

SURETY BONDS IN THE US: UNDERSTANDING TODAY'S MARKET

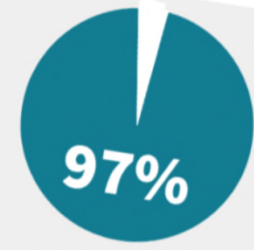
Lynn M. Schubert
President
The Surety & Fidelity Association of America



The Surety & Fidelity Association of America



Serving the Industry Since 1908



Percentage of U.S. surety and fidelity premium written by SFAA member companies

\$7.2 Billion
Surety and fidelity premium in 2016

Statistics

As a licensed statistical agent, SFAA collects statistical plan and financial statement data and satisfies members' mandatory reporting requirements countrywide. SFAA develops aggregate industry statistical reports available on the Member section of the SFAA website.

Contact: Ed O'Donnell | eodonnell@surety.org

Advocacy

SFAA advocates, monitors and reports to members on industry-related legislative, regulatory and judicial developments. Staff also presents SFAA's position on issues to legislatures, agencies, courts, and trade associations and promotes the interests of Members.

Contact: Lenore Marema | lmarema@surety.org

Education

SFAA provides industry-specific educational seminars and programs to promote public understanding and confidence in the surety and fidelity bonding industries and products and to support member training efforts.

Contact: Joanne Brooks | jbrooks@surety.org

Expertise

Members can access staff for help on a wide range of matters from risk-type classifications and analysis of bond forms to development of a mentoring program and industry-specific recruiting support.

Regulatory Services

SFAA develops and files countrywide surety and fidelity manual rules, loss costs and standard fidelity forms. Members may elect to provide SFAA with authorization to file on their behalf or may submit independent filings. Authorizations are filed on a by-state, by-company basis.

Contact: Daniel Wanke | dwanke@surety.org

Fidelity Forms

SFAA develops and files standard fidelity forms and endorsements for policies, bonds and other forms for optional use by Members. Current members are also free to utilize SFAA copyrighted material to develop and file independently.

Contact: Rob Duke | rduke@surety.org

Promotion

Promotion of the products of the surety and fidelity industry is at the foundation of all of SFAA's member services. SFAA has served as the industry thought leader and trusted adviser for over a century, promoting surety and fidelity bonds as the gold standard.

Contact: Bryan Surcouf | bsurcouf@surety.org

Networking

Membership provides a valuable forum to discuss topics of common interest within the bounds of SFAA's Antitrust Guidelines. All members are invited to participate on the SFAA Board's advisory committees.

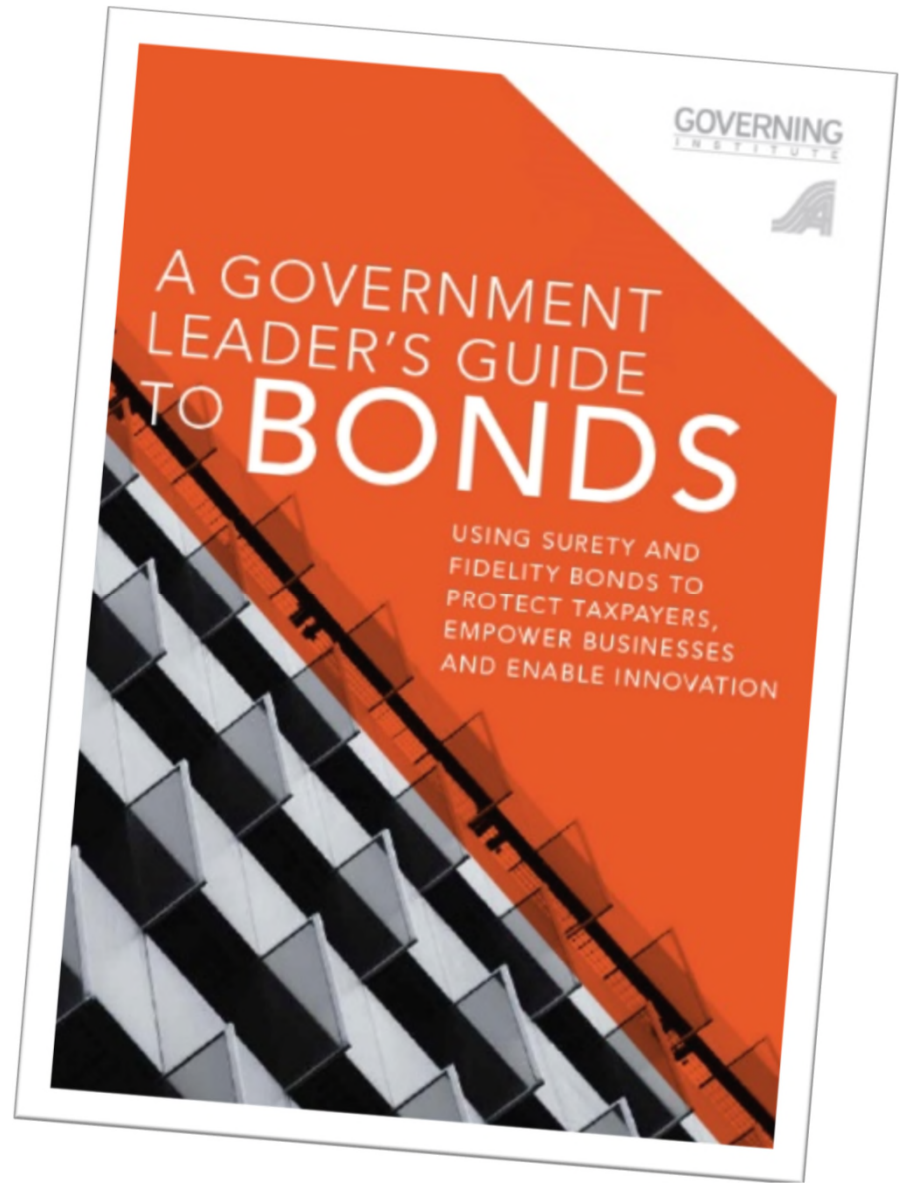


- Statistical Organization
- Actuarial Organization
- Advisory Organization
- Trade Association

What issues are we facing?

