



# Willis

*The Revolving Surety World*

**Smith Currie & Hancock LLP**

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**Presented By**

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- ✓ **Surety Market Changes**
- ✓ **Surety Underwriting Results**
- ✓ **Implications To Construction Firms**
  - ✓ **Contract Terms**
  - ✓ **Subcontractor Default Insurance**
- ✓ **What You Need to Ask About Your Surety Program**
- ✓ **Market Update**

# Surety Market Changes

<u>1999</u>	<u>June 2004</u>	<u>2003</u>
St.Paul	St.Paul / Travelers / Fireman's Fund	Travelers
Zurich	Zurich	St.Paul
CNA Surety	CNA Surety	CNA Surety
Reliance	Sold to Travelers in May, 2000	Zurich
AIG	AIG	Safeco
Travelers	Merged with St.Paul in April 2004	Chubb
Liberty Mutual	Liberty Mutual	Liberty Mutual
Frontier	Exited the business in 2001	The Hartford
Chubb	Chubb	AIG
Fireman's Fund	Sold Surety renewal rights to St.Paul in 2002	Int'l. Fidelity
Safeco	Safeco	Great American
Amwest	Exited the business in 2001	NAS

# *Leading Sureties no longer in the market*

- **Amwest \$105 million in premium 2001 – Bankrupt**
- **Kemper \$117 million in premium 2002- Sold business as a result of financial ratings – Co-Surety - Loss**
- **Atlantic Mutual \$37 million in premium 2002 Sold business as a result of financial ratings**
- **Fireman’s Fund \$117 million in premium Sold business because of losses**
- **Frontier \$37 million in premium – Bankrupt**
- **St Paul \$391 million in Premium 2003 – Merged with Travelers**

# Results Top Ten: SAA

1990

<u>Company</u>	<u>Direct Premiums Written</u>	<u>Loss Ratio</u>
Fidelity & Deposit	137,737,707	18.4
USF&G	122,339,387	16.6
Reliance Group	121,028,201	20.8
Aetna Life & Cos.	115,421,781	65.1
Fireman's Fund	96,630,511	13.6
Seaboard Surety	96,022,192	5.5
Continental Ins.	96,004,836	22.1
C N A Group	83,827,080	0.7
American Int'l	74,836,632	21.8
Safeco Ins. Group	74,612,101	6.8

2003

<u>Company</u>	<u>Direct Premiums Written</u>	<u>Loss Ratio</u>
Travelers Property	578,042,440	26.5
St. Paul	380,938,359	79.4
C N A Ins.	338,343,915	43.2
Zurich Group	273,475,495	2.8
Safeco Ins. Co.	211,906,171	(1.1)
Chubb Group	168,036,483	(4.4)
Liberty Mutual	150,072,986	44.1
Hartford Group	142,349,304	78.3
HICA Holding	100,459,501	54.8
Am Int'l Group	75,975,752	19.5

