2017
Insurance Market Outlook
Insights from our national practice leaders
Table of contents

03 Executive summary
05 2017 Market Outlook premium trends forecast
06 Property
08 Liability
10 Workers’ compensation
12 International
14 Environmental
16 Aviation
18 Public company directors’ and officers’ liability
19 Fiduciary liability
20 Private/non-profit management liability
21 Employment practices liability
22 Crime
24 Medical malpractice
26 Kidnap, ransom and extortion
28 Representations and warranties
29 Technology and professional errors and omissions
30 Network security and privacy risk (cyber)
31 Commercial surety
32 Contract surety

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Executive summary

As predicted in the 2016 Wells Fargo Insurance Market Outlook, 2016 was a buyer’s market for both property and casualty (P&C) commercial insurance and affiliated lines. The majority of insureds experienced medium to high single-digit to low double-digit rate decreases across a broad range of coverage offerings with a few coverage line exceptions. These insureds also benefited from increasing market capacity in the form of new markets competing for business and broader coverage terms and conditions. This abundant market capacity and competition for new business helped drive prices down overall for the majority of insureds, despite an environment of level or declining treasury yields. Cyber liability insurance, which is a newer product, continues to expand in scope — as have the cyber attacks and high-profile data breaches it is intended to cover.

For 2017, experts predict the U.S. economy will continue to expand. Job growth means higher payroll, sales, more autos insured by businesses, construction, property expansion, etc., which will increase gross premiums underwritten. The majority of insureds will continue to see reductions, just not as high as in prior years.

Hurricane Matthew did little to dent industry surplus, which remains at an all-time high. However, we are beginning to see the pace of reductions slowing and the market stabilizing somewhat. Due to year-over-year rate reductions, the degree of positive underwriting gains is decreasing. Coupled with the combined ratio ticking back up to 100%, these headwinds will result in more underwriting discipline than in past years, and some insurers are walking away from perceived unprofitable deals.

Specific factors and trends that will affect the 2017 market include:

- Continued rise in medical inflation as evidenced by the 6.5% year-over-year growth rate
- Profitability challenges faced by the Affordable Care Act (ACA), which may drive injured people to file workers’ compensation claims in lieu of healthcare claims
- Terrorist events increasingly occurring on U.S. soil
- High-profile data breaches and impostor fraud continuing to occur, increasing the focus on cyber crime and reputational risk loss mitigation; these issues are board level considerations and companies are doing what they can to assess their risk and attempt to mitigate losses in advance of an event
- Aggregation a concern for cyber carriers, because a single data privacy event could result in multiple claims reported to the same insurance companies
- The recent ruling in Florida, which permits negotiated fee agreements between claimants and attorneys, leading the National Council on Compensation Insurance (NCCI) to raise workers’ compensation rates by an unprecedented 15% (this has been challenged so there is a delay in implementation)
- Elimination of the option for employers to opt out of the Workers’ Compensation Act in Oklahoma, which will likely drive costs up for employers and cause other states considering opting out to push these initiatives out many years
- Securities class action filings increasing year over year
- Continued focus on data analytics, as insurers use cleaner data to develop more sophisticated and accurate predictive loss patterns and trends for a variety of P&C lines, and increasingly factor the data into underwriting decisions
- Surplus capital continuing to be deployed in existing and emerging product lines, although there will be more underwriting discipline
- Catastrophe bonds and other forms of alternative capital continuing to attract investors for property-oriented risks, and similar products being developed for non-property exposures for both insurers and corporate entities
Insights from our national practice leaders
2017 Insurance Market Outlook

- Larger guaranteed-cost or low-deductible programs in excess of $1 million in premium becoming more challenging to underwrite — especially workers’ compensation, insureds with large auto fleets, clients exposed to cyber risks, and clients who maintain sensitive personal data that can be compromised.

- Risk managers increasingly considering terrorism and political violence coverage for international exposures, due to the growth in terrorist organizations.

As these conditions extend throughout 2017 and beyond, we believe insurers will sustain underwriting profitability, resulting in the continuance of a buyer’s market. The market will not be as robust as in prior years, because the pace and level of reductions for the majority of insureds will temper a bit. In particular, buyers of guaranteed-cost or low-deductible programs will experience lower reductions and likely single-digit increases in 2017, compared to buyers of large deductible and retention programs. Of course, a series of events, including natural disasters, terrorist events of significance across the globe, or a pandemic, could negatively affect the insurance market.
## 2017 Market Outlook forecast trends

<table>
<thead>
<tr>
<th>Category</th>
<th>Forecast Range</th>
</tr>
</thead>
<tbody>
<tr>
<td>Property</td>
<td>Flat to 10% decrease</td>
</tr>
<tr>
<td>CAT property</td>
<td>Flat to 10% decrease</td>
</tr>
<tr>
<td>Primary general liability</td>
<td>Flat to 10% decrease</td>
</tr>
<tr>
<td>Primary auto liability</td>
<td>Flat to 15% increase</td>
</tr>
<tr>
<td>Umbrella liability</td>
<td>Flat to 10% decrease</td>
</tr>
<tr>
<td>Excess liability</td>
<td>Flat to 10% decrease</td>
</tr>
<tr>
<td>Loss-sensitive workers’ compensation</td>
<td>Flat to 10% decrease</td>
</tr>
<tr>
<td>Guaranteed-cost/low-deductible workers’ compensation</td>
<td>Flat to 10% increase</td>
</tr>
<tr>
<td>International</td>
<td>Flat +/- 5%</td>
</tr>
<tr>
<td>Environmental</td>
<td>5% decrease to 5% increase</td>
</tr>
<tr>
<td>Aviation</td>
<td>Flat to 10% decrease</td>
</tr>
<tr>
<td>Public company directors’ and officers’ liability</td>
<td>5% to 10% decrease</td>
</tr>
<tr>
<td>Fiduciary liability</td>
<td>5% decrease to 5% increase</td>
</tr>
<tr>
<td>Private/non-profit management liability</td>
<td>Flat +/- 5%</td>
</tr>
<tr>
<td>Employment practices liability</td>
<td>Flat +/-5%</td>
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<tr>
<td>Crime</td>
<td>Flat +/-5%</td>
</tr>
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<td>Medical malpractice</td>
<td>5% to 10% decrease</td>
</tr>
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</tr>
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<td>5% to 10% decrease</td>
</tr>
<tr>
<td>Technology and professional errors and omissions</td>
<td>Flat to 5% decrease</td>
</tr>
<tr>
<td>Cyber</td>
<td>Flat to 5% decrease</td>
</tr>
<tr>
<td>Contract surety</td>
<td>5% to 10% increase</td>
</tr>
<tr>
<td>Commercial surety</td>
<td>5% to 10% increase</td>
</tr>
</tbody>
</table>
Property

The global property insurance marketplace remains extremely competitive, from a pricing, terms and conditions, and available capacity perspective. In 2016, like the past several years before it, there was a lack of substantial industry-wide catastrophic losses and plenty of working capacity available. The exception was Hurricane Matthew, for which insured losses are estimated to be in the $6 billion to $9 billion range. Carriers continue to fight for market share. This environment should continue into 2017 and the foreseeable future, assuming normal loss activity continues at a similar pace.

The market today

- The market can be categorized as consistent, steady, and capacity-rich. Both general carriers and reinsurance forces are effectively mirroring the past couple of years.
- Years 2012 through 2016 have been mostly profitable for commercial property carriers from a macro perspective. It appears that 2017 will again bring reduced premiums and rates.
- As a result, we expect insurers to be very competitive in 2017, with continued single to low double-digit price or rate reductions available to most commercial property insureds — especially those with favorable loss records and superior risk quality.

Market capacity

- Carriers injected some new capacity and capital into the global property marketplace, although at a slower pace than preceding years.
- Carriers are deploying additional capacity on large layered and shared programs, frequently forcing incumbent markets to offer significant increases in authorized line sizes as they strive to hold program participation and increase market share.
- Earthquake, flood, and named windstorm capacity have increased since 2015. However, California earthquake exposure and high-hazard flood zone risks are driving the deployment of total capacity that any particular insurer will provide.
- Capacity for stand-alone terrorism coverage is broadly available with approximately $1.5 billion available in the global marketplace.