- **Economy**
- **Politics**
- **Perception**
- **Statistical**





In their own words...

“We brought in the surety and started discussing how to get each project back under construction as quickly as possible....They did all the work that we would have to do if we didn’t have the performance bond. Everything got back under construction, and we got them [projects] all done.”

-John Obr

former director of the
Construction Division, Texas
Department of Transportation
(TxDot)





Surety Bonds in the Alternative Delivery Environment

The Challenges and Trends: P3s

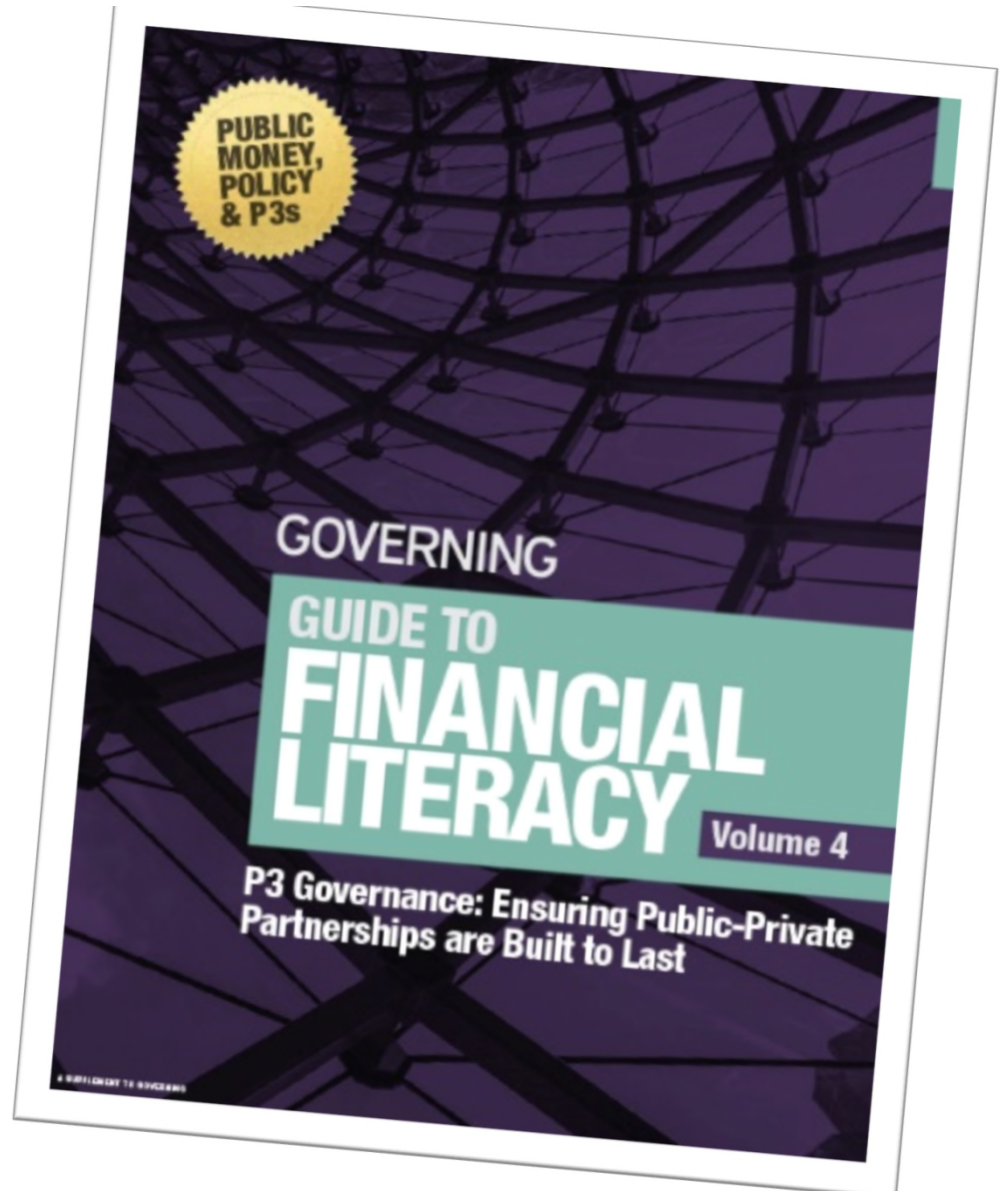
- SFAA takes No Position on use of P3s
- The End Result is a public works project that should be bonded
- We seek bonding for the design and construction portion of P3s



The Challenges and Trends: P3s

- Public Private Partnerships (P3s) are increasingly attractive to states that lack the funding for needed infrastructure projects
- Federal infrastructure program. Changed attitude toward P3
- States need alternative funding/financing







SURETY BONDS: A CRITICAL SAFEGUARD FOR P3 PROJECTS



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Most P3 projects involve construction, and construction involves risk. Research conducted between 2013 and 2015 found that contractors had a failure rate of approximately 29 percent, meaning more than 1 in 4 of these businesses will fail. Even though bonded contractors are less likely to fail, over the last 15 years, surety companies paid nearly \$12 billion to complete construction contracts and pay subcontractors and suppliers what they were owed. These numbers do not include the significant money sureties spent to finance troubled contractors so they could complete contracts, protecting governments and private owners from defaults. In 2016 alone sureties paid approximately \$1.4 billion to owners, subcontractors, suppliers and contractors on surety bond obligations.

