

Surety and Construction Markets--2009

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Topics Covered Today

- Snapshot of the Surety Industry
- Expected Market Conditions--2009
 - Surety Companies' Perspectives
 - Producers' Perspectives
- Issues to Watch in 2009
- NASBP and AGC Joint Initiatives



A Snapshot of the Surety Industry



2007 Top 10 Writers

(Source: Surety and Fidelity Association of America)

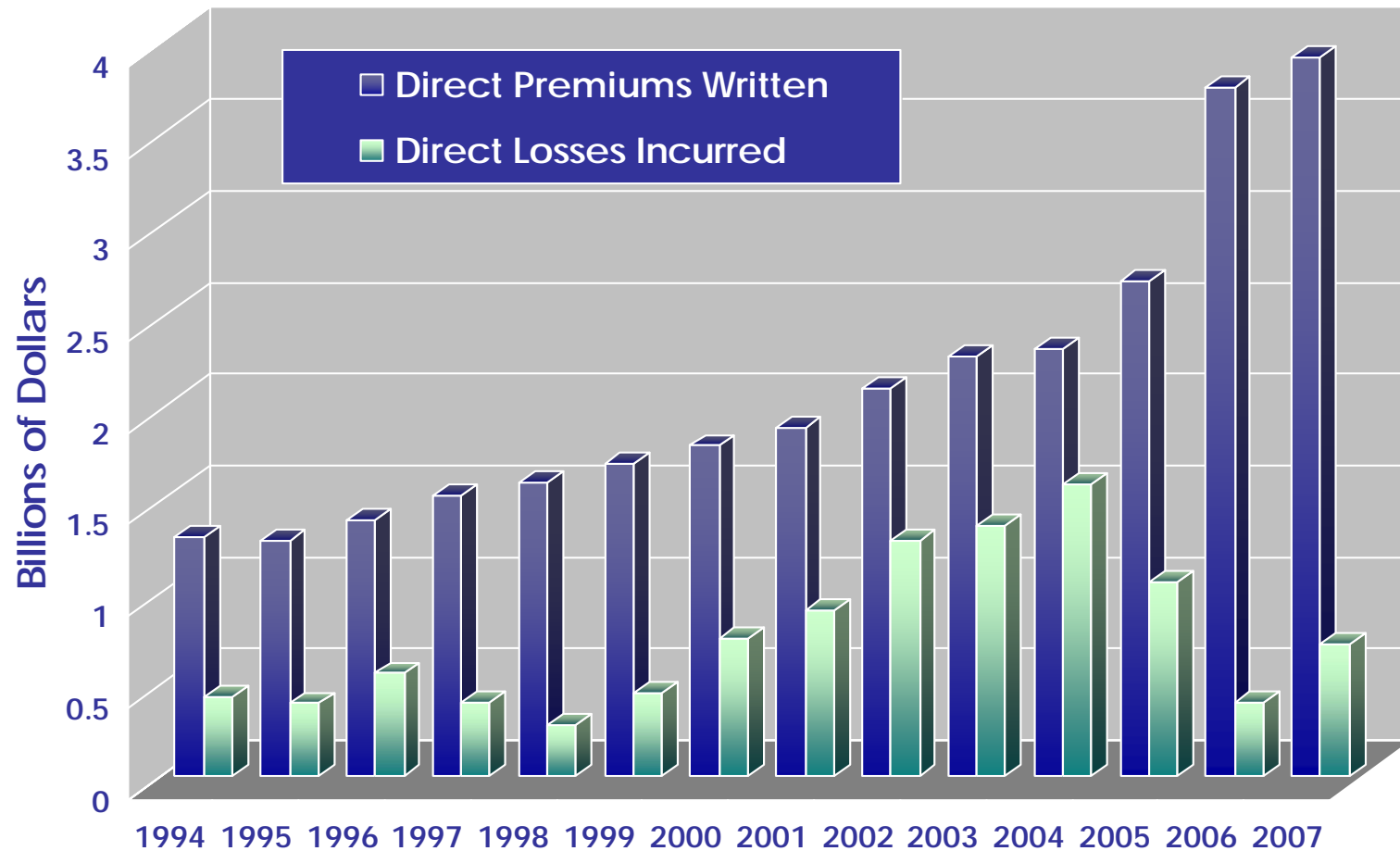
Direct Premium Written (Millions \$)

• Travelers Bond	\$1,017
• Zurich Insurance Group	\$449
• CNA Insurance Group	\$436
• Safeco Insurance Group	\$423
• Liberty Mutual Insurance Group	\$341
• Chubb & Son Inc.	\$303
• The Hartford	\$223
• HCC Surety Group	\$163
• Arch Capital Group	\$127
• ACE Ltd. Group	\$119