# *Market Share*

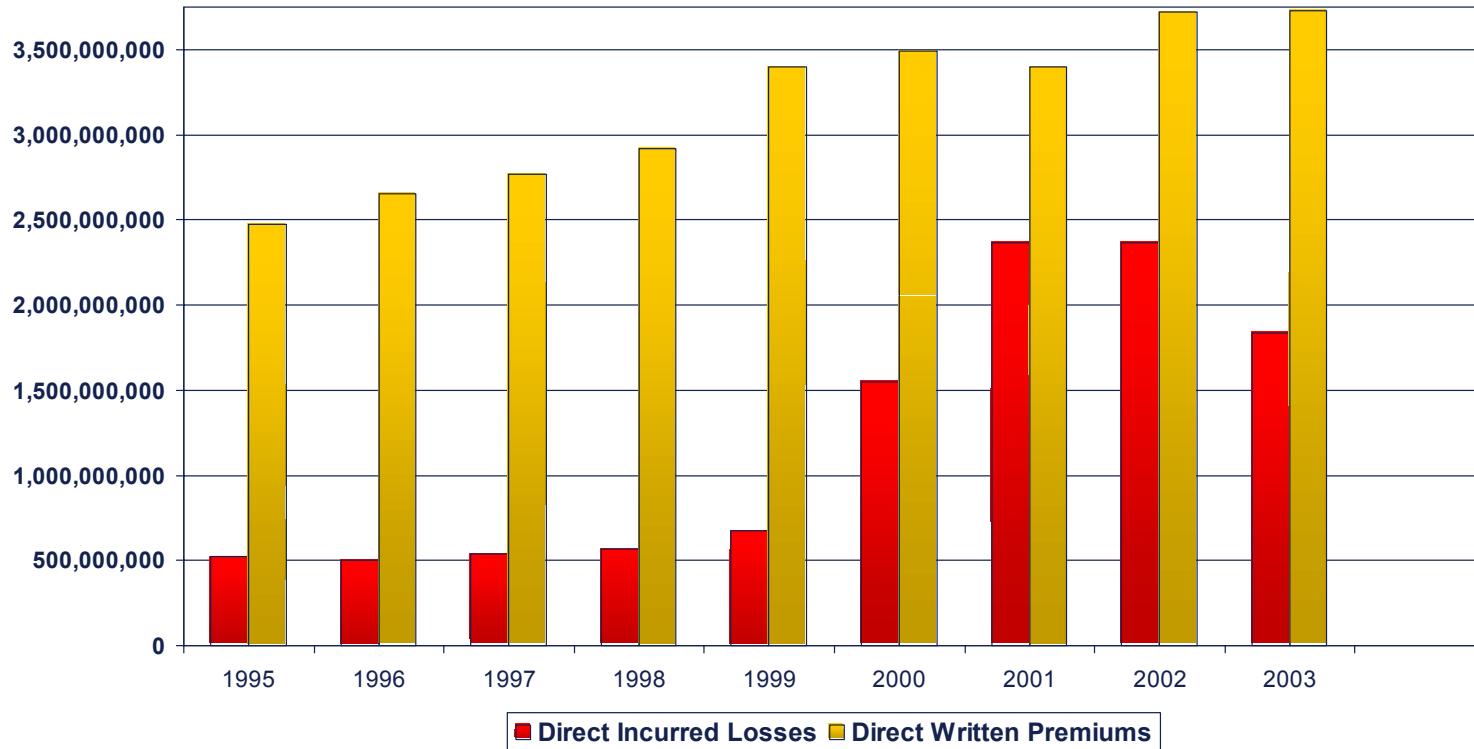
## ➤ **Changes?.....What Changes?**

### **Top Dozen Surety Writers' Market Share**

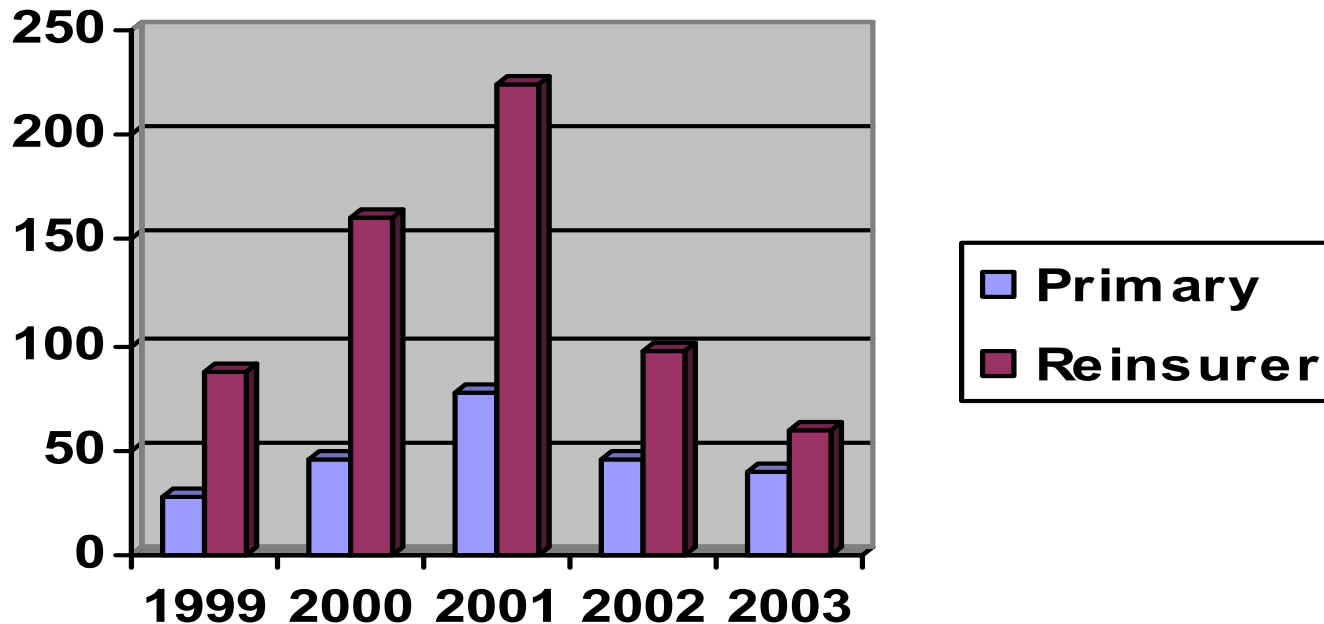
➤ **1999 – 63.1%**

➤ **2003 – 69.2%**

# *Surety Underwriting Results*



# *Primary & Reinsurer Loss Ratios*



## **Leading Loss Causes**

- **Rapid Growth – Most Frequent**
- **Geographic Expansion**
- **Performance Issue**
- **Experience – Complex Project**