Topical issues

- While meaningful, wind, flood, and storm surge losses result due to Hurricane Matthew are unlikely to affect market surplus and/or deployment of capacity.
- The newest modeling software incorporates convective storm probability.
- Data quantity and integrity remain paramount to achieve optimal results.
- Insurance to value (ITV) continues to be important for global property carriers.
- The already completed extension of the Terrorism Risk Insurance Act and Terrorism Risk Insurance Program Reauthorization Act (TRIA/TRIPRA) through 2020 makes coverage for terrorism widely accessible — except for properties that are seen as potential targets (i.e., malls, power plants, and sports stadiums) and those that are located in very large metropolitan geographies (i.e., New York, Chicago, San Francisco). The overall take-up rate is around 70%, and the rates range from 0% to 5% of the commercial property premium.
- Cyber is becoming more of a concern even on the property side, and will be a hot topic for years to come.
- 2016 showed reduced pricing and increased availability for named windstorm and storm-surge coverage, along with reductions in industry-common retentions in some cases.
- High-hazard flood continues to be analyzed and underwritten cautiously.
- Tornado and hail damage continue to drive loss records and will be scrutinized more closely in the future, as these perils have been loss leaders recently.
- Further relief on global catastrophe (CAT) treaties will become effective January 1, 2017.
- There is an increased opportunity to fortify multiyear program terms as many carriers try to level-off continued softening of property rates. Many of these agreements are put into force with preset declining rate agreements.
Forecast for 2017

• The property insurance market is stable and well capitalized, and rate reductions will be achievable in most risk classifications. Accounts without recent or historical losses, and with above-average construction and acceptable fire protection features, will continue to receive the most positive results.

• Carriers will continue to battle for market share but may be cautious while deploying increased capacity, especially in catastrophic areas.

• Property insurance underwriters will likely continue to be extremely competitive with respect to new business opportunities.

• Most parties are questioning what might change the “softness” of the property market. Many consider that it will take an event or events totaling more than $100 billion to shift the market from its current environment. Another viewpoint is that several consecutive quarters of underwriting unprofitability may put pressure on carriers to increase rating metrics on a more widespread scale. Additionally, a sharp rise in interest rates may lure some alternative capital away from the insurance marketplace, potentially decreasing some of the available capacity.

• Accurate, high-quality underwriting data will improve renewal outcomes, with insurers remaining disciplined as profitability is crucial. Modeling (RMS/AIR/Blended) will continue to affect capacity and pricing guidelines. By having the most comprehensive data (including secondary modifiers), insureds will be in a better position to understand their true risk profile and will be more likely to achieve favorable renewal outcomes.

• From a cost of capital perspective, catastrophic property pricing may be getting near a bottom where carriers have to consider required returns and expenses incurred. Although there remains a wealth of capacity, the models — along with these capital requirements — may slow some of the decreases in that arena. Underwriting results stemming from Hurricane Matthew are unlikely to influence behavior in 2017.

• Overall, we expect the property market to continue to realize reductions, generally ranging on average from flat to 10%.

* Any reductions are predicated on positive and favorable loss experience. Accounts with loss frequency and severity issues will continue to be evaluated carefully, and many may not see pricing in line with peers that have better experience, construction, and exposures. Also, accounts that received substantial reductions in 2016 may not be afforded renewal reductions to the same magnitude in 2017.
Liability

In 2016, we’ve seen continued competition for premium dollars, as well as new capital entering the market. However, increased natural disaster losses and a continued decline in treasury yields and other low-risk investment options are putting additional pressure on underwriting discipline. These two factors, combined with increased settlements for auto liability claims and recent court decisions that are causing increased costs for workers’ compensation claims in specific states, are projected to cause the P&C industry’s pretax return on equity to decline by 1 to 2 percentage points in 2016. They also are expected to move the combined ratio closer to 100%, the highest level since 2012.

The most aggressive pricing will be for clients with exceptional loss experience and who demonstrate appropriate risk management. Increased use of predictive modeling will also drive a more selective marketplace.

Insurers recognize that lowering premium every year to gain market share is not sustainable. Overall, U.S. P&C statistics for the first half of 2016 reflect this (published in September by A.M. Best):

- “Posted an underwriting loss of approximately US $2.3 billion, and a 3.5% decline in year-over-year net investment income.”
- “… realized capital gains declined 42.3% from their level for the first two quarters of 2015, U.S. $4.6 billion from U.S. $8.1 billion. Taxes were down by 14.6%, which provided a modest benefit to net income…”

The market today

Increasing loss ratios and decreasing return on investments suggest less-aggressive pricing. The competition for premium dollars still exists, but with a slight climb in overall pricing. Premium competition will not be nearly as aggressive for more volatile industries, such as pharmaceutical and energy.

The market for automobile liability has been more volatile than primary general liability and umbrella and excess liability. Auto liability remains competitive for clients with substantial fleet safety initiatives and positive loss experience. However, retentions are generally moving upward. Automobile premiums for smaller, private passenger and service fleets are competitively priced, but with slightly higher prices. The wholesale market for small and large auto risks is still viable, although pricing may be somewhat higher.

Pricing in the umbrella and excess liability market remains very competitive. However, markets are seeking a reduction in single-layer limits to secure an improved premium per million of limits.

Market capacity

Generally, the liability market remains flush with capacity, with new capital continuing to flow into the insurance marketplace. Continued mergers and acquisitions (M&A) within the insurance industry should have no real effect on market capacity, at least in the short term.

- Automobile liability capacity remains adequate, but is shrinking somewhat for larger fleet risks. There is good capacity in the retail and wholesale marketplace for a higher cost.
- For stand-alone products liability, the market remains limited, with only a select numbers of insurers willing to compete aggressively on risks for inherently difficult product lines and severe and volatile loss experience.
- Lead umbrella and excess liability capacity continues to be plentiful. Pricing per million on the upper layers may have reached minimum levels, thereby reducing insurers’ willingness to reduce premiums in those layers.

Topical issues

- Clients need to conduct insightful analytics to best assess and secure optimal pricing for all program designs: guaranteed-cost, lower-deductible, and larger loss-sensitive programs. These analytics include assessments of safety initiatives and claims mitigation measures, as well as loss analytics.
- While insurers are seeking to grow their market share, there is more disciplined underwriting, and the best terms will be given to existing and longstanding clients. Multiyear deals are also still available and may prove to be a client’s best option as the market changes.
Creative and alternative risk options for legacy risks (known and unknown) are worth exploring. The rate-on-line for these types of programs is far higher than for general, ongoing risks.

Alternative forms of collateral to letters of credit (LOC) remain available, but are restricted to clients with stronger financials. Cost of collateral from financial institutions will continue to increase for clients with suspect financials. Collateral is a key component of a client’s overall loss-sensitive insurance program that should be negotiated as strongly as the risk transfer component.

**Forecast for 2017**

**Primary casualty:**
- Insureds with higher retentions will see a competitive softening of the market, probably flat to a 10% decrease. Those clients with stellar loss experience and a willingness to assume greater risk could see bigger decreases.
- Insureds with heavy fleet exposures will experience a hardening of the market, and clients with average experience will see flat to slightly increasing premiums. The market will require larger retentions and potential increased rates of up to 15% or more for clients with poor loss experience.
- More increases than decreases are likely with guaranteed-cost programs based on deteriorating loss ratios experienced by the P&C marketplace. This fluctuation in pricing should be limited to a moderate swing of 5% increase to 5% decrease, depending greatly on a company’s specific loss experience.

**Umbrella and excess liability:**
- Lead umbrellas are still competitive. We expect increasing capacity and the staunch competition seen in past years to continue during 2017. Expect 5% to 10% pricing decreases, but with an effort by the market to raise attachment points for auto liability, particularly on tougher auto fleets.
- Excess liability rates are expected to vary based on the layer, with rates flat to decreasing 10% for mid-limit layers, and rates leveling out at the current pricing for the upper layers.
Workers’ compensation

In 2016, we saw a continued trend in workers’ compensation (WC), including a reduction in premium rates overall. Combined loss ratios are increasing, and this, in conjunction with declining treasury yields and low-risk investment opportunities, means a cash-flow underwriting mindset will not continue as in the past. There is underwriting discipline for clients that have experienced poor loss results and declining financials, and that reside in more difficult jurisdictional domiciles (i.e. Florida, California, New York, and others) and industry classes. Additionally, carriers have been seeking higher retentions as the result of loss severity activity, or in circumstances where clients are pursuing greater premium savings.

