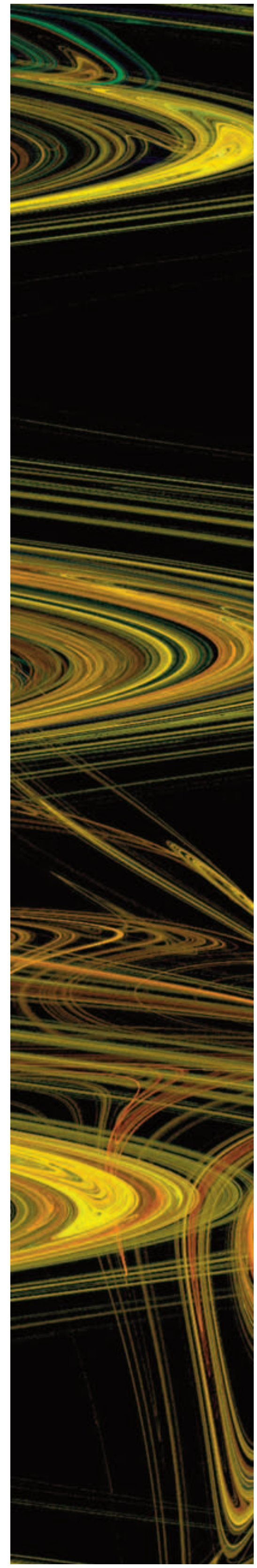
CASUALTY

UNANTICIPATED OPPORTUNITIES

So far, the much anticipated market shift of 2009 remains just that: anticipated.



In general, rates have remained relatively flat to slightly down across most classes of excess Casualty business, despite traditional industry signs of market hardening in 2008: major property losses, increasing combined ratios for most insurers, rating agency downgrades and reinsurance increases. Caveats exist for traditionally difficult classes of business, such as invasive medical products, pharmaceuticals, firearms, critical auto parts, etc. However, relatively flat premium has been the story even for accounts that have had losses pierce the umbrella layer or have reported poor or deteriorating financials. This is often the case even for those who enjoyed significant rate savings in recent years.

That said, flat premiums in the current economic landscape are not the same as flat premiums in a healthy economy. Decreased activity means decreased exposure. Flat premiums translate into rate increases for accounts with exposure decreases, while the opposite holds true for accounts with increasing exposure.

TERMS AND CONDITIONS

Coverage terms and conditions remain consistent with those of last year. Carriers continue to strive for the appropriate attachment point on underlying limits and will generally price risks accordingly. Gone are the days of umbrella/excess insurers attaching above primary programs that have insufficient limit from a per-occurrence standpoint, as they continue to underwrite accounts to a zero loss ratio. To obtain best-in-class terms, conditions and clauses, clients will need to demonstrate their risk management efforts, including quality control standards and other operational and management procedures employed to reduce risk through transfer, avoidance and mitigation.

RATES

While rate stabilization is apparent for accounts of all sizes, reductions and increases can be found in any given sector depending on the risk profile of the insured. Overall, abundant competition is putting a surprising amount of downward pressure on rates. Lower hazard classes with good loss experience and strong financial footing are highly sought after by insurers, driving rates down through sharp competition. Even higher hazard classes can see rate reductions if terms, conditions, underlying attachment points and basic risk management mitigation standards are appropriately set in place by insureds and incumbent insurers. This is thanks to lively competition among newer players, such as Torus, Canopius, ArgoRe and

Ironshore, and traditional markets, such as AIG and Ace. Further fueling this competition is the shifting risk appetite of existing markets, such as AWAC, Endurance and Zurich. Many accounts are looking to test the waters this year, encouraging some of the new entrants and veterans alike to provide options during the underwriting process. This helps keep rates and policy terms competitive.

CAPACITY

While capacity has increased since last fall, buyer appetite has changed. The name of the game this year for many buyers is diversification, as they are unwilling to place as much risk with one insurer as they have in the past. This will result in greater opportunity for the less dominant players who may have participated on a lead basis right through mid and high excess layers on many programs but have been pushed aside by large limit players who leveraged their marketplace muscle. It should be noted that while overall capacity may have increased, lead umbrella capacity remains very conservative for tougher classes and higher hazard risks, with still too few insurers competing for the business. The major players in this arena for the last decade have been American Home, Lexington and National Union – all divisions of AIG.

TERRORISM

Terrorism risk varies significantly from account to account, but for those who face the exposure, it remains a critical underwriting concern, as no insurers lead the pack in terms, conditions and rates. When applicable, traditional umbrella/excess Liability markets are looking to have this risk limited through utilization of the SAFETY Act (part of the Homeland Security Act of 2002), which allows insureds to carve out this exposure from their otherwise insured products or services. Terrorism exposure also reaches far beyond product liability, which is traditionally insured under an umbrella/excess Liability tower and remains a concern for insurers and insureds alike in connection with sporting venues, theaters, malls and other venues where people gather in large numbers.

TRENDS

Diversification of exposure through wider distribution of risk to more insurers seems to be the most notable trend in excess Casualty. Accounts historically have placed as much as $250 million in limits with one insurer on larger limit placements; however, we are now seeing more insurers with lesser limits on most placements. One of the main drivers is the concern buyers have with the financial positions of the sellers. Diversification spreads counterparty risk, and careful program structuring allows insureds to maintain limit continuity. Diversification also expands insurer relationships, offering opportunities for flexibility down the road. This trend has resulted in greater use of quota-share layers, as traditional stacking of limits, particularly on larger limit programs, can result in excessively thin pricing in the high excess and insufficient return on capital for insurers. Utilization of quota-share layers enables pricing models to decrease as the attachment increases, and yet it allows sufficient premium per million to attract the necessary capacity to meet the limit requirement.

Many markets are reconsidering their historical position in umbrella/excess Liability by participating on new layers (lead, mid or high), expanding into classes of business they have historically shied away from, and generally trying to increase market share. The marketplace today offers opportunities. We caution buyers to be mindful of the claims handling abilities, underwriting discipline, commitment to the market and financial strength of the carriers in this long-tail line of business. Diversify your program with a greater number of insurer participants, meet with the markets *early* and think long term.

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