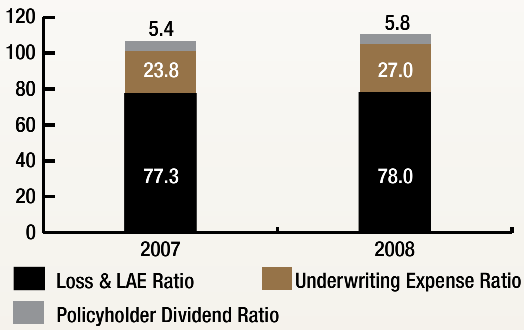
Market Review

September 7, 2009

Sector
Property/Casualty

U.S. Workers' Compensation – A.M. Best Composite[1] Combined Ratio Components (2007-2008)



(1) 103 Groups and Unaffiliated Single Companies (Including State Funds)
Source: A.M. Best

Rating Analysts

Michelle Baurkot, Assistant Vice President
+1 (908) 439-2200 Ext. 5507
Michelle.Baurkot@ambest.com

Edward Keane, Senior Financial Analyst
+1 (908) 439-2200 Ext. 5291
Edward.Keane@ambest.com

Brian O'Larte, Senior Financial Analyst
+1 (908) 439-2200 Ext. 5138
Brian.O'Larte@ambest.com

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Workers' Compensation: How Bad Will It Get?

Challenging market conditions, the financial crisis and the recession drove profitability downward for the U.S. workers' compensation market in 2008, and A.M. Best expects the impact to linger through 2009 and well into 2010. Meanwhile, changing regulatory issues and reforms are continuing to affect workers' comp, bringing turmoil in terms of pricing, competition, loss costs, frequency, severity and profitability.

- A.M. Best Co.'s workers' compensation composite, which consists of 103 groups and unaffiliated single companies (including state funds), saw net income deteriorate by $1.4 billion, or 62%, to $0.9 billion in 2008.

- This drop in earnings reflected both the fall in the financial markets and sharply reduced premium volume due to persistent soft pricing, competition, legislative reforms, the recession, rising unemployment and shrinking payrolls.

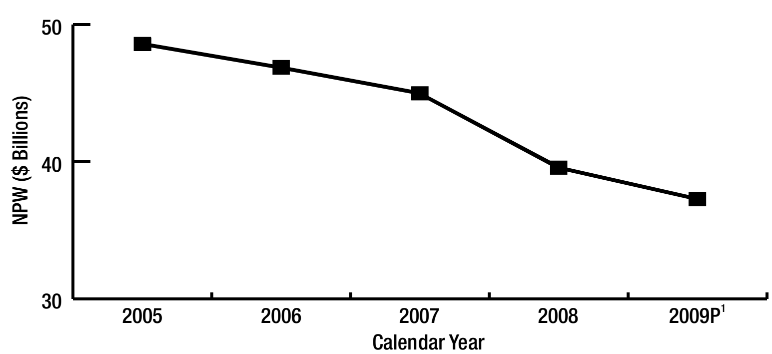
- The composite's 2008 net premiums written (NPW) fell to its lowest level since 2000, down approximately 30% from its high of $20.9 billion in 2004.

- After posting relatively strong underwriting results in 2005 and 2006, the composite recorded underwriting losses of $1.2 billion and $1.5 billion in 2007 and 2008, respectively, with combined ratios of 106.5 and 110.8 for the same periods.

- NPW in the workers' comp line of business fell for the third consecutive year in 2008, declining about 12.0% – far faster than the 2.0% decrease for the overall U.S. P/C industry.

- The workers' comp line reported a calendar-year combined ratio of 104.4 in 2008, up only slightly from 103.6 in 2007, but up sharply from the low of 98.5 reported in 2006.

U.S. Workers' Compensation – Line of Business Net Premiums Written (2005-2009P[1])



(1)P = Projected
Sources: Best's Statement File Supplement - Insurance Expense Exhibit (IEE) - P/C, US; State Insurance Fund NY Annual Statement

Waiting to Hit Bottom

The workers' compensation industry has not been immune to the unprecedented events that have impacted the overall U.S. property/casualty industry over the past 18 months. Challenging market conditions, the financial crisis and the subsequent impact on the economy led to the downturn in profitability for the workers' comp market in 2008, which is expected to continue through the remainder of 2009 and well into 2010. Also impacting the workers' comp market, probably more than any other line of business, are changing regulatory issues and reforms. As history has shown, changes in these areas create major turmoil with respect to pricing, competition, loss costs, frequency, severity and, ultimately, profitability.

As the issues currently facing the workers' compensation market are highlighted throughout this report, the market will be segmented two ways. First, the report will review the performance of A.M. Best Co.'s workers' compensation composite, which consists of 103 groups and unaffiliated single companies (including state funds) that write predominantly workers' comp. Second, the report will review the aggregated underwriting performance of the workers' comp line of business, as reported by those companies and state funds that have completed and filed the Insurance Expense Exhibit (IEE) with A.M. Best.

