

Arizona Department of Insurance

2014 Market Monitoring

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Surety

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I. Rate System:

Arizona's "open competition" law, applicable to surety insurance, prohibits insurers from charging excessive, inadequate or unfairly discriminatory rates, or rates that will have the effect of destroying competition, or establishing a monopoly. As a matter of law, the Department cannot find a rate to be 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, annual statements filed with the Department, insurers' responses to an annual Department survey, current trade press articles, and A.M. Best data.

III. Annual Statement Data:

The compiled annual statement data for surety evidence that overall in 2013:

- The market is concentrated in the Top 25 insurers that have a market share of 85.6%.
- Thirty-four groups have a total market share of 94.4%.
- Arizona's surety market is concentrated in contract surety.
- Arizona's 2013 incurred loss ratio of -109.1% is much better than the national ratio of 17.0%.

Historical Experience (All Insurers Page 19, Line 24, Annual Statement Data, Year Ending December 31)

CY	1	2	3
	Written Premium	Earned Premium	Paid Losses
2013	\$88,436,910	\$90,174,789	\$30,251,109
2012	\$91,497,708	\$92,705,648	\$42,117,983
2011	\$87,672,177	\$92,086,249	\$8,278,073
2010	\$93,759,398	\$92,593,769	\$3,352,607

CY	4	5
	Incurred Losses	Incurred Loss Ratio (Col 4 / Col 2)
2013	-\$98,533,621	-109.27%
2012	\$54,905,211	59.23%
2011	\$2,371,038	2.57%
2010	\$760,804	0.82%

IV. Survey Responses:

Insurers (55) having 96.8% of the market responded to the 2014 survey. The majority said that their particular company:

- Is actively seeking new business.
- Is not increasing the number of declinations or nonrenewals in 2014 as compared to 2013.
- Believes rates impact solvency.
- Believes the availability of reinsurance is becoming less problematic.
- Will not change its underwriting stance in the immediate future.
- Believes underwriting cycles have an impact on surety.

They also reported the following information:

CY	1	2	3
	Written Premium	Policy Count for Active Insurers	Average Premium (Col 1/Col 2)
2013	\$85,631,501	112,937	\$758
2012	\$88,968,471	118,563	\$750
2011	\$85,582,451	103,808	\$825
2010	\$91,743,145	149,995	\$612

CY	4	5	6
	Paid Losses	# of Paid Losses	Average \$ Paid Claim Col 4/5
2013	\$28,947,143	3,695	\$7,834
2012	\$38,628,909	3,969	\$9,733
2011	\$8,144,727	3,762	\$2,165
2010	\$3,726,556	3,107	\$1,199

CY	7	8	9
	Incurred Losses	Incurred Loss Ratio	Combined Ratio
2013	-\$97,467,683	-111.48%	-48.40%
2012	\$53,251,578	59.36%	115.98%
2011	\$3,445,955	3.85%	52.54%
2010	\$2,187,135	2.43%	49.38%

V. Surety Market Trends:

Trend # 1: Most surety written in Arizona is contract surety. In 2013, a market share of 78.5% (80.1% in 2012) responded that it primarily writes contract bonds. The demand for contract surety is dependent on Arizona's commercial construction, population growth and economic conditions.

Trend # 2: Direct written premium decreased in Arizona. Arizona's direct written premium decreased by 3.3% in 2013 compared to an increase of 3.5% nationally. The decrease in Arizona appears to be attributable to the decrease in construction spending and a sluggish economy.

Trend # 3: The market is concentrated in the Top 25. The market remains concentrated in the Top 25 that wrote 85.6% of the market in 2013 (86.2% in 2012). The top five insurers in 2013 controlled 46.5% (46.8% in 2012) of the market.

Trend # 4: Groups control a major portion of the market. Thirty-four groups control a market share of 94.4% in 2013. The Liberty Mutual Group has regained the top spot with the highest market share of 16.9%, followed by the Travelers Group with 15.0%.

Trend # 5: Arizona's loss experience is much better than the national market. The Arizona 2013 all-insurer surety incurred loss ratio of -109.27% is better than the national 2013 incurred loss ratio of 17.0%. Arizona's negative 2013 incurred loss ratio is directly tied to one large loss reserve take down.

Trend # 6: The Arizona surety combined ratio decreased dramatically. The 2013 combined ratio of -48.4% is much lower than the 116.0% in 2012. The Arizona surety market is heavily based in contract surety, and the volatile nature of these types of bonds could impact future experience.

Trend # 7: More insurers are entering than exiting the market. There were six insurers that entered, and three that exited.

Trend # 8: A majority of the market continues to actively seek new surety business. A market share of 77.3% (74.0% in 2013) is actively seeking new Arizona surety business in 2014.

Trend # 9: Insurers are not increasing or decreasing the number of new business declinations or non-renewals. A majority of the market (96.7% for new business declinations and 87.2% for non-renewals) is not increasing or decreasing the number of declinations or non-renewals in 2014.

Trend # 10: The degree to which insurers believe rates impact solvency increased. A market share of 38.5% responded in the 2014 survey that rates impact solvency, up from 34.9% in 2013.

Trend # 11: Reinsurance is available. Only two companies with a combined market share of 1.3% who indicated obtaining reinsurance is problematic.

Trend # 12: The majority of the market perceives that underwriting cycles impact surety. A market share of 62.8% responded in the 2014 survey that underwriting cycles impact surety.

VI. Conclusions:

Most surety business written in Arizona is contract surety. Incurred loss ratios and combined ratios decreased in 2013. The Arizona surety market has been profitable for the past eight years, with the exception of 2012 when the combined ratio exceeded 100%. The market remains concentrated in the Top 25 insurers and three more insurers entered than exited the market. Insurers are actively seeking new business, are not increasing declinations or nonrenewals and find reinsurance is available.