Why are performance and payment bonds, typically for 100% of the contract price, universally required on infrastructure projects in the U.S.? To provide public owners, developers and lenders the benefit of an independent third party, the surety, and to help determine that a contractor has the ability to perform the contract and meet its payment obligations. And, if something goes awry and the contractor defaults, to have the surety provide funds to complete the contract, and to directly manage and pay claims of subcontractors and suppliers on the job. Those subcontractors and suppliers have a direct right to make

a claim on the surety bond for payment rather than having to attempt payment from a bankrupt contractor or from a public entity.

Surety bonds significantly increase the likelihood that a construction contract will be completed and that subcontractors, suppliers and workers will be paid.

P3s provide a new source of financing for the public entity to procure work, not a new revenue source. A P3 is a way for public entities to access the capital market but the construction risks remain the same. High percentage performance and payment bonds remain a best practice for the design build portion of any P3 contract.

Surety bonds also empower contractors. Contractors can obtain more work when they are backed by surety bonds than by only their own balance sheet. This significantly benefits small, emerging, disadvantaged and minority contractors.

Strong businesses are bondable businesses and sureties focus on strengthening businesses, managing growth and building legacy wealth. No matter the project delivery method, bonding helps public agencies assess and minimize their risk while empowering contractors to undertake work they can deliver.



TO FIND OUT MORE, DOWNLOAD A GOVERNMENT LEADER'S GUIDE TO BONDS AT WWW.GOVERNING.COM/GUIDETOBONDS OR VISIT WWW.SURETY.ORG.

The Challenges and Trends: Expanding the Pie



<https://vimeo.com/266771693/073a9149c9>

Internationally

- **Carillion and the Surety Industry**
- **International Surety Association**





Members: Australian Surety Association - Surety & Fidelity Association of America -
International Credit Insurance & Surety Association - Surety Association of Canada - Surety Association of Mexico-
Pan-American Surety Association

To: the editor

What is the impact to the taxpayers and unpaid subcontractors, suppliers, materialmen and laborers when the second largest contractor in the UK files for liquidation? Could the government have taken steps to protect taxpayers, mitigate the risk of losses to the taxpayers while increasing the likelihood of completion of the various projects and payment to those performing work on the project? What about the reputation risk to the government?

The extent of the collapse of the construction company, Carillion, has yet to be determined. Some estimates indicate that the "too big to fail" company held close to £5 billion in financial obligations. UK taxpayers and as many as 30,000 subcontractors will be forced to bear the cost of the insolvency.

Current data indicates that the vast majority of Carillion construction contracts are not secured by a surety bond, and when those contracts are for government projects, the UK taxpayer is the victim. The additional cost to complete those contracts and pay workers and subcontractors now will be paid for by public funds, and not reimbursed by a surety company.

Surety bonds protect tax-payers' money. Government departments, public bodies, subcontractors, workers and ultimately the tax payer benefit from the security of a surety bond. These bonds guarantee the performance of a contractor. They provide the security to protect the construction project owner against the insolvency of a contractor or the failure of a contractor to complete a contract in accordance with its terms and specifications.

When a government entity awards a construction contract to a contractor, and obtains a large penalty surety bond, it knows that the surety bond company stands behind the contractor's promise to complete the contract according to the owner's specifications and terms of the contract. A surety's prequalification of a contractor decreases the chance of contractor failure, but when a contractor failure occurs, taxpayers are protected against virtually all losses caused by the contractor failure. That's because surety bond companies provide the resources necessary to complete the contracts and pay certain bills for labour,

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SFAA Financial Statement* Calendar Year 2016

Line of Business	Premium Written	Premium Earned	Losses Incurred	Loss Ratio	Combined Ratio
Surety	\$5,896 M	\$5,760 M	\$892 M	15.5%	71.5%
Fidelity	\$1,254 M	\$1,242 M	\$479 M	38.6%	78.7%