Total \$5.4 Billion



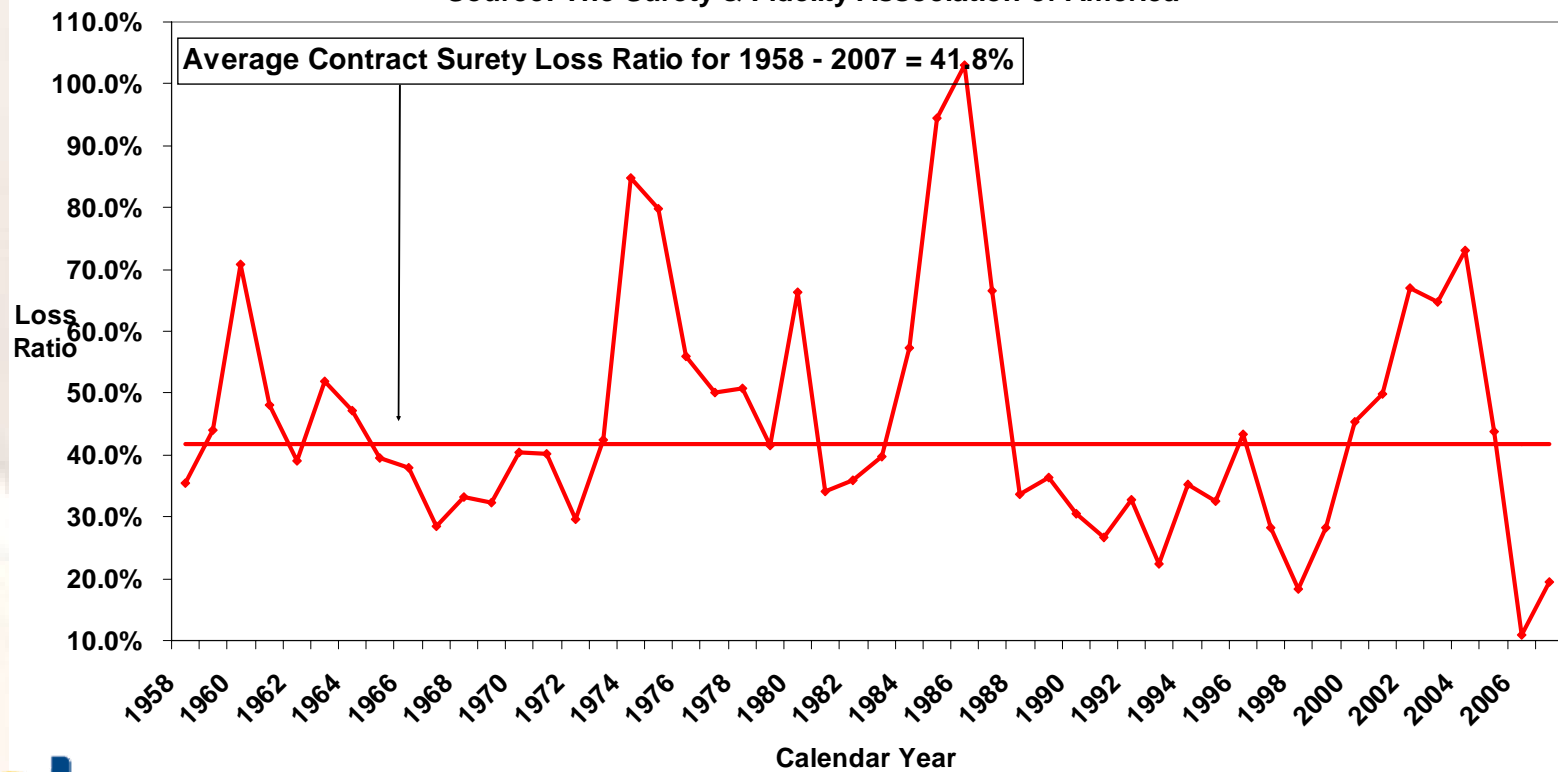
Contract Surety Premiums and Losses



Surety Losses & Profitability

Contract Surety Industry Loss Ratios CY 1958 - 2007

Source: The Surety & Fidelity Association of America



A large, faded, circular logo of the National Association of State Budget Prisons (NASBP) is centered in the background. The logo features a stylized city skyline with a sun rising behind it, and the acronym 'NASBP' is written in a serif font across the middle.

