Bonds

# Political Risk Cover for Banks

## What role does the banks play?

- financing the transaction for the supplier – supplier credit
  - ▶ can be **loss payee** only
  
- financing the transaction for the buyer – buyer credit
  - ▶ Can be directly Insured
  
- accepting a financial risk in the transaction – trade and structured finance
  - ▶ Can be directly Insured

# Political Risk Cover for Banks

## Case example

Insured:	Syndicate of Banks
Country of Risk:	Dominican Republic
Contract:	USD 48,000,000 refurbishment and re-equipping of technical colleges
Cover:	CF for Non Honouring by Secretario Technico de la Presidencia - 100% commercial loan
Period:	24 months (15%) & 60 months (85%)
Sum Insured:	USD 47,000,000 (92.5% indemnity)
Rate:	3.1% p.a.
Waiting Period:	180 days

# Political Risk Cover for Banks

## Case example

Insured:	Bank
Country of Risk:	Romania
Purpose:	Project finance loan to gold mine
Cover:	Lenders Interest for Expropriation, Currency Inconvertibility & Political Violence
Period:	7 years
Sum Insured:	US \$ 240 million
Indemnity:	100%
Rate:	1.35% p.a. on exposure
Waiting Period:	180 days

# The international political risk market



AIG  
Chubb  
Zurich



Lloyd's  
AIG Europe  
Atradius  
Ace Europe



Unistrat



(Bermuda)

Sovereign  
EIC  
Axis  
Quanta

## ◆ Geographical distribution

◆ The main market : London

◆ American markets : USA and Bermuda

◆ Continental European market :  
France - new 2004 Garant – Austria  
/ Switzerland