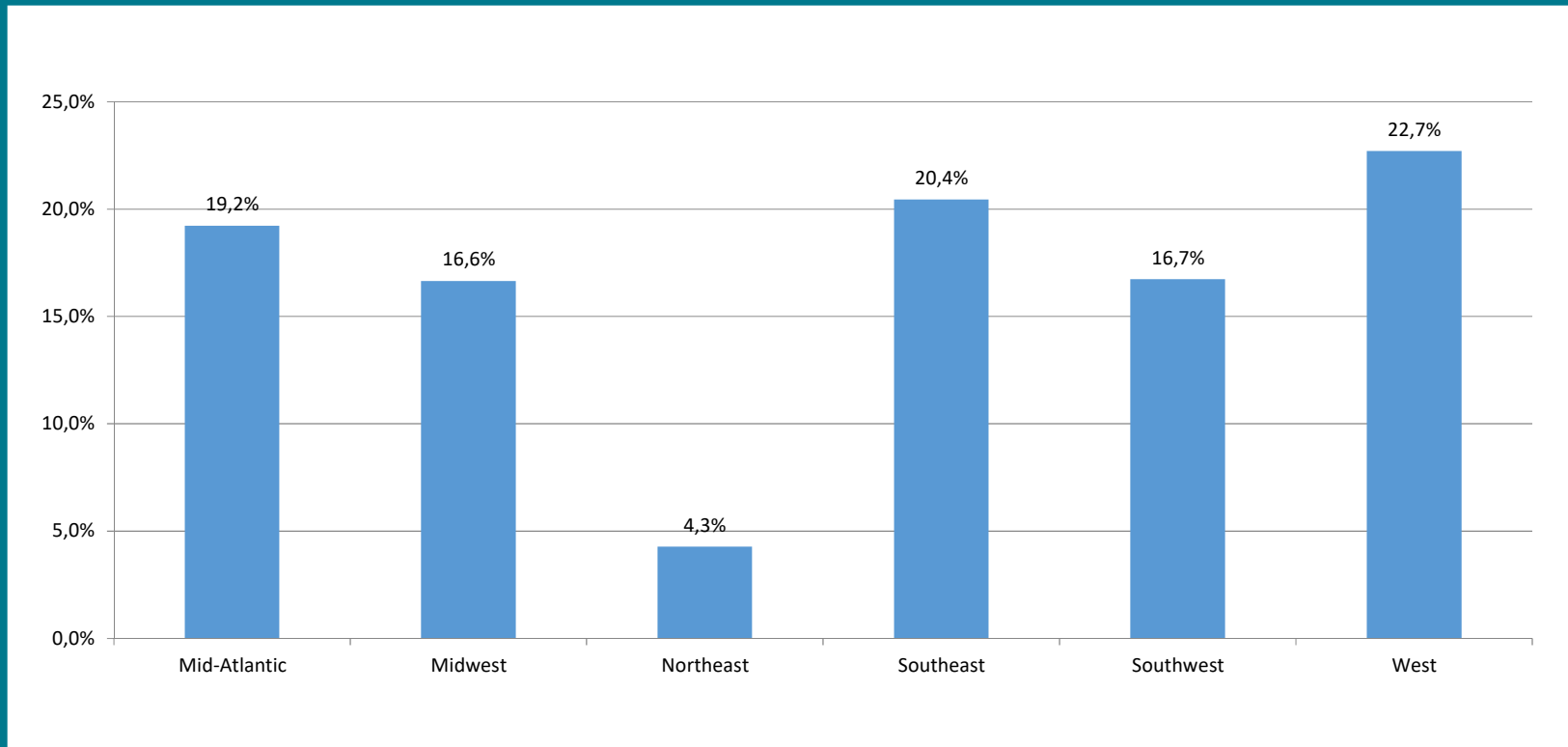
** IBNR included; premium and loss amounts direct and in millions*

2016 Top 10 Surety Writers

Losses include IBNR

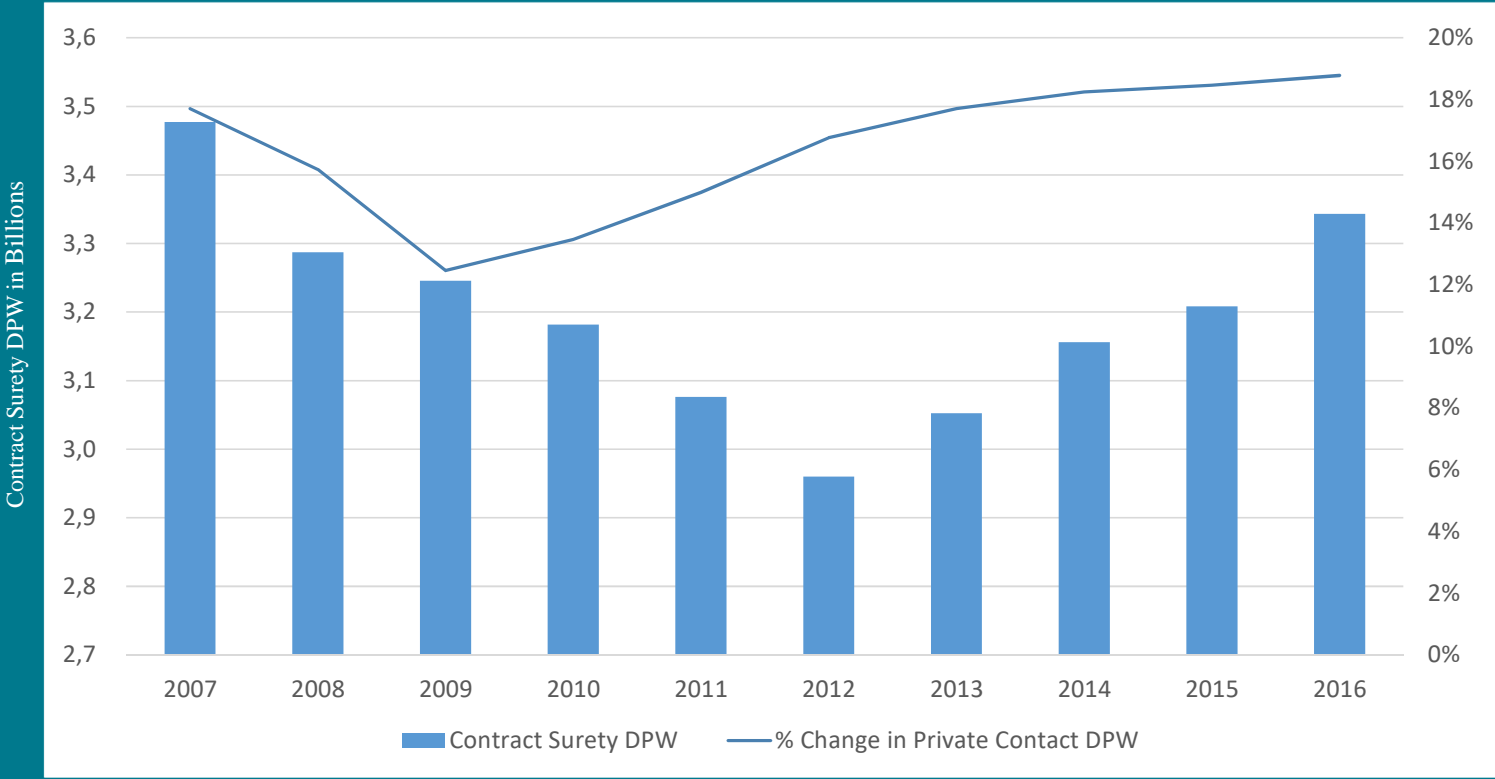
GROUP/COMPANY	Direct Premium Written	Market Share	Direct Premium Earned	Direct Losses Incurred	Direct Loss Ratio	DCCE	DCCE Ratio	Loss+DCC E Ratio
1 TRAVELERS BOND	784,538,250	13.3%	797,469,010	(5,944,787)	-0.7%	(30,514,858)	-3.8%	-4.6%
2 LIBERTY MUTUAL GROUP	751,121,417	12.8%	729,561,650	124,506,131	17.1%	24,185,144	3.3%	20.4%
3 ZURICH INSURANCE GROUP	541,774,411	9.2%	525,981,263	89,791,117	17.1%	38,233,786	7.3%	24.3%
4 CNA SURETY GROUP	438,312,381	7.5%	429,830,476	67,922,818	15.8%	18,207,201	4.2%	20.0%
5 CHUBB LTD.	385,409,658	6.6%	385,718,811	53,535,475	13.9%	11,112,213	2.9%	16.8%
6 HARTFORD FIRE & CAS GROUP	179,999,191	3.1%	175,516,971	36,637,932	20.9%	3,776,060	2.2%	23.0%
7 HCC SURETY GROUP	164,555,267	2.8%	163,048,556	13,555,800	8.3%	8,813,183	5.4%	13.7%
8 IFIC SURETY GROUP	154,310,156	2.6%	155,442,290	8,302,822	5.3%	3,450,923	2.2%	7.6%
9 GREAT AMERICAN INSURANCE COMPANIES	139,920,025	2.4%	136,747,925	42,431,983	31.0%	2,038,208	1.5%	32.5%
10 RLI INSURANCE GROUP	124,932,592	2.1%	124,271,653	16,928,092	13.6%	5,459,784	4.4%	18.0%
Top 10 Writers Subtotals	3,664,873,348	62.3%	3,623,588,605	447,667,383	12.4%	84,761,644	2.3%	14.7%
All Writers Totals	5,882,986,093	100.0%	5,746,640,658	892,138,599	15.5%	181,559,468	3.2%	18.7%

