

# Arizona Department of Insurance

## 2011 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 162 surveys sent, 162 insurers with a combined total market share of 93.69% responded to the Department's 2011 OL survey. The survey targeted three OL sublines: Lawyers Professional ("LP"), Directors & Officers

("D&O"), and Architects & Engineers ("AE") Professional Liability. Of the 162 insurers that responded, 26 insurers write LP, 55 insurers write D&O, and 18 insurers write AE.

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

- Competition is intense;
- Coverage is available;
- Underwriting stance remains conservative;
- Reinsurance is not problematic;
- Market entry is easy;
- New business is actively sought; and
- Subprime/credit issues are ongoing.

### 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 72.85% of the Arizona 2010 LP market, up from 67.20% in 2009. The Top-Five D&O insurers hold 50.00% of Arizona's D&O market, down from 51.30% in 2009. The Top-Five AE insurers control 65.10% of the AE market, down from 74.15% in 2009. 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 increased from 25 to 26 insurers; 23 were existing insurers; three were new insurers and two insurers exited. The D&O market increased from 51 to 55 insurers; 47 were existing insurers, 8 were new insurers and four insurers exited. The AE market increased from 15 insurers to 18 insurers; 14 were existing insurers, four were new insurers and one insurer exited.

**Trend #3:** Coverage remains available. Insurers from all three markets indicated they

expect no change in coverage availability in 2011 compared to 2010 availability. An increase occurred in both insurer participation and the number of in-force policies written, except for AE where the number of in-force policies written decreased. In the LP market, insurer participation increased 4.00% and the in-force policy count increased 6.02%. In the D&O market, insurer participation increased 7.80% and the in-force policy count increased 18.17%. In the AE market, insurer participation increased by 20.00% while the in-force policy count decreased by 4.02%. Fluctuation in the average premium size occurred in all three market segments.

**Trend #4:** The majority of the insurers indicated they would continue their conservative underwriting stance in 2011. In addition, three of the 26 LP insurers, five of the 55 D&O insurers, and two of the 18 AE insurers indicated they were tightening their underwriting approach in 2011 due to a national corporate decision, loss severity and higher than normal operating expenses.

**Trend #5:** Changes in loss experience varied in the three market segments. While the LP incurred loss ratio ("ILR") and claims severity decreased, frequency increased. The ILR decreased (45.11%, 2009; 38.86%, 2010). Claim severity decreased (\$121,000, 2009; \$86,751, 2010), while claims frequency increased (64, 2009; 83, 2010).

The D&O reflected decreases in the ILR (104.4%, 2009; 51.30%, 2010) and claims severity (\$295,196, 2009; \$178,597, 2010) while claims frequency increased (119, 2009; 233, 2010). Claims and lawsuits arising from the 2009 economic downturn and credit events will continue to impact the D&O and the LP subline markets for many more years.

The AE market is the least impacted of the three sublines by the economic downturn and credit events of 2009. Claims frequency decreased (125, 2009; 119, 2010) and claims severity decreased (\$83,074, 2009; \$29,506, 2010). The overall ILR increased from 35.25% in 2009 to 42.94% in 2010.

**Trend #6:** Insurers in all three market segments were not expecting changes in their 2011 non-renewals. The majority of the LP, D&O and AE insurers indicated no change or increase in the number of nonrenewals expected in 2011.

**Trend #7:** Reinsurance is not problematic for most insurers. Although the majority of the LP, D&O and AE insurers indicated no problems in obtaining reinsurance, one LP insurer indicated a problem associated with the high cost of coverage and one AE insurer had difficulties with reinsurers not wanting to write their risks.

**Trend #8:** Impact from the subprime/credit issues vary by market segment. Two LP insurers (3.75% market share), seven D&O insurers (34.59% market share) and three AE insurers (6.99% market share) indicate that the impact is substantial due to increases in claims and litigation. The full impact won't be known for years.

**Trend #9:** Alternative markets increase the availability and affordability of commercial liability insurance. Ten Risk Retention Groups ("RRGs") are within the Top 162 insurers that wrote OL in 2010; however, only one RRG fell within the targeted sublines. This particular LP RRG's direct written premium ("DWP") is 37.55% of the total DWP in the admitted LP market subline. There is no indication within the Top 162 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 although no one yet knows the full impact of the subprime/credit issues, we do know that claims, litigation and loss ratios are impacted by this issue.