The market today

- There is healthy competition for premium dollars, which continues to drive desirable pricing. This is more prevalent on loss-sensitive programs.
- Increased retentions will be more prevalent due to increased underwriting discipline and stronger claims (post- and pre-) mitigation exercised by clients.
- Carriers will give more consideration to unbundling claims service. This is confirmed by Liberty Mutual’s move toward an unbundled alternative.
- Guaranteed cost is a less attractive option for clients who are not driven by absolute budget certainty or balance sheet variability. This movement away from guaranteed cost is driven by clients with an improving tolerance for risk, and also in response to continued medical cost inflation, statutory benefits escalation, and the encroachment of employee benefits claims into the WC coverage area. Recent court decisions in Florida may weigh heavily on the state’s guaranteed-cost (GC) rates and could affect some insurance carriers’ appetites to write programs for clients with significant Florida exposures.

Market capacity

- Carriers are still entering this market space, including those not normally considered WC alternatives, although this is more likely for loss-sensitive programs.
- Specific industries will continue to experience reduced capacity and a smaller marketplace from which to secure alternatives, mainly due to the loss severity and volatility associated with those industries.
- Dialogue continues in various states regarding nonsubscriber options, but states that have recently passed such legislation have not seen the same success or participation level as Texas.
- Guaranteed-cost capacity is still available, but less so for clients with volatility and severity in their losses.

Topical issues

- Pre- and post-loss mitigation, and proactive claims reserving and resolution, are becoming more common than in the past. This enhanced strategy is undertaken to mitigate such things as continued medical cost inflation, increasing severity, and increasing levels and cost of collateral.
- Alternative forms of collateral are still being used to address the decreasing LOC capacity, including trust or pledge of security (working or nonworking), surety, buy-downs, and advance future paid-loss credits (based upon the client’s financial strength).
- We expect clients to continue to receive loyalty- and longevity-based pricing and collateral benefits from the incumbent carrier, including multiyear rate offerings.
- Reinsurance remains plentiful, as competitively priced alternative forms of reinsurance continue to exist and grow.
- Medical cost inflation is increasing WC claims costs.
- Internal reserve strengthening for older policy years, combined with an increasing reliance on predictive modeling by carriers, is having an adverse effect on pricing, but the market is still competitive.
• Analytics relative to past and future loss data are increasingly being used and are an absolute necessity to intelligently negotiate optimal pricing, program design, and collateral. Predictive modeling has become a key underwriting tool in the industry.

• While self-insurance remains a WC alternative, states are becoming more conservative on their collateral position for many qualified self-insureds. Additionally, more onerous costs associated with exiting self-insured status have caused many companies to view this option more closely.

Forecast for 2017

• Pricing will be driven by maintaining or increasing market share. However, expect underwriting discipline to be exercised more than in the past. For attractive clients with good risk profiles, positive loss experience, and the right appetite for risk retentions, competition will remain strong.

• We expect a continued upward movement of retentions due to increases in claim development and severity.

• A client’s pre- and post-loss mitigation activities will be key underwriting factors, as these activities are seen as a measurable effort to slow loss development.

• The underwriting community is becoming far more analytics based and is using improved predictive modeling tools as a differentiator. Solely reducing premiums to secure additional market share is not sustainable at current investment return rates. Premiums can only go so low before the return on capital no longer makes sense for carriers.

• Loss-sensitive programs will experience pricing that is flat to down 10% for clients with clean and improving loss experience. Clients with deteriorating loss experience will see pricing range from flat to a 10% increase.

• Guaranteed-cost programs will experience flat to a 10% or more increase. Clients with extremely clean loss experience may be exceptions. Guaranteed-cost pricing will also vary by a client’s specific state payroll distribution, due to states’ legislative pressure on adequacy of rates and, as referenced earlier, the effects of inflation and court decisions.

The increasing combined loss ratios and deteriorating returns on investment will drive more stringent pricing and underwriting.
International

In 2014 and 2015, we saw international placements as a buyers’ market, with the availability of an average 5% rate reduction across P&C lines (with the exception of more catastrophic-prone risks). In 2016, market rates stabilized somewhat — although due to still growing capacity and competition among multinational insurers, rate decreases were available for more attractive risks.

The market today

We speculate that in 2017 we will continue to see stable rates and carriers putting more underwriting onus on quality risks and better underwriting data coming from insureds.

In the past couple of years, especially in Europe, carriers have been allocating more of their capacity at competitive rates to risks that have in-depth exposure data. This was at first more relevant for carriers to substantiate the fair market value of their allocated rates and premiums.

Now we are seeing laws, such as the Insurance Act of 2015 that fully took effect on Aug. 12, 2016, changing legal provisions in insurance contracts in the U.K. This has forced both insurers and insureds to be more specific in their “duty of good faith.” This puts more responsibility on the insured to provide good underwriting information and represent a true loss picture, regardless of providing a “no known losses” or “known, but not reported” letter. In effect, the Insurance Act changed cancellation provisions in the policy contract to disallow the insurer from denying or canceling coverage due a misrepresentation of material facts. Policy forms have changed, and therefore underwriting has been tightened up and insureds need to do a better job representing their risk exposures in their submissions to underwriters.

Market capacity

Over the last the year there has been some consolidation of insurers, and in 2016 we are seeing multinational insurers divesting themselves of the owned operations in countries where world trade and growth potential is lower than in more robust marketplaces.

With compliance and governance still a main concern for brokers and insureds, the question is whether multinational insurers will still have control over best practices and a good local standard of coverage and service.

P&C rates, depending on geographic location and business class, have stabilized. However, moderate rate decreases of 2% to 5% are still available.

Topical issues

- U.K. insurance premium tax rate increased 9.5% to 10%.
- In China, “cash before cover” for multinational businesses is being enforced by some local carriers in some provinces.
- Several large multinational insurers rolled out new policy forms with material changes.
- Brexit is not yet having an effect on Freedom of Service (FOS) policies. However, once the U.K. completes its withdrawal from the European Union (EU), we expect the origin of FOS policy issuance to possibly change. London market carriers are looking at contingency plans for redomiciling in the EU or at least forming additional EU-based companies.
- There is a new scenario for the Brazilian insurance market, where there is a local tendency to issue policies with a maximum 30-day retroactivity period.
  - Although there is no official statement on that, from SUSEP (the Brazilian regulatory entity), the top three local insurers for global programs have already positioned themselves favorably with respect to this standard.
  - Therefore, in the case of a program with an expiration date of December 31, the local insurers must receive the conditions from the controlling office no later than January 15, so they have enough time to work on the conditions and send those to the local broker. Insurers and local brokers need at least five days to receive conditions from the controlling office underwriter, prepare a local quotation and send it to the local broker to check, and forward the terms onto the local insured.
  - All required anti-money laundering forms must be filled out, signed by the client, and submitted to the carrier for approval prior to binding coverage.
As cyber risk continues to become an increasing issue, insureds are inquiring and obtaining proposals for this coverage.

Due to continued and increased political risk, political violence, and trade credit concerns, insureds are taking a more active approach to procuring the needed coverage, even though minimum premiums are much higher than expected for international placements.

Forecast for 2017

Primary foreign casualty — Guaranteed-cost programs should experience stabilized but moderate (2% to 5%) rate decreases.

Primary foreign property — Property programs should experience stabilized but moderate rate decreases of 2% to 5%.

“Duty of good faith” puts more responsibility on insureds to provide good underwriting information and represent a true loss picture. Insurers vying for business growth are more apt to allocate their capacity for extremely competitive pricing toward insureds that have better-than-average risk management practices, and that are able to provide documented exposure data.
Environmental

The big story of 2016 that no one predicted was AIG’s sudden and stunning exit from the pollution legal liability marketplace (i.e., environmental site liability) without warning. This caused shockwaves in the industry. AIG, the “inventor” of pollution legal liability, had written some of the toughest risks and created unique solutions, then called it quits after more than 30 years of leadership in this area.