2016 Surety Market Share by Region



Market share determined by direct premium written

Change in Private Contract's Share of Overall Surety



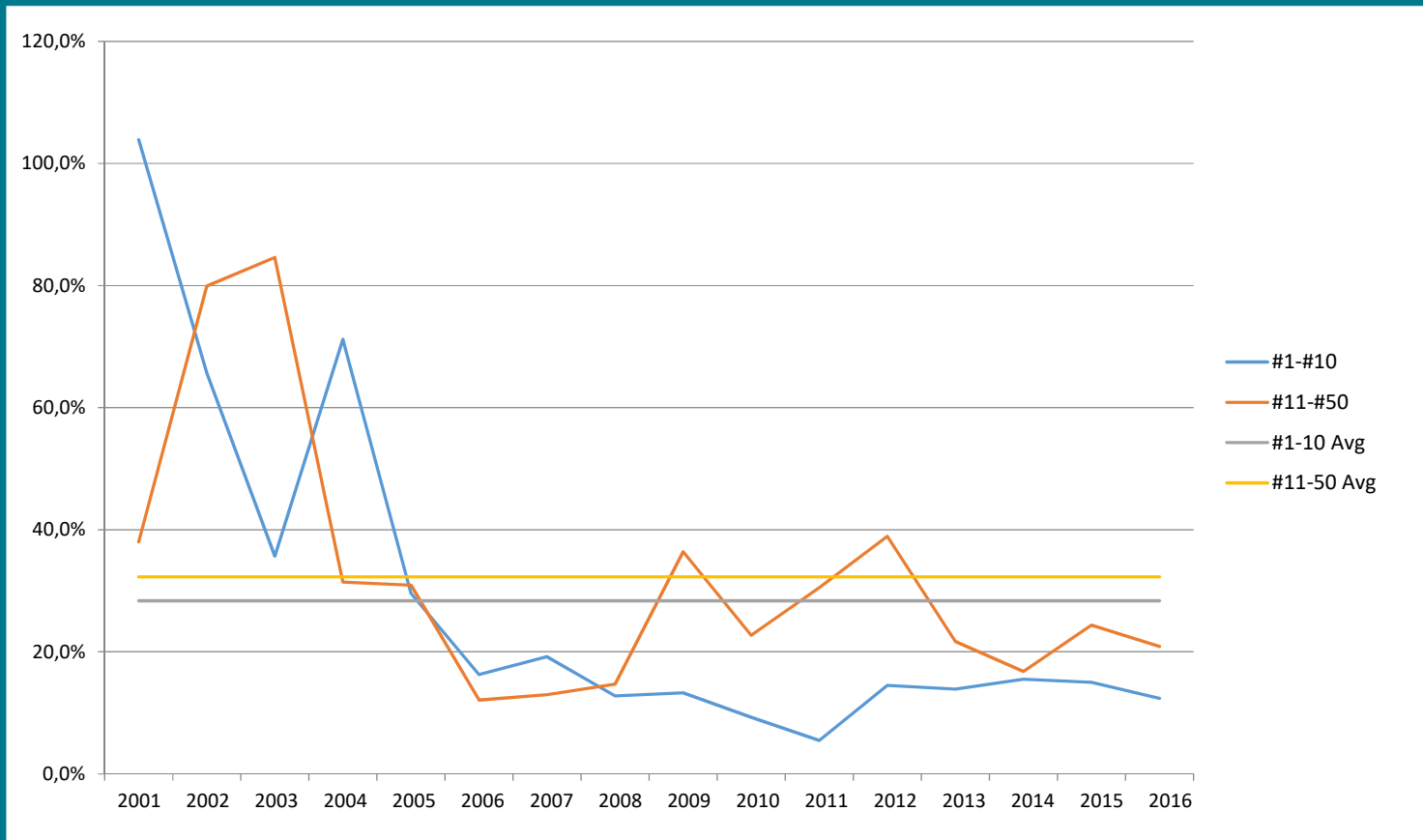
2016 Commercial Surety Loss Ratios by Subline

