BEST'S REVIEW
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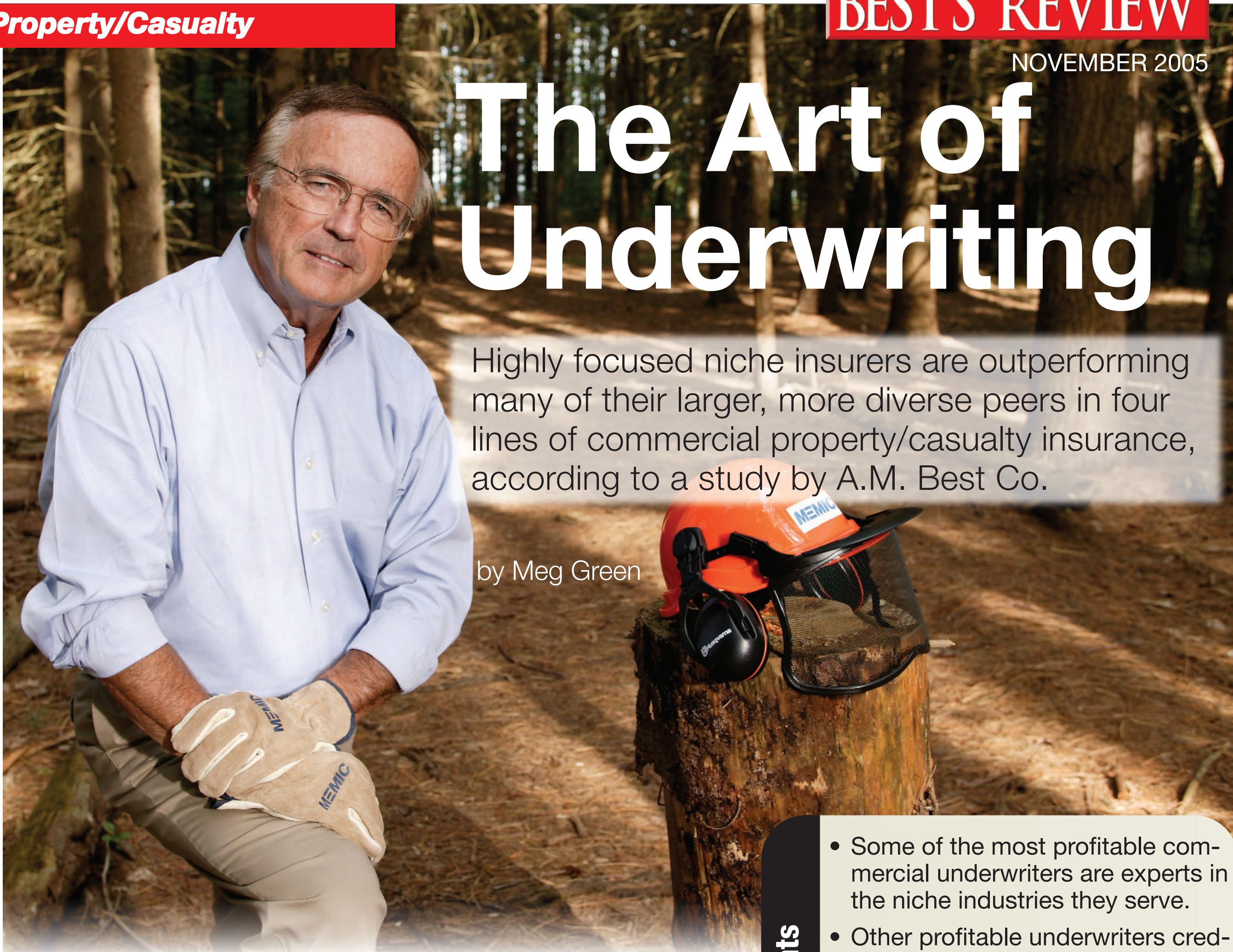
The Art of Underwriting

Highly focused niche insurers are outperforming many of their larger, more diverse peers in four lines of commercial property/casualty insurance, according to a study by A.M. Best Co.

by Meg Green



CUTTING LOSSES: John Leonard, president of Maine Employers' Mutual Insurance Co., attributes the company's low combined ratio to its focus on loss control. The company requires employers in the logging industry to send their employees to a 40-hour training course, which includes hands-on training on how to safely cut down and move trees. The company hasn't had a serious loss-time injury in the wood products area since 1996, a year after it launched the course.