While AIG still had tremendous market share even after five years of unprecedented growth of insurer entries into the industry, its exit was shocking yet somewhat of nonevent for 80% of the risks. AIG’s talent was quickly absorbed across the environmental industry. The real questions remain: If AIG couldn’t be profitable in this space after collecting 30 years of actuarial data, what carrier might be next? And more importantly, when will the “musical chairs” stop and rates start to rise?

With all the headwinds in 2016, including a significant rise in claims across the industry with volumes of indoor air quality claims for mold, Legionella, and vapor intrusion, the market adapted extremely well. AIG’s exit will continue to play out in 2017, with the shakeout of the industry and with regard to whether current rates can produce profits and be sustainable. We predict profitability will be, in effect, postponed because there are simply too many players and thus, increased capacity.

We don’t anticipate dramatic rate increases. Therefore, we are confident that there will be continued growth with a soft market in 2017 for most classes or risks, except higher risks such as petrochemical, oil and gas, power and utility, and mining. There will also be some measured constraints for certain higher real estate risks such as hospitality, and indoor air quality, with the potential for higher retentions and coverage limitations.

The market today

- Highly competitive
- About 40 insurers

Market capacity

- More than $600 million and relentless growth. There are more new players, including some limited London market participation after decades of no interest. All signs point to more growth.
- Capacity varies by line and by industry segment. Tougher classes, such as energy, risks from downstream to upstream, and power and utility risks, may have significantly less capacity as the U.S. Environmental Protection Agency (EPA) increases its scrutiny of these industries’ effect on air and water quality.
- The #1 trend to watch is the skyrocketing number of claims. Claim frequency and severity continue to rise double digit year over year for insurers. All types of claims are occurring, but there is significant growth in indoor air quality issues, such as mold and Legionella in hospitality and real estate settings, as well as vapor intrusion claims (i.e., vapors from historical contaminants in the soil and groundwater entering buildings). There has also been a substantial increase in business interruption and extra expense claims.
- Transactional risks 10-year term policies for pollution legal liability are still available in the market for transactions, but only from certain insurers. There is more movement to align environmental insurance policies with representations and warranties coverage, which may include some limited environmental risk.
- “Excess of indemnity” deals, i.e., coverage written to backstop an environmental indemnity in the event it fails, are becoming more common.
- One-year policy terms are becoming the norm for difficult risks, such as day-to-day operations of energy, mining, petrochemical, power, and utility firms. These one-year terms will create volatility for these classes of business and increase the risk of gaps in coverage depending on timing of a loss.
- There is more global awareness of environmental liability, and the laws in other countries are becoming more stringent and more like those in the U.S. This is resulting in companies buying more global policies.
• With a booming construction marketplace, the demand for contractors’ pollution liability continues, making the marketplace highly competitive. Prices continue to drop with no floor.

• The marketplace is saturated with opportunities from a new and diverse set of prospective policyholders, as well as the replacement of policyholders from AIG’s exit. This translates into slower turnaround times for quotes.

• Coverage for complex mergers and acquisitions, contaminated properties, and Brownfield projects require more time in the market to carefully customize policies. Losses on policies written for redevelopments have caused insurers to become tougher on insurance terms regarding contamination. Policies can include many restrictions along with a push for short terms.

• EPA — new targets: Emerging chemicals and lower detection levels are creating new risks from perfluorooctanoic acid (PFOA) coating used in Teflon and carpeting, etc., to pharmaceuticals. Liability continues to become more stringent as science and technology advance.

**Forecast for 2017**

Rates will be fairly stable, but will vary by coverage line. We expect:

• Pollution legal liability: 5% decrease to 5% increase
• Contractors’ pollution: Flat to 10% decrease
• Combined general liability and pollution: Flat to 5% increase

**Topical issues**

**New threats:**

• Water quality: Lead in water, i.e., the Flint, Michigan water crises, and other high-profile industrial spills, show the vulnerability of water supplies and the significant financial and reputational consequences. Expect environmental justice cases to continue rising and our cities’ water treatment systems to be scrutinized.

• Environmental terrorism: This form of terrorism, including nuclear, chemical, radiological, and bioterrorism, is on the front burner for municipalities and other public entities.

• Emerging threats: Legionella has been a significant problem for some cities. Also, new bacteria, viruses, and brain-eating amoebas are causing stirs between what can be covered on environmental policies versus casualty coverages.

• Product pollution liability risks: These risks are coming into the forefront, especially higher risks that have big consequences if a product fails and causes personal injury to consumers or results in lawsuits. Marketplace and capacity are more limited. We expect to see a bigger push toward claims-made coverage for tougher chemical classes of product pollution.
Aviation

The buyer’s market continues in 2016 with declining rates and abundant capacity. Clients with favorable loss experience and growth potential should continue to enjoy the benefits of low premiums and broad coverage at high limits. This soft market continues to cast uncertainty on the long-term stability of the aviation insurance market. Experts have said for years that current market conditions with historically low premiums, rising claim costs, and high competition is unsustainable.

The market today

- The products and completed operations sector of the market has had a rougher year than in the recent past, with overcapacity putting pressure on premiums while new losses have amounted to a sizable total of more than $500 million.

- The airport sector, including air traffic control (ATC) risk, has seen falling premiums and high capacity.

- General aviation is still experiencing premium reductions and competition for market share. Premium reductions of 5% to 7% from policy expiration are often seen on businesses with low loss levels, strong management, and an established safety culture.

- The airline sector remains much the same as in 2015, with rate reductions for accounts that show fleet growth and strong safety programs.

- The war hull market has been a volatile sector since 2014, when the largest war hull loss since 2001 rocked the market. Despite predictions of a major market correction in 2015 to recover the loss, the market premium only went from around $65 million to around $80 million. Fortunately, the 2016 losses to date have been low, so the future looks brighter. However, several insurers withdrew from this market this year due to the lack of profitability.

- There has been an increase in M&A activity, with insurers believing the only way to make any profit is by merging with other companies and reducing staff costs. Even with these changes, it would take a large percentage of the market to withdraw before making any real difference in capacity. There doesn’t seem to be that drive at this time.

Market capacity

- Current capacity levels remain high and may be the single strongest contributor to market conditions. It is unlikely that there will be any price correction with the amount of capital and the number of markets available. There have been mergers between insurance carriers, and some syndicates have left the aviation market, but neither at a level that is powerful enough to change market conditions.

Topical issues

- Carriers continue to compete for market share and will aggressively pursue clients in most lines of aviation that have favorable loss history, good safety programs with solid management philosophies, and growth potential. In some cases, the underwriter’s desire to keep market share drives the renewal premium of some business, rather than true risk underwriting.

- Underwriters’ talk of increasing rates to offset losses in prior years has been reduced to a whisper, and rate hikes do not appear to be on the horizon unless there is a dramatic event in the fourth quarter of 2016.

- The opportunity presented by unmanned aircraft systems (UAS) in aviation insurance continues to be a vast unknown that presents excitement, new product development, and a changing underwriting mentality. The Federal Aviation Administration (FAA) estimates that approximately 2.5 million UAS will be sold this year, with almost 600,000 used for commercial purposes. With widespread use potential, industries such as industrial inspection, agriculture, real estate, aerial photography, government, and others are investing considerable amounts of money into this emerging industry.

- With fourth-quarter large renewals just completed in London, if the results are similar to the large renewals earlier this year, premiums will be even or slightly lower than current rates. The hope that 2016 would be a year of premium increases and stronger underwriting is not going to be realized if the current trend holds.
• Large losses with many fatalities have been limited to two in 2016. FlyDubai’s crash in Rostov, Russia, in poor weather conditions (March 2016) resulted in 62 fatalities, and Egypt Air’s A320 crash into the Mediterranean Sea (May 2016) resulted in 66 fatalities. There has been a steady trickle of smaller claims as well. At the end of July, the combined 2016 hull and liability loss figure was around $300 million. This is much lower than 2014 and 2015 figures at this same point in time.

