

Arizona Department of Insurance 2013 Market Monitoring

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Businessowner' Insurance

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The BOP policy is a multiple-line insurance policy for small and medium-sized businesses (e.g., retail businesses, etc.) that meets each insurer's program specifications and qualifications. Insurers originally designed the BOP as an alternative to the commercial multi-peril policy ("CMP"). While BOPs are easier to read and understand, their limits and coverage is generally less flexible than CMPs.

I. Rate System:

Arizona's "open competition" law, applicable to BOP, prohibits insurers from charging excessive, inadequate or unfairly discriminatory rates, or rates that will have the effect of destroying competition, or establishing a monopoly. By statute, a rate is not excessive if "a reasonable degree of price competition" ("RDPC") exists at the consumer level. The law presumes a competitive market exists unless the Director, after a public hearing, determines that a RDPC does not exist in the market.

II. Market Monitoring Methodology:

To monitor the market, the Department relies upon insurers' rate filings and annual statements filed with the Department, insurers' responses to an annual Department survey, current trade press articles, statistical reports, and A.M. Best data.

III. Annual Statement Data:

Insurers combine their BOP and CMP experience for annual statement reporting purposes to the Department. See Table A. Typically, the BOP comprises about 30% of the reported CMP direct written premium ("DWP"). BOP 2012 data evidence that:

- Insurers' 2012 DWP increased about 2.42% over 2011.
- Insurers' direct incurred loss ratio decreased to 82% (includes loss adjustment expense) in 2012 compared to 205% in 2011.
- Business is concentrated in the Top 25 insurers.
- Insurance company groups (i.e., affiliated companies) dominate the entire market with Zurich Financial Services, St. Paul Travelers Companies, Hartford Insurance Group, CNA Insurance Companies, and Nationwide Group controlling 63.65% of the market. These five company groups have a total of 27 affiliates writing BOP business in Arizona.
- The number of insurers that have the authority to write BOP business exceeds the number actually writing the coverage.

Table A: Commercial Multi Peril versus Businessowner's Historical Experience (Year Ending 12/31)

CY	Line	Written Premium	Earned Premiums	Losses Paid	Losses Incurred	Incurred Loss Ratio *
2012	CMP	\$526,971,040	\$515,966,616	\$347,480,013	\$238,143,958	46.16%
	BOP (31.15% of CMP)	\$164,146,783	\$156,586,619	\$118,678,149	\$96,627,554	61.71%
2011	CMP	\$500,006,641	\$497,948,004	\$781,160,069	\$670,633,037	134.68%
	BOP (32.05% of CMP)	\$160,258,038	\$147,757,012	\$296,582,583	\$273,696,787	185.23%
2010	CMP	\$487,051,027	\$495,768,114	\$375,701,305	\$619,616,965	125.98%
	BOP (28.65% of CMP)	\$139,524,805	\$138,611,034	\$104,329,090	\$154,914,631	111.76%
2009	CMP	\$504,881,829	\$519,111,473	\$254,820,751	\$179,647,306	34.61%
	BOP (29.14% of CMP)	\$147,101,343	\$146,667,789	\$83,979,909	\$80,547,137	54.92%
2008	CMP	\$555,879,290	\$565,859,546	\$274,807,296	\$246,929,532	43.64%
	BOP (28.74% of CMP)	\$159,743,454	\$157,370,915	\$75,268,041	\$100,742,067	64.02%
2007	CMP	\$577,984,619	\$577,214,782	\$234,662,461	\$238,904,916	41.38%
	BOP (28.94% of CMP)	\$167,255,732	\$159,678,175	\$67,176,390	\$67,419,452	42.22%
2006	CMP	\$578,623,018	\$559,163,269	\$224,347,051	\$221,975,147	39.70%
	BOP (28.45% of CMP)	\$164,594,783	\$155,207,165	\$68,015,748	\$77,443,692	49.90%

* Incurred Loss Ratios do not include loss adjustment expenses.

IV. Survey Responses:

In 2013, 77 active insurers responded to the ADOL's BOP survey and reported that they are seeking new policies while also retaining their existing business. Overall, insurers' responses regarding market conditions were positive.

- **The majority of surveyed insurers said that:**
 - Competition is high;
 - Coverage is available;
 - Groups play a major role;
 - Combined ratios have decreased;
 - Pricing is important and levels are adequate;
 - It is not difficult to enter the market; and,
 - Reinsurance is readily available.
- **The majority said that their particular company:**
 - Adjusted rates in 2012;
 - Is actively seeking new business;
 - Considers the BOP, in Arizona and nationally, to be of major importance;
 - Perceives that the BOP is a profitable line;
 - Has not materially increased declinations, cancellations, or non-renewals in 2012; and,
 - Will maintain its current underwriting and risk-eligibility approach at least through 2013.