Kevin Brusie for Best's Review

Key Points

- Some of the most profitable commercial underwriters are experts in the niche industries they serve.
- Other profitable underwriters credit their success to their loss-control efforts and their committment to safety programs.
- Others tout their efforts on claims and emphasize how important their claim managers and adjusters are.

When it comes to profitable underwriting, commercial property/casualty insurers that outperformed their peers tend to have a one-track mind.

A.M. Best Co. studied four lines of commercial insurance—workers' compensation, fidelity and surety, medical malpractice and commercial auto—and found those companies that rose to the top in underwriting profitability often did so with a sharp, laser-like focus on a particular area of expertise.

Insurance companies can make money two ways: first, through the actual business of insurance, and secondly, through investments. It's common for insurers to break even or even lose money on their main business, insurance, but still be profitable based on their revenue from investments.

One measure of business profitability is combined ratio, which reflects losses and expenses as a percentage of premiums. A combined ratio less than 100 marks a profit. Over 100 equals an underwriting loss. The study examined companies who derive more than 50% of their premiums from one of the selected lines of insurance, and ranked them by their 10-year combined ratio.

The smaller, niche superstar companies that scored the best use various techniques. Some emphasize underwriting and take special care before adding a new client to their roster. Others focus on preventing the loss before it happens, paying close attention to educating clients. Still others put their muscle into handling claims to keep costs down.

It's likely that most people have never heard of many of the companies that trumped the competition. For instance, Yel Co. Insurance, a Miami-based privately held company, provides commercial-auto liability insurance to two fleets of taxis in South Florida. Yel Co. paid out only 37 cents in claims and expenses for every $1 of premium it took in over a decade. The industry average for commercial auto was 107.25, meaning the average commercial auto writer paid out $1.07 in expenses and claims for every $1 of premium taken in over a decade.

Global Surety & Insurance Co., an Omaha, Neb., surety and fidelity company, could have one of the best

> "The combined ratio is truly the number an insurance company needs to focus on to measure their financial expertise."
>
> *—Gloria H. Everett, MedAmerica Mutual*

combined ratios of any company, anywhere: 6.36. That's not a typo. For every $1 of premium received, Global Surety only paid out 6.36 cents in claims, well below the industry average 10-year combined ratio of 98.23. True, Global Surety is a unique company in that it writes only contract surety business for its parent, construction contractor Kiewit Corp.

The results of both Yel Co. and Global Surety aren't typical, and neither is their business focus. Yet both demonstrate how knowing their business as an insider can help profitability. Both companies declined to be interviewed for this article, saying they're not looking for new business and don't want to share any of their secrets of success.

Other companies were proud to talk about their experience and how they overcame markets plagued by skyrocketing rates and shrinking availability. Several were forged in the fires of hard insurance markets, and ironically, have pulled ahead of their peers in terms of profitability, proving that what was once viewed as "too risky" by the general market can indeed be profitable—if insurers mind their business.

Focus, Focus, Focus

Companies can have an advantage by keeping a narrow focus, said Bruce D. Hale of Conning Research and Consulting Inc. "Sometimes you can have outstanding results because you have missed catastrophic weather. For instance, every personal and commercial insurer in Hawaii has made money hand over fist since Hurricane Iniki in 1992. A company focused on Hawaii would be great just because they haven't been hit," Hale said.

Companies also can excel if they take the time to really understand the risks.

MedAmerica Mutual Risk Retention Group, based in Walnut Creek, Calif., has a narrow focus that other insurers have shied away from: It provides medical malpractice insurance for emergency room doctors and nurses in California. It also whipped the competition, with a 10-year combined ratio of 89.9, the third lowest of any dedicated medical malpractice writer in the country. It's one of only four medical malpractice writers to turn an underwriting profit in the past 10 years.

"The combined ratio is truly the number an insurance company needs to focus on to measure their financial expertise," said Gloria H. Everett, MedAmerica chief executive officer. Like other profitable underwriters, MedAmerica is selective and doesn't take all applicants. "Before we will even issue a rate indication, not to mention a full quote, we ask what the company's motivation is in changing carriers. If they say price, it's a good indication that we aren't going to write it," she said.