Forecast for 2017

• Orders for new aircraft and increased passenger numbers for both airlines and charter operators paint a promising picture for the near future of air travel.

• UAS will be the most dynamic growth sector within aviation, but with small premiums for most of these units, the effect on the aviation insurance market with respect to premium contribution is unknown. Continued Federal Aviation Administration (FAA) involvement and rulemaking will iron out the operating standards and help determine how to safely integrate UAS into the national airspace. Underwriting companies will continue to assimilate policies to cover risks, pricing structures, limits, and operating requirements.

• With all factors considered, the forecast for 2017 has a familiar ring to the forecasts for recent years past. Lower premiums and continued high capacity will work to the buyer’s favor.

Following a steady flight path – good news for the buyer, but at what cost to the insurer?

Sources:
1 Source for UAS sales info: http://www.faa.gov/data_research/aviation/aerospace_forecasts/media/FY2016-36_FAAN_Aerospace_Forecast.pdf
4 Source for hull and liability loss figure: https://www.jltspecialty.com/~media/files/sites/specialty/insights-plane-talking/jlt_sp_plane_talking_july.pdf?la=en-gb
Public company directors’ and officers’ liability

The buyer’s market continues. Coverage and pricing economics continue to improve in meaningful ways for buyers, as market capacity remains abundant and competition remains strong.

The market today

Pricing: In general, a 5% to 10% price decrease appears to be the baseline. Greater decreases are observed for particularly favored risks and for those where historical pricing offers greater capacity for reduction. We expect premium increases for challenged risks.

Retentions: Retentions remain fairly stable. However, markets have used competitive retention options as a means to differentiate their offerings. The use of separate M&A retentions appears to have abated.

Terms and conditions: The market continues to provide coverage improvement, either as part of a self-generated offering or in response to broker-initiated requests. Overall, market behavior shows a significant level of cooperation to accommodate coverage requests, which continues to drive coverage expansion.

Excess capacity and Side A: Competition and pricing softness remain solid. However, some market resistance is observed due to the longer-term continued erosion of minimum pricing levels that has taken place in recent years.

Market capacity

Public company directors’ and officers’ liability capacity exceeds $1.5 billion and surpasses client demand.

While recent industry consolidation has occurred (ACE/Chubb, XL/Catlin, and Tokio Marine/HCC), this has not resulted in disruption to either capacity or competition.

Primary carrier options are increasing, with established markets seeking to move from excess to primary roles. Excess capacity continues to expand with the entrance of new capacity, Sompo Canopius.

Topical issues

Securities class-action filings have been increasing. For the first half of 2016, the number of securities class action filings increased relative to historical norms and the prior-year same period, yet remain below pre-financial crisis levels. In addition, the percentage of U.S. listed firms subject to securities class action filing has outpaced historical norms. At the current pace, the annual percentage of U.S. listed firms that are subject to securities class actions could be double the historic annual rate.

M&A related (merger objection) filings have declined substantially since the Delaware Chancery Court’s rejection of “disclosure-only” settlements in the “Trulia” case.

Regulatory enforcement activity has increased. The “Yates Memo,” issued at the end of 2015, sets forth a clear focus of the U.S. Department of Justice (DOJ) in investigating and prosecuting individuals for corporate wrongdoing.

Cyber security and disclosure continue to draw attention in board rooms as well at the Securities and Exchange Commission (SEC). SEC enforcement actions relative to cyber disclosure may be forthcoming.

For firms with international exposure, appropriate international coverage is increasingly a major topic. Globally compliant programs are being implemented on a more widespread basis.

In addition to a continued focus on improved coverage, clients are increasingly evaluating and assessing evolving coverages in entity investigation inclusive of Foreign Corrupt Practices Act (FCPA) exposure.

Forecast for 2017

The present market conditions are expected to continue into 2017. Without a significant disruption, the markets will continue to seek to protect share and to achieve growth by competing aggressively on opportunities.

There is no time like the present. There is great opportunity to efficiently augment programs, add to, or improve coverage in substantial ways.
Fiduciary liability

The fiduciary liability market today continues to be competitive based on abundant capacity, but insurers are evaluating the effect of excessive fee litigation on their book of business.

The market today

- Rates remain relatively stable in 2016, although expect a more thorough underwriting review on upcoming renewals.
- Based on recent cases filed, there is additional scrutiny on higher education industry risks; insurers may look to manage capacity and retentions on these programs.

Market capacity

- Capacity continues to drive the market.
- Newer players, Allianz and QBE, provided additional capacity in 2016; expect this to continue into 2017.
- ACE’s acquisition of Chubb has not adversely affected overall capacity for this line of coverage.
- While significant overall limits are available, we may see some insurers less inclined to provide large limits on any one risk.

Topical issues

Underwriters are concerned with trends in:

- Excessive fee cases: Insurers are seeking additional underwriting information regarding the insured’s procedures and oversight of plan service providers, benchmarking of fees, and performance of investment options, especially for plans with significant assets.
- Recent litigation against 403(b) plans in the higher education sector: The initial focus of the lawsuits was directed against large universities; some expect we may see suits against other smaller colleges and universities.
- Litigation in the asset management space with regard to plan investments in proprietary funds is also an area of underwriting focus. We may begin to see insurers look to restrict or manage limits offered and increase retention levels for this class of risk.

Forecast for 2017

- Expect rates to range between 5% decreases and 5% increases on average, depending on total plan asset value and overall changes in exposure, with more scrutiny on the larger plans.
- Look for rate increases of less than 5% for risks with significant plan assets and growth, adverse loss history, or other underwriting concerns.
- Insurers may also focus on retentions and may move to increase retentions based on overall risk profile.
- Although there is significant capacity in the mix and underwriters are keen on maintaining their existing clients while growing new business, there should be an interesting dynamic as insurers evaluate rates.

While there is ample capacity for this line, the litigation landscape may begin to change the underwriter’s appetite.
Private/non-profit management liability

In 2016, we saw the merger of two of the largest providers of executive liability to private companies and nonprofit organizations. Any fears over a reduction in capacity were quickly allayed, as the newly combined Chubb fought to retain and grow its market share. A few carriers were finalizing their efforts to re-underwrite their book with an eye toward profitability, and struggled with account retention. Despite the uncertainty, we have seen the marketplace continue to be competitive.

The market today

Underwriters continue to take a differentiated approach to submissions to provide attractive pricing and coverage terms for companies with strong risk profiles. With a continued strengthening of the economy, business bankruptcy filings (a key risk for private directors’ and officers’ claims) have been relatively flat from 2015. Many companies are reaping the benefits of strong balance sheets and overall growth as they renew their management liability policies. Certain industries, including healthcare, pharmaceuticals, retail, and hospitality, continue to see higher claims activity, resulting in a more challenging underwriting environment.

Market capacity

- There are a large number of financially sound carriers with an appetite for private and nonprofit business.

- Overall capacity remains plentiful, although carriers continue to manage limit and retention structures on any given program.

Topical issues

- M&A activity continues to be a leading indicator for claims, prompting many companies to explore transactional products (reps and warranties policies) to transfer risk.

- Impostor fraud remains a significant concern with severity of losses rising as fraudsters use increasingly sophisticated tactics against corporate victims.

- With respect to employment practices issues, the market is closely watching how changes to U.S. Department of Labor overtime rules and Employment Information Report (EEO-1) reporting may affect claim trends.

- Increasing frequency of claims related to the ADA Title III continues to be concerning, particularly for certain jurisdictions (California and Florida).

Forecast for 2017

- During the latter half of 2016, we saw signs of more softening in the marketplace. Barring significant macroeconomic changes or other external factors, we predict more insureds will see some pricing reductions in 2017.

- Carriers are working to differentiate themselves through coverage terms, offering enhancements and coverage extensions, rather than competing solely on premium.
Employment practices liability

The wave of layoffs and workforce reductions as a result of the economic downturn beginning in 2008 has subsided, but employment claims have not. For fiscal year 2015, the Equal Employment Opportunity Commission (EEOC) had 89,385 total charges filed against organizations with more than $525 million in monetary benefits paid.1 While this is down from the record-high of 99,947 charges filed in 2011, the organization has averaged 90,630 filings in the past three years.1 No employer is immune. If you have employees, you have risk.