Expected Market Conditions--2009



Surety Companies' Perspectives

- Most surety executives see increased risk coming but believe the construction and surety industries are better prepared to manage the cycle.
- Sureties indicate that contractors continued to carry strong backlogs with good profit margins most of 2008. This indicates that short-term default activity should remain low.



Surety Companies' Perspectives (Cont'd)

- While many sureties also believe that strong cash flow earned during more robust times may be keeping some contractors afloat during the current downturn, they recognize the cash flow requires a sufficient number of new projects being let to sustain the construction industry.



Producers' Perspectives

- Historically, construction lags behind downturns in the financial marketplace.
- The construction industry will be subject to fierce competition in the procurement of work.
- Lack of work in the private sector will compel new entrants into the public works marketplace.
- More contractors pursuing fewer projects will place undue pressure on margins.



Producers' Perspectives (Cont'd)

- Budget crises at state and local levels may result in delays of construction projects.
- The current banking crisis causes no small amount of concern.
- All indicators point to there being sufficient work in the pipeline in 2009.



Issues to Watch in 2009



Issues to Watch in 2009

- Building Information Modeling and Green Building construction will demand new and improved skill sets by the contractor and the surety.
- Contractors will need to keep systems up to speed and be educated and certified to remain competitive.
- Risk shifting from owners to general contractors and from general contractors to subcontractors will continue.



BIM

- New concept to the surety industry; no clear industry opinion has emerged and surety companies are still forming their positions.
- When contractors utilize BIM technology as part of their contractual performance requirements for a project, certain surety issues may arise, particularly in absence of a clear delineation of design, coordination, and communication responsibilities.



Green Building

- March toward green building standard will continue.
- There is a movement to require performance bonds. In all cases, clarity is needed on which party in the project—building owner, contractor or designer—is responsible for obtaining the performance bond, therefore bearing the risk of noncompliance.
- Recently enacted DC Green Building Act could become a model Act for others and is not clear and is fraught with more risk than relief.
- Surety companies and producers are carefully evaluating the risks.



Subcontractor Default Insurance

- First appeared in 1996
- Not designed to be used as single project insurance
- Not for contractors that are risk-averse
- See comparison chart.



Comparison of Surety Bonds to Subcontractor Default Insurance

Issues	Performance and Payment Bonds	Subcontractor Default Insurance
Prequalification Process	Conducted by surety	Left to policyholder
Structure	Three-party agreement	Two-party insurance policy
Payment protection for subcontractors and suppliers	<ul style="list-style-type: none"> - Yes, covered 100 percent by payment bond - Direct payment protection 	<ul style="list-style-type: none"> - Not covered - Unable to file a direct claim with the insurer
Default Management	<ul style="list-style-type: none"> - Claims investigated by surety to ensure legitimacy - If subcontractor defaults, surety completes, arranges for, or pays for the contract completion up to the amount of the bond 	<ul style="list-style-type: none"> - Contractor declares default subject to later judicial review - Contractor manages default, including completing the contract and filing the claim with the insurer
Risk	Shifted to surety for contract completion and payment to subcontractors and suppliers	Contractor retains a portion of the risk through deductibles and copayments; sub-subcontractors and suppliers bear risk of nonpayment
Legal	<ul style="list-style-type: none"> - Required by federal and state law on public projects - Long history of case law and legal precedents 	<ul style="list-style-type: none"> - Does not satisfy federal and state bond requirements - Little history of case law or legal precedence

Chart excerpted from Construction Executive magazine, "Subcontractor Default Insurance A Hidden Treasure—Or a Danger," April 2007, p. 41.

NASBP and AGC Joint Initiatives



NASBP and AGC Working Together

- Delivered “Urgent” Hill message encouraging Members of Congress to support investment in U.S. infrastructure.
- Support curtailing of improper bundling of smaller federal construction contracts into larger projects in order for small and emerging contractors to participate in federal procurement.
- Support amending FAR regulations to require contracting officers to be transparent with their decision to waive performance and payment bonds on overseas construction projects.



NASBP and AGC Working Together (Cont'd)

- Support lessening the administrative burden on contracting officers by more narrowly defining acceptable assets proposed by individual sureties to back performance and payment bonds for federal construction projects.
- Participate as endorsing members in the ConsensusDOCS™ effort.



NASBP and AGC Working Together (Cont'd)

- Co-administer the AGG/NASBP/SFAA Surety Underwriter Intern Program
 - National educational program where an underwriter from a surety company spends a week with a contractor observing operations both in the contractor's office and job site.
 - Surety company pays all intern's expenses.
 - Host contractors needed!
 - Sign up at <http://www.suretyintern.org>



For More Information

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Thank you!

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