<i>Type of Commercial Surety</i>	<i>Loss Ratio</i>
Fed & Public Official	5.0%
Court Fiduciaries	13.4%
Court Guarantees	18.1%
Miscellaneous	7.6%
License and Permit	10.8%
All Commercial Surety	10.7%

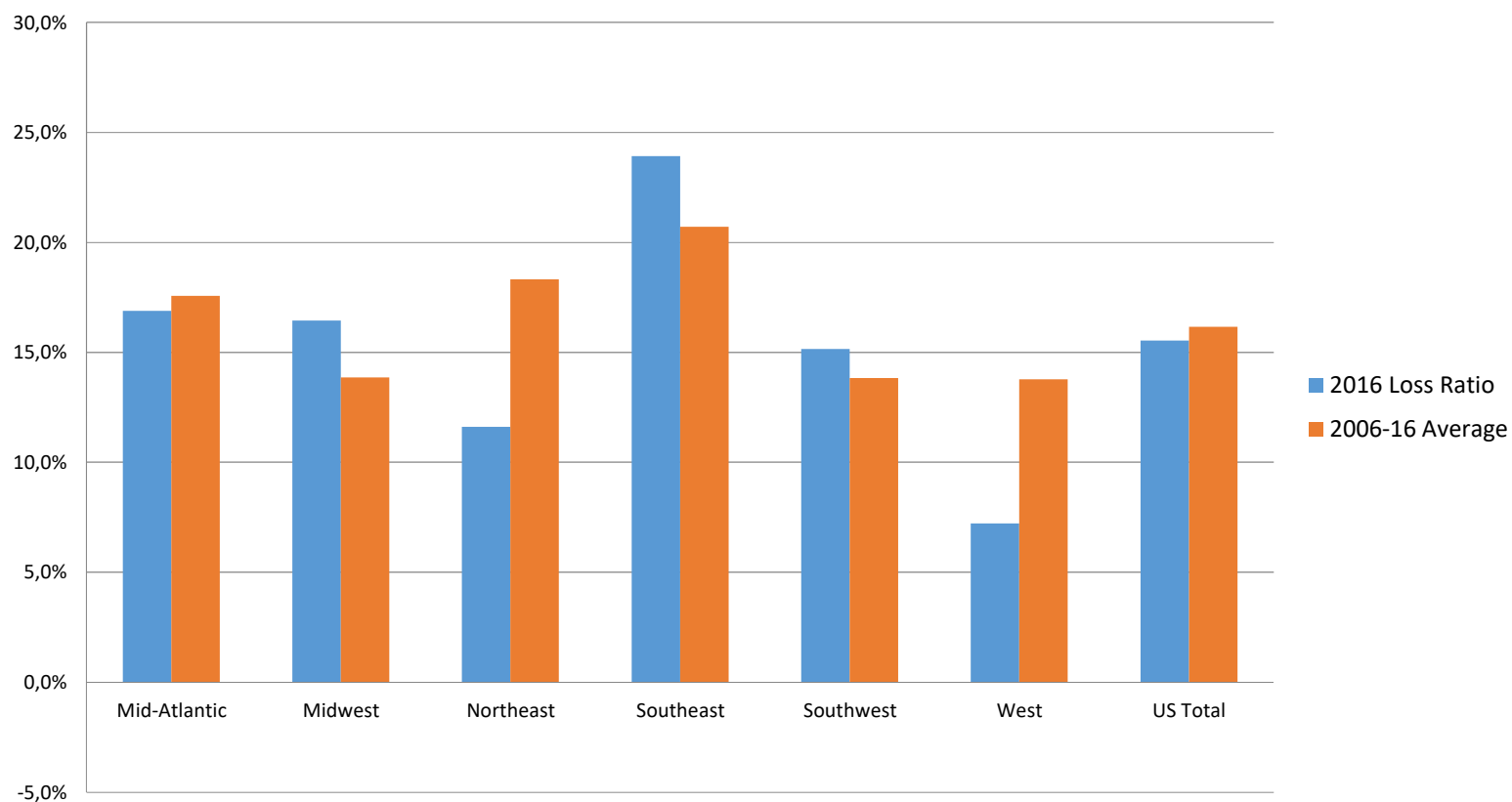
2016 Contract Surety Loss Ratios by Subline

<i>Type of Contract Surety</i>	<i>Loss Ratio</i>
Federal Contracts	29.4%
State/Municipal Contracts	16.2%
Private Contracts	15.8%
All Contract Surety	14.4%