The market today

- Market continues to be stable.
- Problematic states are California, New York, Texas, Alabama, Georgia, Florida, New Mexico, and Nevada.
- In California, most carriers are looking for separate and higher retentions.
- Fair Labor Standard Act (FLSA) claims continue to be problematic, as most of them have class- or mass-action status. A limited number of carriers are willing to offer a small defense costs only sublimit (i.e., $100,000).
- Top three classes of charges are race, retaliation (all statutes), and retaliation (Title VII only).

Market capacity

- There is plenty of market capacity.
- Preferred classes of business are small private and nonprofit organizations. These entities usually have more favorable retention levels.
- Organizations that have highly compensated employees (i.e., healthcare, financial institutions) tend to carry higher retentions and premium.
- Monoline FLSA policies are available.
- Carriers try to innovate to capture market share.

Topical issues

- FLSA claims
- EEOC’s substantive area priorities for fiscal years 2017 – 2021
- Eliminating barriers in recruitment and hiring
- Protecting vulnerable workers, including immigrant and migrant workers, and underserved communities from discrimination
- Addressing selected emerging and developing issues
- Ensuring equal pay protections for all workers
- Preserving access to the legal system
- Preventing systemic harassment
- Racial equality

Forecast for 2017

- EEOC has released its five-year plan, and has no plans to let up on enforcement.
- Choice of counsel is critical and should be negotiated at the time of the renewal, not mid-term.
- Timely notification of claims is critical.
- The market remains flat.

1 Source for statistics: https://www.eeoc.gov/
Crime

Little has changed for the crime insurance market, with the exception of all things related to impostor fraud. Impostor fraud coverage is no longer new, but interest from both the underwriting and brokerage communities — as well as from organizations that might benefit from this insurance — continues to grow.

Insurance companies are more receptive to offering higher limits of coverage for impostor fraud, as long as underwriters are comfortable with the controls in place. Coverage terms and conditions are also improving, as more carriers begin to eliminate their ominous call-back verification requirements.

The market today

- There is a relatively flat and stable rate environment.
- Competition among insurance companies promotes rate stability.
- Employee dishonesty (fictitious vendor schemes and payroll fraud in particular) continues to be the largest source of claims.
- Smaller (often less sophisticated) companies are experiencing greater crime losses than larger companies.

Market capacity

- Capacity is abundant for “traditional” crime products.
- Some insurance companies continue to offer multiple-year policies for mid-sized and smaller risks with favorable loss histories.
- Coverage for claims arising out of employee theft of client property has become easier to procure, even for more difficult-to-place industry classes.
- As an attachment to a crime insurance policy, modest limits of coverage for impostor fraud are readily available. Additional premium may apply depending on the carrier and coverage limit.
- The impostor fraud market is evolving swiftly. The application process, when required, is less cumbersome. Some insurance companies are removing their call-back verification requirements as a condition precedent to providing coverage, in turn making placing this coverage much simpler.
- Monoline coverage for impostor fraud remains unavailable in the market.

Topical issues

- Impostor fraud: Introduced in 2014, coverage for impostor fraud garners tremendous attention and dominates most discussions involving crime insurance, especially during the renewal cycle. Upon inquiry, we find that most organizations have experienced multiple attempts against them by fraudsters who perpetrate these types of crimes. Today, more companies demonstrate a general awareness of fraudulent payment instruction and false pretense schemes, and have avoided costly mistakes.
- Virtual currencies: The domestic crime insurance market continues to grapple with an effective method to address the theft of virtual currencies, given questions about their valuation and security.
- Contractual requirements: Organizations entering into business relationships with one another should expect to see contracts requiring more robust crime insurance programs than in prior years.
- Loss-discovered versus loss-sustained coverage: While crime coverage has migrated toward a “loss-discovered” culture, underwriters continue to scrutinize the risk of providing loss-discovered coverage to organizations that historically had purchased “loss-sustained” products. Depending on the size of the insured organization and the scope of the coverage sought, underwriters will be more judicious about offering loss-discovered policy forms.
Forecast for 2017

- There will be a continued focus on underwriting. Coverage for certain exposures (such as impostor fraud) will impose new burdens on organizations to evaluate their policies and procedures.

- A significant demand for higher limits and more robust coverage limits associated with impostor fraud exists and will continue to grow. It remains to be seen whether stand-alone coverage will become available either domestically or through the London marketplace.

- For most carriers, rate activity will remain relatively flat, determined more by exposure changes within the client's own risk profile (i.e., increases in revenues or employees and claim activity).

The impostor fraud market is evolving swiftly as insured organizations demonstrate greater awareness of fraudulent inducement schemes.
Medical malpractice

In 2017, we anticipate medical malpractice rates and premiums to remain competitive. In the past decade, medical malpractice insurance rates have been declining while industry profits remain historically high. Despite a slight increase in claims frequency and indemnity severity, insurers’ return on investments is favorable.

The market today

Medical professional liability insurance (MPLI) net-written-premium volume for the U.S. P&C industry fell for the 11th consecutive year in 2015. Financial results for year-end 2015 provide some evidence that the profitability levels experienced by medical professional liability writers in recent years could be waning. Profits remain high; however, the trend is negative.

The industry combined ratio remains below 100%, which represents a trend of deteriorating performance during the past six years. MPLI loss ratios on an accident-year basis have climbed recently due more to price deterioration than adverse claims trends. Calendar-year results in MPLI continue to benefit from substantial favorable loss reserve development that averaged 22% of annual earned premiums for the past eight years. This level of favorable development is anticipated to diminish due to recent accident years, which account for the largest proportion of all MPLI reserves, and which are experiencing a materially higher level of development relative to past years.

Medical professional liability financial results for 2015 were similar to those in 2014. Results for 2016 are not yet available.

Market capacity

During 2016, capacity remained abundant. The loss of market share medical professional liability insurers experienced is a direct result of physicians being employed directly by hospitals and large-system acquisitions of community hospitals, standalone outpatient facilities, and urgent care clinics. All of these groups are unable to realize positive financial outcomes as a result of decreasing inpatient days, combined with changes in Medicare and Medicaid reimbursements.

Many physician medical professional liability insurers expanded their appetites and are issuing policies to healthcare facilities and systems. Meanwhile, hospital professional liability insurers expanded their appetites to include ancillary products, which provide insurance for emerging risks associated with accountable care organizations. There is a reemergence of the need for provider stop loss caused by healthcare reform. These factors, combined with the entrants of new insurers and reinsurers, continue to keep the market competitive for healthcare facilities and providers.

Market consolidation by acquisition continues and is likely to continue: e.g. Med Pro bought MLMIC, ACE bought Chubb, and Coverys acquired a minority state in Strategic Risk Solutions in 2016.

The reinsurance market has been favorable; the flow of capital remains strong.

Healthcare providers continue to move from independent and smaller group practices toward direct employment with hospitals and large medical groups. This shift is changing purchase and coverage preferences for MPLI. Large groups are more likely to self-insure and use captive or alternative-risk programs, reducing demand for primary MPLI coverage.

There has been continued growth of captives and risk retention groups (RRGs) in the healthcare sector in 2016. Many offshore healthcare captives have domesticated to U.S. domiciles.
Topical issues

- Emerging risk for medical professional liability
- Medical professional liability systemic risk and batch claims
- The plaintiff’s bar has become more aware of these types of claims. Plaintiff’s attorneys have a greater return on batch claims versus individual medical professional liability claims. The allegations paint a picture of hospital and medical providers being highly focused on profits versus patient care.
- Some examples include, but are not limited to:
  - Unnecessary stents, surgeries
  - MRSA, Hepatitis C, compounding pharmacy, and fungal meningitis
- Carriers reporting increased frequency of these claims in 2015 and 2016

Forecast for 2017

We continue to experience additional capacity in this space. The extent of the change and when it will take place are unknown. Most insurers and reinsurers believe there will be no significant changes in 2017. In the past, the market cycle has historically been 20 years. We are fast approaching the 20-year mark. It is prudent for providers within the healthcare industry to begin preparing for a change.