MedAmerica emphasizes loss control and training, both for its staff and its insureds. The company sent its own staff to spend a day in an emergency room. "There's nothing more comforting to physicians than if you have an insurance person, or any service provider, really understand your business. That's what we have focused our energy on. We don't sit in an ivory tower and give advice that isn't appropriate to their business," Everett said.

For instance, after seeing a number of claims related to doctors having difficulty opening airways, the company developed a special kit with the tools needed for the task, and provided doctors with additional training.

MedAmerica could have expanded outside of its niche area of emergency care in California, but chose not to, Everett said. "We felt it wasn't our core competency. We weren't tempted. Working at a large company, one of the things I learned was that it's easy to get seduced by your own top line growth. Especially in med mal, we've seen a lot of top line growth that came back to bite us on the bottom line," she said.

See the Forest for the Trees

Maine Employers' Mutual Insurance Co. of Portland, Maine, is the workers' compensation insurer of last resort in the state. It was founded by the Maine government in 1993 when the state's workers' comp market was considered the worst in the nation. With forests covering 89% of the state, logging and forestry are major industries, and claims from those dangerous occupations were major contributors to the state's high loss ratio.

John Leonard, president and CEO since the company opened its doors, said MEMIC immediately focused on preventing losses from happening.

"The core operation is based around our commitment to workplace safety. We have nearly 40 certified safety professionals working in our territory on a daily basis," Leonard said. "We look more like a loss-control company than an insurance company."

Those safety professionals have all worked in the industries they now try to improve, he said. "For example, our construction industry safety professionals come out of that industry. They really understand and know the operations. They are not your traditional safety counselors with white shirts and clipboards," Leonard said.

Unlike other companies, MEMIC must take all comers. It doesn't have to keep all employers, however, and any who refuse to undergo MEMIC's safety training can be dropped. Even as the insurer of last resort, 65% of MEMIC's business stems from the voluntary market, and it writes about 70% of the commercial market in Maine, and expanded into New Hampshire in 2000.

MEMIC can tout its 89.7 combined ratio in the past 10 years as proof that its emphasis on loss prevention is paying off.

Don't Drop the Sandwich

Like MEMIC, Blood Centers Exchange, a risk retention group based in Overland Park, Kan., was formed in a hard market. It was the mid-1980s, and the blood-borne disease AIDS was making headlines nationwide. Insurers, fearful of the lawsuits related to the collection of blood, had second thoughts about providing liability coverage for blood collection centers.

"A lot of insurance companies said 'we're going to lose lots of money in claims, affecting financial results,'" said Alan Cable, chairman of the Blood Centers RRG. "Companies raised their rates, and stopped writing blood centers altogether. They thought the risk was too great."

The blood center where Cable worked saw its liability insurance rate jump about 350%. "Some blood centers even went without insurance. The bottom line is that those of us in the industry, we disagreed with the insurance companies. We don't think there's that much liability out there, knowing the business as we know it. In the end, we felt we should form our own insurance company," Cable said.

The RRG began doing business in 1993 by insuring 21 blood centers. It's since expanded to 43 blood centers, and has produced strong results. The RRG, with a 10-year combined ratio of 87.1, had the second best combined ratio of any dedicated medical malpractice writer in the country and has outperformed the medical malpractice industry, which had a combined ratio of 125.48 during that time. Remarkably, the Blood Centers Exchange has done that without a single employee. It relies on consultants to handle the insurance business, but is governed by its board of directors who are chosen from its member blood centers. Other blood center employees sit on committees to review everything from claims to underwriting, plus loss control and risk management.

"Everyone involved in the program is either from the blood industry or has been doing business with the blood industry for years," said Brad Ellis, who acts as manager of the RRG but works for the Haake Cos., a consulting firm. "The company has never needed to have its own employees. It may grow to the point where it decides to, but the committees within the company are very, very active."

For instance, an underwriting committee reviews all new applications from new blood centers who want to join the group.

"If the insured or potential insured has had regulatory shortcomings, we want to know how they've been dealt with. It's a highly regulated industry. We know what is expected of one another. If an applicant is having a problem with the FDA (U.S. Food and Drug Administration), we can see what the FDA has written them up for, and whether or not their response was adequate. We can encourage change, and if they choose to not adequately address the FDA's concerns, we may choose to no longer insure them," Cable said.