# *State of the Surety Industry – Recent History*

## **All U.S. Surety Writers (in Billions\$)**

	<b>2001</b>	<b>2002</b>	<b>2003</b>	<b>Nine Months Sept 2004</b>
<b>Written Premium*</b>	<b>\$3.244</b>	<b>\$3.484</b>	<b>\$3.708</b>	<b>\$3.251</b>
<b>Losses*</b>	<b>\$2.568</b>	<b>\$2.364</b>	<b>\$1.833</b>	<b>\$2.150</b>
<b>Expenses**</b>	<b>\$1.460</b>	<b>\$1.568</b>	<b>\$1.669</b>	<b>\$1.462</b>
<b>Profit/Loss</b>	<b>(\$0.784)</b>	<b>(\$0.448)</b>	<b>\$0.206</b>	<b>(\$0.361)</b>

**\*Source: Surety Association of America Data**

**\*\* Estimated Expense Ratio of 45%**

# *Impact of Underwriting Results*



- **Capacity Crunch for large accounts \$250,000m plus**
- **Reinsurance shortages impacts underwriting approach – Rates – Higher Deductibles – Opportunistic Players**
- **Return to underwriting discipline (% case, personal indemnity, quality submissions etc)**
- **Co-surety programs for large accounts to obtain needed capacity – Stand-by surety – Credit Risk of Surety Companies – Comfort of Surety with Co-Surety partners**
- **Insurance Company management view of Surety**

# *Insurance Company Management View Surety*



- **Surety generates small premiums in relation to overall insurance operations**
- **Surety is a volatile catastrophic line of business – you can have large losses that impact the overall company results**
- **Specialized underwriting required**
- **Capital deployed / returns in surety vs to other lines of business – Allocation Competition**

## To Attract Capital – And Increase Capacity – What Has To Happen?

- **Sustained Underwriting Discipline**
- **Confidence in Pricing Model**
- **Acceptable Risk Allocation**
- **Calm Economic Waters**



# *Implications to Construction firms*

- **Co-surety/Shared surety relationships**
  - ◆ Credit risk of surety companies
  - ◆ Comfort of a surety with Co-surety partner
  
- **Indemnity agreement changes**
  - ◆ Place in collateral wording
  - ◆ Security agreements
  - ◆ Definition of loss
  - ◆ Surety vs Bank
  
- **Changing market makes having a back up surety programs a must**
  - ◆ Keep file up to date
  - ◆ Meetings - Interviews
  
- **Financial ratings**
  - ◆ Know that sureties underwriting results
  - ◆ Know the overall insurance results
  
- **Program terms**
  - ◆ Indemnity
  - ◆ Rates
  - ◆ Contract terms – Warranties, Design build, % cases

# **Contract Terms and Conditions Underwriters look for**

- **Contract Duration**
- **“Underengineered” Designs**
- **Warrant Provisions**
- **Performance Efficiency Provisions**
- **Liquidated Damages Levels**
- **Materials Escalation Clauses**
- **Bond Forms**
- **Residential Projects may be the next big thing**

# *Best Practices*

- No Surprises
- Timely, Quality Financial Presentations
- Have Surety Understand Your Business Plan
- Understand Surety's Need
- Highly Value and Continually develop Lasting Surety Partnership Relationships

# *What you need to be able to know about you surety program?*

- **Underwriting results for my Surety**
- **Financial rating of your surety**
- **Who is my back up surety**
- **How does my surety analyze my company**
  - ◆ **Know clearly what the surety is expecting and what you expect of them**
  - ◆ **Look at their analysis**
- **What are the personnel changes within my surety at the Local and National level**
- **What level of reinsurance support does my surety rely on to service business**



## *The Goal*

**A stable reliable surety program that  
allows your firm to achieve its stated  
business plan and take advantage of  
unique opportunities in the market**

# *Market Update Conclusions*

- **Surety Market will continue to be unsettled**
- **More consolidations likely**
- **Surety programs will require more effort than in the past**
- **Fragmenting market between carriers on jumbo risk and the rest of the market**
- **Rates likely to increase**