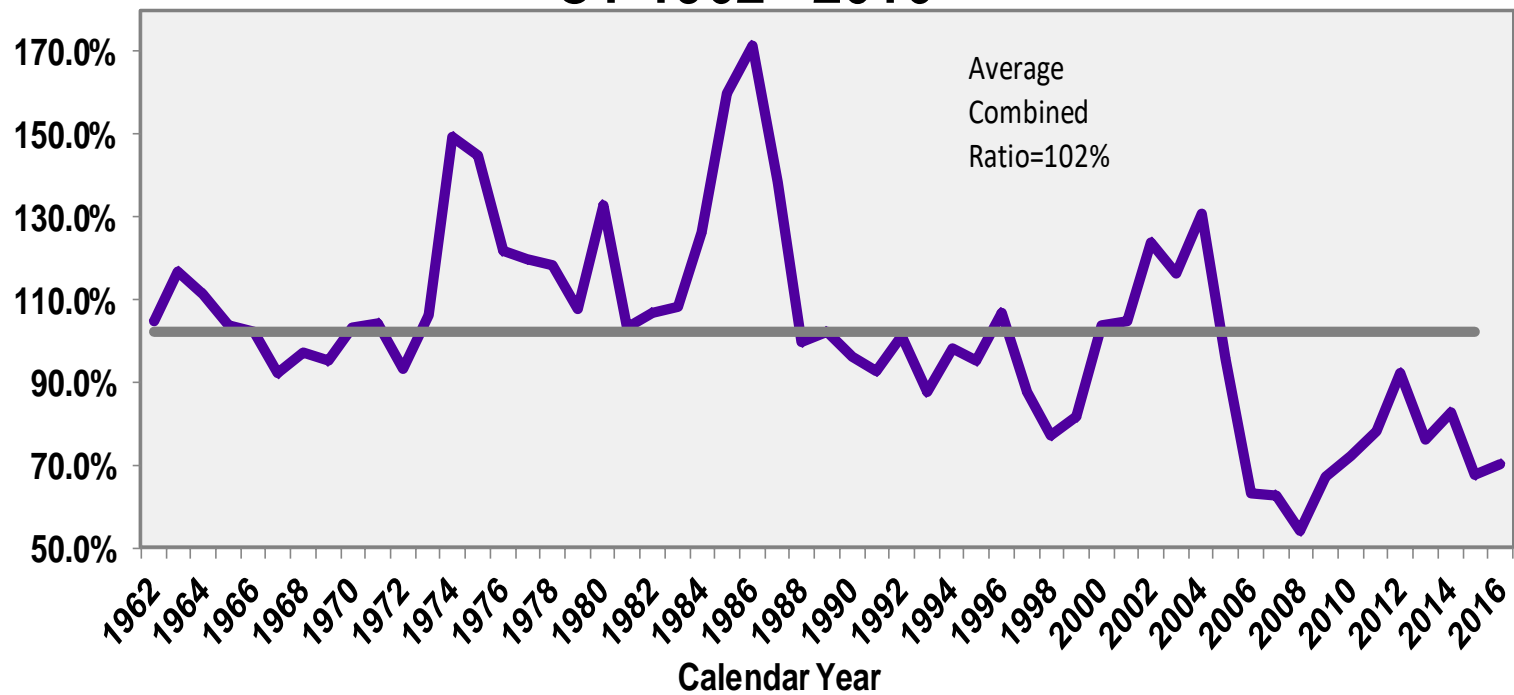
2001-16 Surety Loss Ratios by Market Share