Ellis said: "If you really understand the industry, look at the claims experience of the applicant, and you'll have a good understanding as to whether the claims history will repeat itself."

The secret to making an underwriting profit is to know the industry, Cable said. "We are not trying to insure a risk that we do not fully understand," he said.

Also, Cable said it's important that the other insureds are equally committed to controlling claims.

"It's like when you are driving down the road, you will see people driving that you wouldn't want to share their liability for auto coverage. You see people whose lifestyle is a bit risky. We look at each other, the other insureds or applicants, and decide if we feel that they are going to do what they ought to do," Cable said. "We don't want them dropping their sandwich in the swimming pool we're sitting in."

"We keep very tight control, and relationships are very important to us."
—Sandy Kohl, Service Insurance Group

Don't Underestimate Relationships

Smaller, more focused companies also are able to develop strong relationships, which can be an added benefit, Hale of Conning said. "Insurance is a people business. Those with strong relationships can really stand out, whether the relationship is with a customer group or regulators," he said.

Service Insurance Group of Austin, Texas, is one such company. "We keep very tight control, and relationships are very important to us," said Sandy Kohl, senior vice president of underwriting for Service Insurance.

Throughout most of its history, the company has concentrated on writing workers' comp insurance only for Texas-based auto dealerships. It's branched out recently to cover mom-and-pop type operations in Texas, but has several sister companies all related to meeting the insurance needs—including credit life, accident and health, and service warranties—for auto dealerships in Texas.

The company has bested every other dedicated workers' comp writer in the country by having the lowest 10-year combined ratio: 84.7. So while the rest of the industry, on average, was paying out $1.10 for every premium dollar taken in, Service Insurance was paying only 84.7 cents on the dollar.

"Prior to taking the risk, as well as after we have the risk, we have a loss control department that visits the insured or prospective insureds. They know what types of exposures there are. In dealerships, for instance, they are looking at things on the floor, like oil, that can cause floors to be slippery. They look for safety measures:

Are mechanics using goggles? Back supports?" Kohl said.

Service Insurance has its own agents that sell directly to dealerships and also uses independent agents. It frequently meets with both types of agents to discuss business. Also, the loss-control department is frequently talking to the underwriters.

"The success is all of the departments working together and closely, and establishing a relationship with insureds and agents," Kohl said. Being small helps, she said. "I think the larger you become, the less relationship building you can do," she said.

Strong Leaders Show the Way

In addition to strong relationships, smaller companies can excel due to excellent management, Hale said. "The power or the value of a strong leader makes a highly concentrated impact in a smaller company, as compared to being watered down through various layers at a larger company," he said.

That could be the case with Charter Insurance Group, which writes business only in Massachusetts, a state with a tough regulatory environment. With a combined ratio of 86.5, the Boston-based company is the second most profitable workers' compensation underwriter, behind Service Insurance, for the past 10 years.

Linda J. Sallop, president of the company, and Mitchel I. Weisman, executive vice president, personally review just about every application and claim that come in the door.

Other companies may put the spotlight on their sales and marketing teams, but not Charter Insurance. "Other companies put their claims people in the basement, where there are no windows, nothing but files. Our claims department has the most beautiful space here," Sallop said.

Sallop and Weisman credit their employees with their success. "I think each and every individual here feels vested in what they do. They feel the results are in some way directly related to their performance," Weisman said.

"The state rates are below what they were in the 1980s," Sallop said. "The rates technically are very inadequate. When the rates go down, our competition lays off people. We invest more in them. We pay our people more than the average insurance company, in addition to other rewards."

For instance, the company caters hot lunches for its employees daily, and offers other perks, such as company dinners and a chance to work from home.