A.M. Best: “… the medical professional liability sector is stable …”
Kidnap, ransom and extortion

Rates continue to remain competitive due to an abundance of capacity and market competition. Clients will benefit from premium stability and enhanced coverage offerings.

The market today

Key insurers remain committed to kidnap, ransom, and extortion (KRE) insurance and continue to focus on expanding the breadth of coverage under their respective policies. Insurers, including Hiscox, HCC, AIG, Chubb, Liberty, Starr, Travelers, and XL, are introducing enhancement endorsements and new policy forms as a means to remain competitive and relevant in the evolving world of KRE.

Market capacity

There is no foreseeable abatement to overall market capacity as key insurers have both the capacity and appetite to routinely offer limits of $10 million to $25 million.

Topical issues

KRE insurance policies are viewed as indispensable for organizations with international travel exposure. Problematic countries such as Mexico, India, Pakistan, Iraq, Nigeria, Libya, Afghanistan, Sudan, and Lebanon are still reason for concern. The crisis management firm Olive Group, as of Q2 2016, listed their top 10 countries for kidnapping foreign citizens as:

- Libya
- Nigeria
- Philippines
- Mexico
- Madagascar
- Mali
- Angola
- Turkey
- Afghanistan
- Venezuela

Similarly, during the past 20 months, the Olive Group noted that Africa accounted for more than 60% of the kidnappings of foreign nationals.

Political instability and unrest are leading to an explosive growth in kidnapping incidents — and ransom money is often used by kidnappers as a method to fund militant and fundamental agendas. According the U.S. Department of Treasury’s National Terrorist Financing Assessment report, the U.S. government estimates that terrorist organizations collected approximately $120 million in ransom payments between 2005 and 2012. In 2014 alone, ISIL acquired ahs as much as $45 million from ransom payments. Kidnap for ransom has become one of the most frequent and profitable sources of terrorist financing.

While international travel is an obvious concern and cornerstone of KRE insurance, it is also important to consider KRE exposures that exist in the U.S. According to NYA International, there were 54 high-profile kidnap incidents in the U.S. during the first three quarters of the past year. These incidents included virtual kidnappings, express kidnappings, tiger kidnappings, and other kidnap-for-ransom and abduction incidents. More than 20% of these victims were under the age of 18, and students are often the target of express kidnapping.

Emerging risks make it necessary for clients to consider coverage extensions for allied KRE risks that transcend country borders. For example, cyber-extortion continues to be a prevalent threat for most organizations. Accordingly, many KRE insurers provide some degree of coverage to address this exposure. It is also important that clients coordinate the coverage granted under a KRE insurance policy with their cyber and network security and privacy insurance.
Workplace violence incidents continue to increase, and incidents of an “active shooter” are widely publicized in the media. According to the FBI, active shooter incidents in 2014–2015 resulted in 92 deaths and 139 injuries. It is highly recommended that organizations assess their exposures and take proactive measures to address and mitigate this risk. Under the Occupational Safety and Health Act (OSHA) of 1970, the courts have interpreted OSHA’s general duty clause to place a legal obligation on an employer to provide a workplace safe from known hazards that cause or are likely to cause death or serious physical harm to employees. Clients should consider a workplace violence extension under a KRE policy or an employment practices liability insurance policy, or possibly a dedicated active shooter insurance policy.

Forecast for 2017

- Competition among insurers remains robust and will continue to keep rates and pricing aggressive. We expect this trend to continue during 2017, resulting in pricing that is flat to down 5% to 10%.

- Clients should consider deploying premium savings toward increased insurance limits and broader coverage enhancements — such as workplace violence coverage, assault coverage, and enhanced cyber extortion — as well as proactively engage crisis management firms to assist with planning and development of crisis management plans.

- Clients should regularly review and audit their crisis management and incident response plans to ensure they remain relevant and appropriate to address evolving risks.

- Insurance brokers should seek to coordinate clients’ KRE, cyber, general liability, and crime insurance programs to ensure a coordinated, thoughtful approach to the evolving risks clients face today.

- As always, review of a client’s global footprint in relation to that of its crisis response firm continues to be material to the decision-making process.

Clients will benefit from premium stability and enhanced coverage offerings.

1 Global Kidnap for Ransom Insight Report, Olive Group, September 2016
3 NYA International Crisis Prevention and Response, Q1-Q3 2016
5 https://www.osha.gov/SLTC/workplaceviolence/standards.html
Representations and warranties

M&A activity for 2016 is off roughly 10% from record 2015 levels. Despite the drop in transactions, the awareness of and take-up rate for representations and warranties (R&W) insurance continues to increase. R&W insurance is typically purchased for transactions ranging from $50 million to $2 billion. We estimate that 25% to 30% of the transactions completed in 2016 have an accompanying R&W insurance policy.

The market today

- Purchasing levels are increasing despite a smaller number of transactions closing in 2016.
- Most insurers are citing growth rates in the 25% to 50% range.
- The number of primary insurers writing U.S. domestic transactions is nearly 20, up from 10 in 2015.
- Influx of capacity has led to price drifting 5% to 10% lower from 2015 levels.
- Newer insurers have helped create more interest in smaller deals ($25 million to $50 million).

Market capacity

- Capacity is up roughly 50% from 2015 levels.
- Most insurers have at least $25 million in capacity and a handful can provide $50 million to $100 million lines.
- We expect additional carriers to join the market in 2017.

Topical issues

- Continued push for lower self-insured retention levels (1% of transaction value and purchase price); more common now.
- Indemnification and escrow amounts posted and agreed by sellers continue to decrease.
- Healthcare and financial services-related acquisitions remain challenging.

- Favorable treatment of multiplied-damages language remains available from most insurers.
- The diligence process is becoming increasingly focused on labor and employment benefits elements relative to FLSA, wage and hour, and treatment of independent contractors versus people with employee status.

Forecast for 2017

- Expecting continued increases in:
  - Number of insurers in the market
  - Capacity (new and growth from existing insurers)
  - Percentage of transactions that have R&W insurance
- Expect broad terms to remain readily available with a continuing trend toward fewer deal-related exclusions

R&W insurance is most typically purchased for transactions ranging from $50 million to $2 billion. We estimate that 25% to 30% of the transactions completed in 2016 have an accompanying R&W insurance policy.
Technology and professional errors and omissions

The market for professional liability for technology and other professional service firms has been stable for some time due to the lack of catastrophic claims settlements and judgments.

The market today

- The rate for this coverage remains stable, and strong brokers remain capable of securing material coverage enhancements to already strongly enhanced programs.
- Risks that present with class action exposure (business to consumer) or have large volumes of personally identifiable information in their care, custody, or control may be underwritten more heavily. But rates in this class have stabilized.
- There are still certain coverage areas that carriers are reluctant to write — cost of corrections, first-party recall, and Telephone Consumer Protection Act (TCPA) coverage are strong examples.

Market capacity

- We have seen a slight increase in capacity as new carriers are entering the space.
- Additionally, strong lead carriers are looking to pool their capacity with reinsurers to put up large blocks of capacity ($50 million to $100 million) for risks that are purchasing high limits.
- There are many carriers offering capacity in this space, but fewer are offering primary forms that offer the breadth and depth of coverage a complex client would require.

Topical issues

- Aggregation remains a concern for carriers, as a single data privacy event could result in multiple claims reported to the same insurance companies.
- We are seeing an increase in TCPA-related claims, and the majority of carriers remain reluctant to offer a small sublimit, although we suspect that we will see more capacity in the future.
- Contract negotiations in the areas of limitations of liability and insurance-specific wording are becoming more complex and detailed.

Forecast for 2017

- We expect market capacity to remain stable. We have seen one or two new markets enter and are not expecting any to depart.
- Underwriters are beginning to offer slight reductions in rate to insureds that are free of claims. We expect this trend to continue and for rate reductions to continue as we move further from large litigation and data privacy incidents. A large data privacy breach would put an immediate halt to any premium and rate reductions to risks with class-action exposure, or for risks that collect, store, or control large volumes of personally identifiable or confidential information.
- Carriers will continue their innovation on capacity maximization as it creates a cleaner and more streamlined program for larger, complex risks. It also assists in the claims process should there be a large loss.
- Innovation in network-based business interruption will continue to occur as the gap between property and professional liability policies needs to be addressed.