V. Major BOP Market Trends:

Trend # 1: Not all insurers possessing the authority to write BOP insurance are actually writing. Of the 316 insurers that reported some CMP activity in their annual statements for 2012, only 77 wrote BOP business. The remaining 239 insurers have the legal authority to write the BOP in Arizona, but for reasons of their own, have elected not to participate in the market. These "latent" insurers, although currently not actively seeking new business, potentially could immediately enter the market.

Trend # 2: Market concentration continues in the Top 25. The market share for the Top 25 was 87% (86% for 2011). The top five insurers have a 42.71% share of the market. Competition among these insurers is particularly intense. Mid-Century IC is in the number one position and replaced American Family Mutual IC, the leader for the prior two years. American Family Mutual IC, Travelers Casualty IC of America, Truck Insurance Exchange, and State Farm Fire and Casualty Co round out the top five in that order.

The top five's 2012 market share and rank follow:

Rank	Company	2012 Market Share
1	Mid-Century IC	10.38%
2.	American Family Mutual IC	9.26%
3.	Travelers Casualty IC of America	8.50%
4	Truck Insurance Exchange	7.65%
5.	State Farm Fire and Casualty Co	6.92%
	Total:	42.71%

Trend # 3: Policy counts decreased while average premiums increased. Policy counts decreased approximately 1% in 2012; while the average premium charged per policy increased almost 2.67%. Although 55 insurers reported rate changes within the past year, the majority of the market (67%) believes that 2012 rates have not substantially changed in the past year. On a national level, the BOP makes up 30% of the CMP line. The increase in average premium may have contributed to an increase in the overall net premiums written for the CMP line. Although rates have been adjusted, insurers appear reluctant to relinquish market share in this economy, resulting in competitive pricing benefits to consumers and businesses. The increased average premium may be a sign that while the BOP market remains in the soft market stage of the underwriting cycle, the soft market may be hardening.

Trend # 4: Loss ratios, number of claims and average claim payments decreased substantially. The direct incurred loss ratio in 2012 was 82% compared to 205% in 2011 and the actual number of claims decreased to 5,610 in 2012 compared to 9,638 in 2011. Less intense storms and weather related incidents may have resulted

in fewer claims filed. Claim payments averaged \$21,155 in 2012 compared to \$30,772 in 2011.

In 2012, insurers have managed to maintain loss adjustment expenses and this, combined with reduced incurred losses, has resulted in a more favorable incurred loss ratio.

Trend # 5: Price is important to insurers. Pricing is a major consideration for insurers and the majority believes pricing levels are adequate. While underwriting results have improved, the poor results in previous years could still be reflected in future pricing. Underwriting may become more restrictive, aiming for an upward trend in pricing levels. In 2013, some insurers expressed concern that pricing is too low. In this highly competitive market, 100% of the responding insurers agreed that price is important.

Trend # 6: Insurers report improved BOP profitability. The Arizona combined ratio decreased (118% in 2012, 236% in 2011, 165%, 2010); and, in 2013, insurers continue to project a favorable perception of BOP's underwriting profitability. While loss adjustment and underwriting expenses impact results, an insurer's losses primarily determine its profitability. Mergers and acquisitions within larger groups can distort the combined ratio changes. In 2013, the incurred loss ratio has decreased, while the loss adjustment expense ratio has remained the same; but the underwriting expense ratio is higher. Severe weather in 2011 and delayed reporting of claims associated with the 2010 hail storms are no longer an issue; however, the reported numbers suggest that insurers efforts to re-underwrite may continue as the BOP combined ratio is still unprofitable.

Trend # 7: It is not difficult to enter the BOP market. The majority of insurers stated that entry into the BOP market is not difficult. While the Top 25 insurers control of the market evidences high competition (87% market share), there are many latent insurers that could, at any time, begin writing this coverage.

Trend # 8: Reinsurance does not appear to be problematic. All insurers surveyed, responded that reinsurance is readily available.

VI. Conclusions:

The BOP is an important line for insurers who continue to prosper and increase their business in a competitive market. Mergers, acquisitions, and consolidations have increased group concentration in the market. Entry and exit from this market is easy. Consumers will find a broad range of insurers able to provide an insurance package geared to meet their specific needs at an affordable price. Although the most recent loss ratios declined, they are still unprofitable. Insurers report a competitive market where pricing levels are perceived to be adequate; however, an increasing number of insurers are concerned that pricing is too low and not adequate for the kind of coverage they write. Insurers continue to look for new ways to market this product line; but also reduce losses while maintaining reasonable pricing levels.