Learn More

Charter Insurance Group
A.M. Best Company # 18396
Distribution: Independent Agents

Community Blood Centers Exchange
A.M. Best Company # 11569
Distribution: Direct

Maine Employers' Mutual Insurance Co.
A.M. Best Company # 11387
Distribution: Independent Agents

MedAmerica Mutual Risk Retention Group
A.M. Best Company # 11431
Distribution: Direct and Brokers

Service Insurance Group
A.M. Best Company # 18385
Distribution: Direct and Independent Agents

For ratings and other financial strength information about these companies, visit *www.ambest.com.*

Maintaining relationships with clients also is important. Adjusters are assigned specific employers, and then handle every claim that comes from that employer. "Our adjusters do not sit at a desk waiting for claims to come in. They meet our accounts face-to-face, and establish the rapport we need to keep the employer doing business with us," Weisman said. BR

Willard Reed and Henry Kane compiled data for this article from the A.M. Best Co. database.

Top Performing Underwriters Among Companies That Derive 50% or More of Their Premiums From Each Specific Line

Medical Malpractice

Ranked by 10-year combined ratio

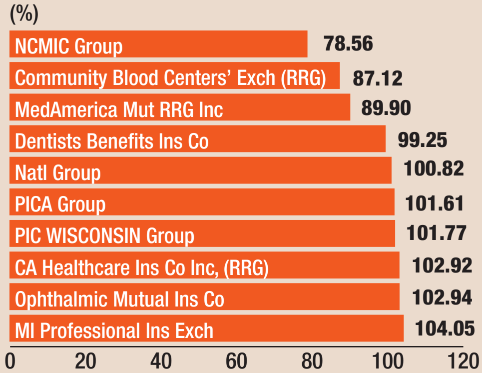
($ Thousands)

Group / Company Name	AMB#	2004 Net Premiums Written	2004 Combined Ratio	5-Year Combined Ratio	10-Year Combined Ratio
NCMIC Group	18579	$61,318	99.30	87.09	78.56
Community Blood Centers Exch RRG	11569	3,717	85.76	86.24	87.12
MedAmerica Mut RRG Inc	11431	8,637	95.24	98.41	89.90
Dentists Benefits Ins Co	10690	2,109	99.75	92.47	99.25
Natl Group	18249	60,461	103.05	103.83	100.82
PICA Group	18480	61,438	93.91	98.14	101.61
PIC WISCONSIN Group	18454	55,495	107.85	110.53	101.77
CA Healthcare Ins Co Inc, RRG	11230	13,879	99.70	104.47	102.92
Ophthalmic Mutual Ins Co (A RRG)	10844	36,059	90.12	103.07	102.94
MI Professional Ins Exch	10804	9,305	107.03	104.54	104.05
Entire Group (50% or more of premiums)		$5,320,101	119.96	129.22	121.83

Source: A.M. Best Co.

Medical Malpractice 10-Year Combined Ratio

(%)



Top Performing Underwriters Among Companies That Derive 50% or More of Their Premiums From Each Specific Line *(continued)*

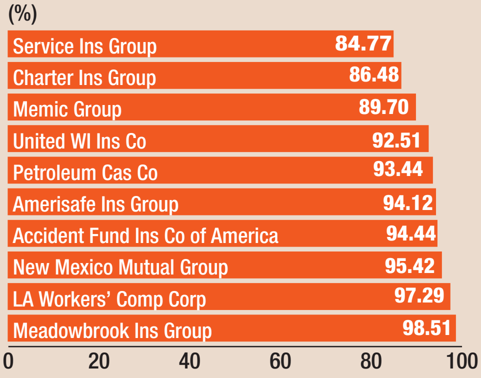
Workers' Compensation

Ranked by 10-year combined ratio

($ Thousands)

Group / Company Name	AMB#	2004 Net Premiums Written	2004 Combined Ratio	5-Year Combined Ratio	10-Year Combined Ratio
Service Ins Group	18385	$46,317	90.38	89.83	84.77
Charter Ins Group	18396	42,748	92.26	91.92	86.48
Memic Group	18524	176,063	101.78	98.79	89.70
United WI Ins Co	01932	67,787	89.81	92.78	92.51
Petroleum Cas Co	00769	4,910	102.42	93.06	93.44
Amerisafe Ins Group	18211	240,560	98.95	97.74	94.12
Accident Fund Ins Co of America	11770	488,533	88.56	95.47	94.44
New Mexico Mutual Group	18292	66,812	107.54	111.63	95.42
LA Workers' Comp Corp	11339	192,244	101.24	96.10	97.29
Meadowbrook Ins Group	18132	120,225	96.60	102.09	98.51
Entire Group (50% or more of premiums)		$16,593,763	98.36	109.12	111.94

Source: A.M. Best Co.