Rates are declining for the first time in many years due to the lack of complex litigation in the past year.
Network security and privacy risk (cyber)

While there have been few large data privacy incidents during the past year, the issue remains at the board level and top-of-mind for leaders in the risk space. Everyone is looking for a way to prevent an event from happening and to properly manage an event if one should occur.

The market today

- The lack of headline-grabbing data privacy breaches in the past year has allowed for more flexibility in pricing, terms, and conditions.
- Carrier innovation has slowed down, but we are seeing “value-add” services offered more readily. These services can include a table-top exercise of an organization’s incident response plan or assistance developing an incident-response plan if an organization doesn’t have one.

Market capacity

- We have seen a slight increase in capacity as new carriers enter the space. However, the new carriers are staying in the excess realm area for now (attaching at $10 million or higher).
- There are many carriers offering capacity in this space, but fewer are offering primary forms with the breadth and depth of coverage a complex client would require.

Topical issues

- Number of records that an insured has in its care, custody, or control has become a “standard” request from carriers, as these are now a key piece of the underwriting puzzle.
- Organizations outside of the traditional buyers (manufacturing, for example) are adding network security and privacy to their insurance arsenal as they realize the risk inherent in their collection of employee records.
- Payment card industry (PCI) compliance remains an issue, and some carriers are focused on Europay, MasterCard, and Visa (EMV) compliance. Others are more concerned with point-to-point encryption.

Forecast for 2017

- We expect market capacity to remain stable at $250 million to $300 million.
- Underwriters are beginning to offer slight reductions in rates to insureds that demonstrate strong controls around data protection.
- Carriers will continue their innovation value-add and loss-control services, as these are enticing to new buyers and improves the risk profile of their insureds.
- Innovation in network-based business interruption will continue to occur as the gap between property and cyber liability policies needs to be addressed.
- Carriers will either look to outside information technology (IT) experts or hire IT professionals to assist in the underwriting of these risks — as the complexity of the underwriting process has changed significantly in recent years.

Rates are declining for the first time in many years due to the lack of large data privacy events in the past year.
Commercial surety

The commercial surety market remains soft. Pricing has stabilized while capacity is still strong, despite recent claims results. A shortage of underwriting talent and continuity planning on the broker side is a growing concern.

The market today

- Surety year-end results from 2015 (released October 2016) indicate commercial surety direct written premium is approximately $1.69 billion and is estimated to comprise 35% of all surety premium.
- The commercial surety loss ratio fell from 2.9% to 1.8% in 2014 and 2015 respectively.
- While consolidation of a few carriers has occurred, there is still an abundance of capacity, creating new opportunities, particularly with third-party contracts and international opportunities.
- Talent management is becoming more difficult, as there is a shortage of talent in the marketplace.
- There is still an abundance of carriers and too much competition in the market, affecting overall profitability.
- Pricing is still trending consistently or, in some cases, is lower than letter of credit costs.
- Larger carriers continue to focus their growth on expanding middle-market opportunities, as well as improving their international footprints.
- The oil and gas and coal mining industry segments are being monitored carefully.

Market capacity

- The number of new carriers entering the marketplace has stabilized.
- Capacity is not an issue and exceeds client demand.
- We have seen cases where capacity can be extended in excess of $1 billion, primarily with the top five carriers: Travelers, Zurich Liberty, CNA, and Chubb.

Topical issues

- Some clients are concerned that they might start to see a slight uptick in pricing.
- M&A activity has been on the rise, causing consolidation among clients, and increasing competition.
- With a large percentage of retirements looming in the next one to five years, the acquisition and shortage of seasoned surety talent is an industry-wide concern.
- Carriers and brokers will continue to look for more efficient ways of handling the business.
- The importance of creating efficiencies through technology solutions is a focus for carriers, brokers, and their clients.

Forecast for 2017

- There are concerns that the political environment could affect the surety industry, leading to changes in regulation. A shortage of talent will continue to stretch resources within the surety marketplace, affecting the ability to maintain underwriting discipline.
- The international surety market will continue to expand and see an increase in opportunities. While underwriting practices and standards have softened during the past several years, we see these stabilizing in 2017 due to some increased claims activity reported in late 2016.
- Rates will start to stabilize at their new low, with little or no increases likely.
- As baby boomers continue to retire, M&A activity among the surety industry client base will continue to increase as a means to improve growth and to acquire needed talent.

The acquisition and shortage of seasoned surety talent is an industry-wide concern.
Contract surety

The combined phenomena of excess market capacity and a declining demand for product are still present. However, signs indicate that the market is beginning to stabilize. In addition there has been a marked increase in new construction work.

The market still remains extremely soft and flexible.

The market today

- Total surety premiums remain at the $5 billion annual level for all surety, with an industry-wide total loss ratio of 20.2% as of December 31, 2015. Preliminary results as of June 30, 2016, show premium at $2.826 billion and a loss ratio of 18.1%.

- Overall results have been very good, and losses have been manageable.

- There are still a few new markets entering the surety marketplace. As a point of interest, these new players are traditional reinsurance companies testing the waters as primary surety providers. Time will tell whether they remain in the market for the long term.

- We are seeing contraction in the marketplace. First, a major contract surety provider exited the business as a major surety writer, and there may be one or two more exits in the next 12 to 18 months. Severity losses have been the catalyst for the exit.

- There has been some market consolidation in the form of M&As in 2016. With the exception of the one major acquisition (ACE and Chubb), the additional M&As have been in the smaller surety company area. Current market conditions make organic growth a major challenge, so acquisition of smaller entities and their books of business are an answer.

- The surety market remains stable and responsive to our clients’ needs.

- Major surety carriers with international capabilities look to the overseas market as a potential growth area. The surety product is being considered as a vital security alternative in certain countries.

Market capacity

- The contract surety marketplace continues to support the projects that are being bid.

- The total single job size available at this time is in the $3 billion range, usually with multiple principals and multiple surety carriers (Travelers, Liberty, CNA, Zurich, and Chubb). This is up from $1.5 billion a couple of years ago.

- Large and mega-contractors with aggregate work programs in excess of $250 million are capably handled by the contract surety marketplace.

- Middle market accounts are the most prized by all the surety carriers we have spoken to. Annual aggregate work programs in the $25 million to $150 million range are the most sought after.

- Small and emerging markets are still being serviced adequately by the surety market.

- The top 10 surety companies still write in excess of 64% of the surety premium charged.

- While market capacity remains strong and premium rates are stable, these factors could be subject to competitive pressures in the near future with the continued soft market.
Topical issues

- Recent developments in the subcontractor default insurance and subguard product marketplace are changing its dynamics. The premium charge is increasing, and the terms and conditions of claims-made policies are being tightened at renewal time.

- Recent adverse losses are the main reason for subguard/SDI changes. For a long time, there was only one carrier in this space. Now there are a total of four carriers providing this coverage — and the final effect has yet to be realized. The market does, however, seem to be in flux.

- A major new development in the surety market is public-private partnerships (PPP or P3 projects). In this scenario, the contractor designs, builds, finances, and operates the finished project until the financing has been paid back. The concept of PPPs was developed in Europe and has come to North America to stay.

Forecast for 2017

- There will be a sorting out of the marketplace in 2017. Limited premium dollars are being chased by numerous markets. There must be a change, as this is not sustainable.

- The advice to clients is to look at who is providing for your surety needs, how deep their field of expertise is, what their reputation for claims handling is, and how long they have been in business.

- The premium pressure is present, but the numbers are limited by the fact that premium rates are filed by state with little room for change; the alternative is for surety carriers to lower underwriting standards to generate premium dollars. This could potentially lead to additional claims activity.

- Surety carriers are recognizing the need to improve the claims handling provisions of the surety product. We see 2017 as being a new horizon in this area, with the potential to improve the manner and speed of a surety bond claim.

- The stimulus provided by the $1 trillion of new infrastructure work proposed by the president elect would be long anticipated relief to a long depressed contract surety industry. However, if surety bond waivers are considered for expediency or cost saving, taxpayer dollars could be put at serious risk. Also, the work needs to include projects across the board in size, and not just mega contracts, or the economic advantage would be lost.