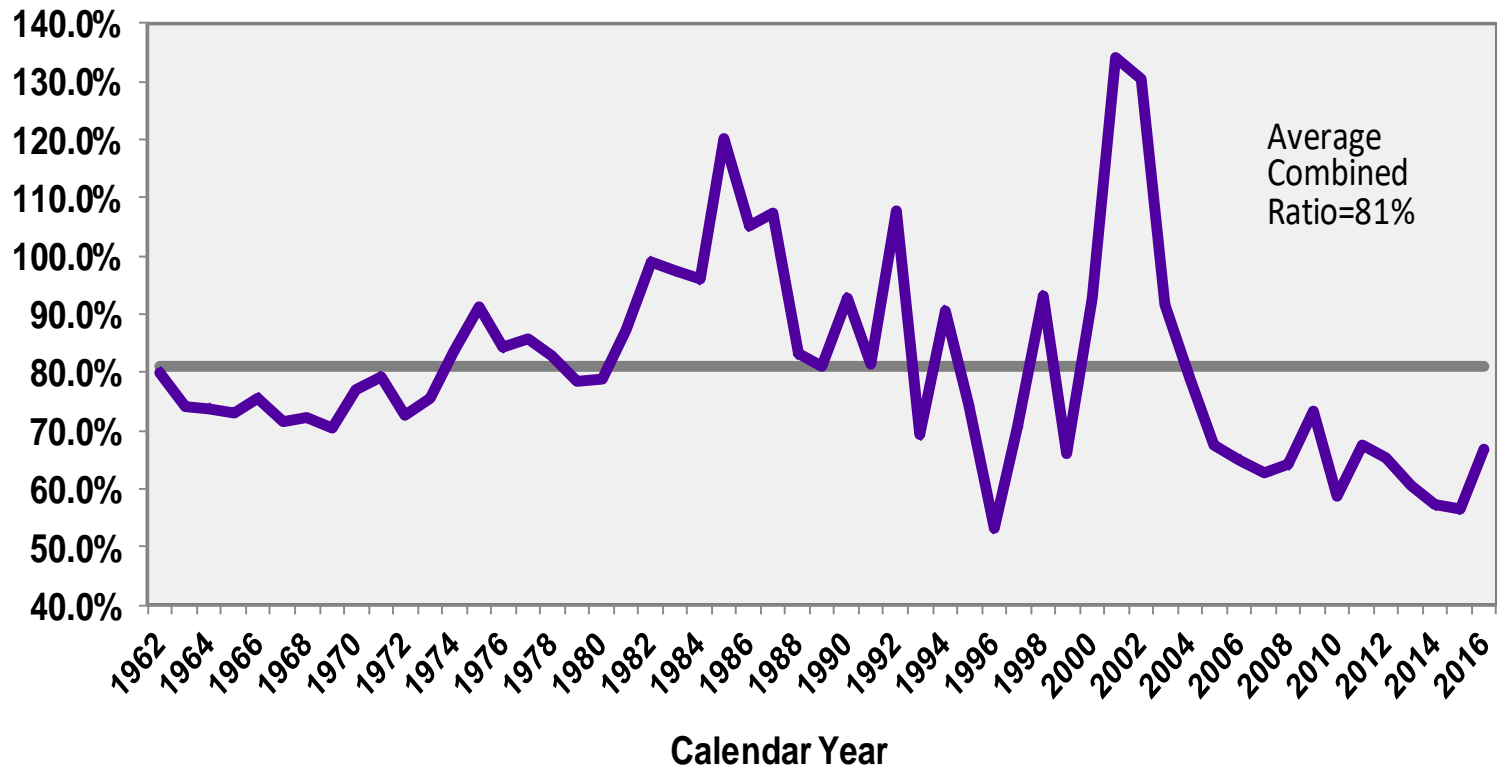
2016 Surety Loss Ratio by Region



Contract Surety Industry Combined Ratios CY 1962 - 2016



Commercial Surety Industry Combined Ratios CY 1962 - 2016



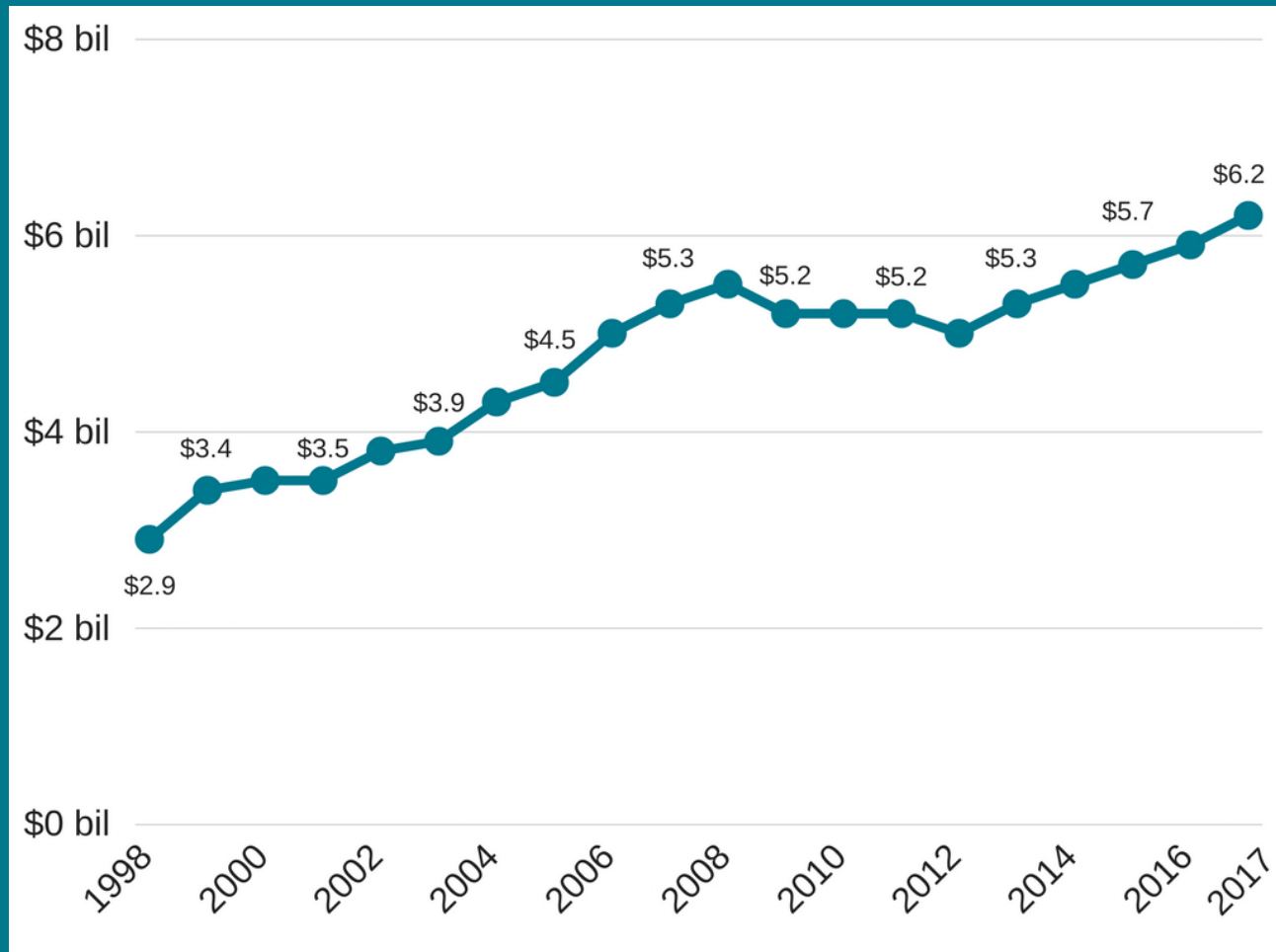


SFAA Financial Statement* Calendar Year 2017

Line of Business	Direct Premium Written	Direct Premium Earned	Direct Losses Incurred	Direct Loss Ratio	Combined Ratio
Surety	\$6,220,369,171	\$6,008,470,346	\$938,192,709	15.6%	69.2%

* IBNR included; premium and loss amounts are direct

Direct Premium Written





- Questions?
- Thank you!