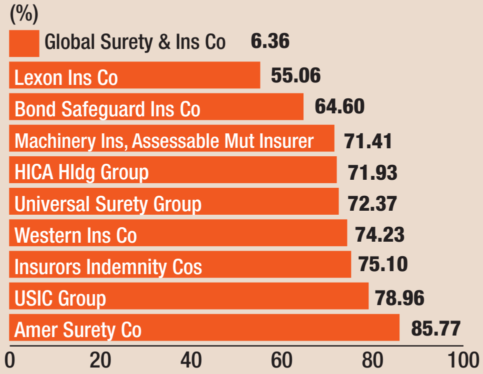
Fidelity and Surety

Ranked by 10-year combined ratio

($ Thousands)

Group / Company Name	AMB#	2004 Net Premiums Written	2004 Combined Ratio	5-Year Combined Ratio	10-Year Combined Ratio
Global Surety & Ins Co	04156	$12,365	5.97	5.49	6.36
Lexon Ins Co	00743	29,782	55.00	60.61	55.06
Bond Safeguard Ins Co	03507	11,220	48.25	62.15	64.60
Machinery Ins, Assessable Mut Insurer	10638	235	53.13	67.31	71.41
HICA Hldg Group	18285	147,990	54.83	65.14	71.93
Universal Surety Group	00937	2,728	53.47	57.63	72.37
Western Ins Co	12055	1,650	58.25	74.34	74.23
Insurors Indemnity Cos	18609	823	81.54	75.43	75.10
USIC Group	18655	11,138	96.05	79.66	78.96
Amer Surety Co	02557	7,434	81.80	87.31	85.77
Entire Group (50% or more of premiums)		$559,396	73.92	89.76	90.30

Source: A.M. Best Co.



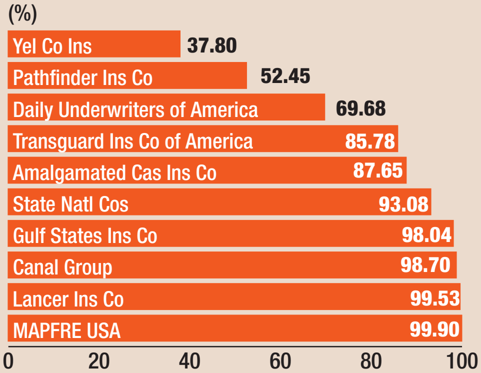
Commercial Auto

Ranked by 10-year combined ratio

($ Thousands)

Group / Company Name	AMB#	2004 Net Premiums Written	2004 Combined Ratio	5-Year Combined Ratio	10-Year Combined Ratio
Yel Co Ins	11343	$1,198	0.75	15.91	37.80
Pathfinder Ins Co	00381	1,860	26.72	29.86	52.45
Daily Underwriters of America	02721	7,471	60.70	69.22	69.68
Transguard Ins Co of America	00327	99,468	102.77	86.54	85.78
Amalgamated Cas Ins Co	00117	4,524	97.46	90.10	87.65
State Natl Cos	18019	45,672	98.41	94.02	93.08
Gulf States Ins Co	10838	6,005	86.33	97.79	98.04
Canal Group	03930	385,593	100.19	99.81	98.70
Lancer Ins Co	02641	61,479	91.99	98.19	99.53
MAPFRE USA	18116	6,768	94.38	101.52	99.90
Entire Group (50% or more of premiums)		$1,398,527	99.63	100.35	101.76

Source: A.M. Best Co.



Leading Writers In Each Line*

Medical Malpractice

Ranked by Net Premiums Written **($ Thousands)**

Group / Company Name	AMB#	2004 Net Premiums Written	2004 Combined Ratio	5-Year Combined Ratio	10-Year Combined Ratio
MLMIC Group	18439	$643,920	204.76	165.22	131.85
GE Ins Solutions Group	18572	533,159	98.94	105.36	105.52
ProAssurance Group	18559	514,798	100.68	116.85	111.55
Doctors Co Ins Group	18083	476,229	96.69	110.48	112.07
Health Care Indemnity, Inc	03701	370,101	100.05	110.71	114.55
CNA Ins Cos	18313	347,090	104.67	146.96	138.11
Norcal Group	18539	285,727	109.40	121.83	128.19
ProMutual Group	18359	275,954	115.05	153.76	141.53
Mag Mutual Group	18635	253,056	105.77	115.90	115.39
ISMIE Mutual Group	18644	223,613	114.02	125.94	128.25
Entire Industry Total and Averages		$7,386,266	112.35	135.54	125.48

Source: A.M. Best Co.

