

# Arizona Department of Insurance

## 2009 Market Monitoring

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Other Liability Insurance

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### I. Rate System:

Arizona's "open competition" law, applicable to Other Liability ("OL") 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. By statute, 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:

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

The purpose of market monitoring is twofold: to assist the Director in determining whether competition exists; and, to assist consumers with their questions and concerns about the availability of certain OL sublines of insurance.

### III. Survey Responses:

Out of 140 surveys sent, 138 insurers with a combined total market share of 90.38% responded to the Department's 2009 OL survey. The survey targeted three OL sublines: Lawyers Professional ("LP"), Directors & Officers

("D&O"), and Architects & Engineers ("AE") Professional Liability. Of the 138 insurers that responded, 22 insurers write LP, 40 insurers write D&O, and 14 insurers write AE.

- **The majority of the subline insurers said:**

- Competition has become more intense;
- Coverage is available;
- Underwriting stance remains conservative;
- Reinsurance is not problematic;
- Market entry is easy;
- New business is actively sought; and
- It's too early to know the overall impact of the subprime mortgage/credit issue.

### IV. Major OL Subline Trends:

**Trend #1:** Markets are concentrated and insurers are actively seeking new business. The Top-Five insurers in each market segment hold the majority of the market share. The Top-Five LP insurers write 68.46% of the Arizona 2008 LP market, up from 65.64% in 2007. The Top-Five D&O insurers hold 56.16% of Arizona's D&O market, down from 58.75% in 2007. The Top-Five AE insurers control 75.16% of the AE market, up from 73.08% in 2007. Insurers in all three market segments are actively seeking new business.

**Trend #2:** Easy market entries and exits. Insurers indicated no difficulty in entering the Arizona market. The LP market decreased from 24 to 22 insurers; 20 were existing insurers, two were new insurers and four insurers exited. The D&O market decreased from 47 to 40 insurers; 37 were existing insurers, three were new insurers and 10 insurers exited. The AE market remained the same as last year with 14 insurers; 12 were existing insurers, two were new insurers and two insurers exited.

**Trend #3:** Coverage remains available.

Insurers from all three markets indicated they expect no change in coverage availability in 2009 compared to 2008 availability. A decline occurred in both insurer participation and number of policies written. In the LP market, insurer participation decreased 8.4% and their policy count decreased 9.3%. In the D&O market, insurer participation decreased 15% and policy count decreased 14.2%. In the AE market, insurer participation remained the same, but policy count decreased 20%. Fluctuation in the average premium size occurred in all three market segments.

**Trend #4:** All insurers indicated they would continue their conservative underwriting stance in 2009. In addition, five of the 22 LP insurers, five of the 40 D&O insurers, and two of the 14 AE insurers indicated they would be taking an even greater restrictive approach in 2009 due to poor loss experience and/or the subprime mortgage/credit crisis.

**Trend #5:** Changes in loss experience varied in the three market segments. While the LP incurred loss ratio ("ILR") decreased, claims frequency and severity increased. The ILR decreased from 78.95% in 2007 to 47.72% in 2008. Claim frequency increased slightly by 1% (126, 2007; 127, 2008), and the average paid claim increased (\$17,702, 2007; \$47,489, 2008) increasing claim severity by 268%.

The D&O ILR improved (49.57%, 2007; 44.77%, 2008), as did the claims frequency and severity. The number of paid claims dropped (120, 2007; 56, 2008) and the average paid claim dropped (\$1,610,200, 2007; \$166,418, 2008). Claims and lawsuits arising from the 2008 economic downturn and credit events have yet to reveal the full impact to the D&O and the LP sublines markets.

The AE market is the least impacted of the three sublines by the economic downturn and credit events of 2008. Claims frequency decreased 52.6%, (95, 2007; 45, 2008) while severity increased by 246.5% (\$40,646, 2007; \$100,205, 2008). The overall ILR increased from 31.96% in 2007 to 59.97% in 2008.

**Trend #6:** Insurers in all three market

segments are not expecting changes in their 2009 non-renewals. The majority of the LP, D&O and AE insurers indicated no change or increase in the number of nonrenewals expected in 2009.

**Trend #7:** Reinsurance is not problematic for most insurers. The majority of the LP, D&O and AE insurers indicated no problems in obtaining reinsurance.

**Trend #8:** Full impact of the subprime mortgage crisis unknown. One LP insurer (8.04% market share), eight D&O insurers (37.5% market share) and two AE insurers (12.46% market share) indicate negative impacts from the subprime credit crisis. Insurers will not know the full impact of this issue for some time to come.

**Trend #9:** Alternative markets increase the availability and affordability of commercial liability insurance. Eight Risk Retention Groups ("RRGs") are within the Top 140 insurers that wrote OL in 2008; however, only one RRG fell within the targeted sublines. This particular LP RRG's direct written premium ("DWP") is 51.2% of the total DWP in the admitted LP market subline. There is no indication within the Top 140 OL insurers that RRGs wrote any D&O or AE policies; however, the Surplus Lines market is also active in writing these two targeted sublines.

**V. Conclusions:** While all of the sublines do not have a large number of insurers operating within their respective markets, coverage is available and affordable in all three sublines; entry and exit is easy; obtaining reinsurance is not problematic; insurers are actively competing for market share, and no one yet knows the full impact of the subprime credit issues.