Workers' Compensation

Ranked by Net Premiums Written **($ Thousands)**

Group / Company Name	AMB#	2004 Net Premiums Written	2004 Combined Ratio	5-Year Combined Ratio	10-Year Combined Ratio
State Comp Ins Fund CA	04028	$7,949,665	95.62	106.69	112.89
Liberty Mutual Ins Cos	00060	3,684,035	108.17	114.00	112.48
St. Paul Travelers Group	18647	2,162,999	100.41	98.47	104.91
Hartford Ins Group	00048	1,920,776	101.77	107.80	107.39
Zurich Finl Svcs NA Group	18549	1,266,589	113.86	105.65	105.03
CNA Ins Cos	18313	1,229,265	123.15	135.64	111.20
Zenith Natl Ins Group	03020	949,188	87.53	100.58	105.97
Ace INA Group	18498	921,904	82.22	93.81	109.12
Chubb Group of Ins Cos	00012	898,988	92.87	95.81	98.92
W.R. Berkley Group	04655	807,348	102.65	102.02	100.60
Entire Industry Total and Averages		$40,049,097	104.90	112.49	109.91

Source: A.M. Best Co.

Fidelity and Surety

Ranked by Net Premiums Written **($ Thousands)**

Group / Company Name	AMB#	2004 Net Premiums Written	2004 Combined Ratio	5-Year Combined Ratio	10-Year Combined Ratio
St. Paul Travelers Group	18647	$873,386	207.31	123.74	106.63
Chubb Group of Ins Cos	00012	523,682	63.82	75.85	80.94
CNA Ins Cos	18313	354,314	64.60	93.01	86.49
Zurich Finl Svcs NA Group	18549	301,620	130.37	111.33	101.22
Safeco Ins Cos	00078	232,467	76.51	79.94	78.55
Berkshire Hathaway Ins	00811	214,857	22.33	43.17	51.31
Hartford Ins Group	00048	190,510	85.58	102.08	97.73
HICA Hldg Group	18285	147,990	54.83	65.14	71.93
Liberty Mutual Ins Cos	00060	146,845	117.90	131.18	115.18
Great Amer P&C Ins Group	04835	112,375	92.92	101.16	93.15
Entire Industry Total and Averages		$4,707,930	111.21	107.96	98.23

Source: A.M. Best Co.

Commercial Auto

Ranked by Net Premiums Written **($ Thousands)**

Group / Company Name	AMB#	2004 Net Premiums Written	2004 Combined Ratio	5-Year Combined Ratio	10-Year Combined Ratio
St. Paul Travelers Group	18647	$2,296,121	90.62	101.09	104.88
Progressive Ins Group	00780	1,613,978	82.35	88.04	90.22
Zurich Finl Svcs NA Group	18549	1,159,817	84.61	96.65	106.40
State Farm Group	00088	1,072,717	92.30	102.96	100.62
Liberty Mutual Ins Cos	00060	1,051,654	95.41	116.15	119.83
Nationwide Group	05987	834,786	89.10	99.77	105.77
CNA Ins Cos	18313	833,112	98.14	103.61	106.71
Hartford Ins Group	00048	731,851	95.34	101.85	104.28
Auto-Owners Ins Group	04354	703,712	84.49	95.70	98.70
Allstate Ins Group	00008	629,434	96.34	101.45	103.32
Entire Industry Total and Averages		$25,556,010	92.18	103.36	107.25

Source: A.M. Best Co.

*Several American International Group companies have delayed the filings of their statutory financial statements. Consequently, data for all AIG companies (A.M. Best Company #18540) is excluded from this report. By direct premiums written in 2003, AIG ranked as the No. 3 largest writer of medical malpractice; No. 2 in workers' compensation; and No. 5 in commercial auto.