A.M. Best Workers' Compensation Composite

While 2008 was expected to be a difficult year, with continued pricing pressures and limited investment opportunities, few predicted the magnitude of the financial crisis and its impact on the workers'

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comp market. The A.M. Best workers' compensation composite's net income deteriorated $1.4 billion, or 62%, to $0.9 billion in 2008, down from net income of $2.3 billion in 2007. This year-over-year decline in earnings was largely due to both the downturn in the financial markets, which resulted in realized losses, and the significantly reduced premium volume related to the prolonged period of soft pricing, competitive market conditions, legislative reform measures, the economic recession, rising unemployment and decreases in payrolls. The composite's 2008 net premiums written (NPW) fell to its lowest level since 2000, down approximately 30% from its high of $20.9 billion in 2004. The composite's top line continued to be pressured through the first quarter of 2009, declining approximately 20% to $3.0 billion from the same period in 2008.

The workers' compensation composite's profitability was substantially above average during the past few years, largely following legislative reforms in California and Florida and earlier years of pricing improvement. However, the impacts from ongoing competition, the economic downturn, increasing medical costs and decreases in payrolls have escalated in the most current years and eroded underwriting profits. After two consecutive years of relatively strong underwriting results in 2005 and 2006, the composite recorded underwriting losses of $1.2 billion and $1.5 billion in 2007 and 2008, respectively. This equated to combined ratios of 106.5 and 110.8 for the same periods and represented the highest combined ratios posted by the composite since it reached 118.7 in 2002. The workers' compensation composite's underwriting performance continued to deteriorate through the first quarter of 2009 with a combined ratio of 111.1. The composite is expected to report modest deterioration through the remainder of the year, as limited rate stabilization and projected reserve releases should partially offset economic pressures in the subsequent quarters of 2009.

Driven by the combined impacts of deteriorating underwriting and investment results, the composite's statutory policyholders' surplus fell for the first time since 2002,

Exhibit 1

U.S. Workers' Compensation – A.M. Best Composite[1] Financial Indicators (2007-2008)

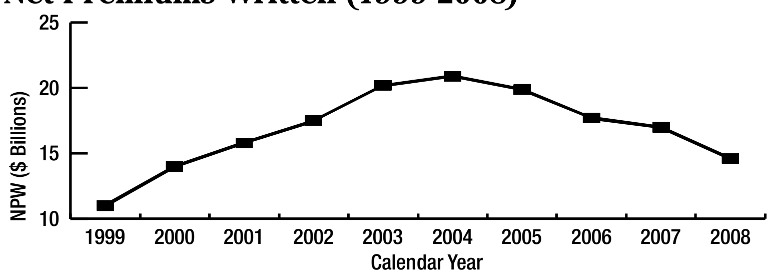
($ Billions)

	2007	2008	Year/Year % Change
Net Premiums Written	$17.0	$14.6	-14.2
Net Premiums Earned	16.7	14.8	-11.2
Pure Losses Incurred	10.5	9.1	-12.6
Loss-Adjustment Expenses	2.4	2.4	-0.4
Losses & LAE	12.9	11.6	-10.3
Underwriting Expenses	4.1	3.9	-2.9
Policyholder Dividends	0.9	0.9	-4.7
Underwriting Income/(Loss)	(1.2)	(1.5)	-31.8
Net Investment Income	3.7	3.6	-2.4
Other Income	(0.0)	(0.2)	-1,525.0
Pretax Operating Income/(Loss)	2.6	1.9	-25.1
Realized Capital Gains/(Losses)	0.3	(0.7)	-288.2
Federal Income Taxes	0.6	0.4	-32.3
Net Income	**2.3**	**0.9**	**-62.4**

(1) 103 Groups and Unaffiliated Single Companies (Including State Funds)
Note: Figures may not add due to rounding.
Source: A.M. Best

Exhibit 2

U.S. Workers' Compensation – A.M. Best Composite[1] Net Premiums Written (1999-2008)



(1) 103 Groups and Unaffiliated Single Companies (Including State Funds)
Source: A.M. Best

Exhibit 3

U.S. Workers' Compensation – Top 10 Carriers in A.M. Best Composite[1]

Ranked by 2008 net premiums written.
($ Thousands)

Rank	Group/Unaffilated Single Company	2007 NPW ($000)	2008 NPW ($000)	Year-over-Year % Change
1	State Compensation Insurance Fund of CA	$2,272,842	$1,666,499	-26.7
2	State Insurance Fund of New York	1,719,136	1,355,121	-21.2
3	Accident Fund Group	819,791	868,420	5.9
4	Texas Mutual Insurance Company	751,005	758,796	1.0
5	Zenith National Insurance Group	717,490	590,440	-17.7
6	Pinnacol Assurance Company	562,968	511,601	-9.1
7	Employers Insurance Group	559,653	470,416	-15.9
8	West Virginia Employers' Mutual Ins Co	702,564	420,764	-40.1
9	PMA Capital Insurance Group	376,992	408,389	8.3
10	SAIF Corporation	591,516	408,323	-31.0
	Total Workers' Compensation Composite [1]	**$16,987,000**	**$14,569,000**	**-14.2**

(1) 103 Groups and Unaffiliated Single Companies (Including State Funds)
Source: A.M. Best

Exhibit 4

U.S. Workers' Compensation – A.M. Best Composite[1] Combined Ratio Components (2007-2008)

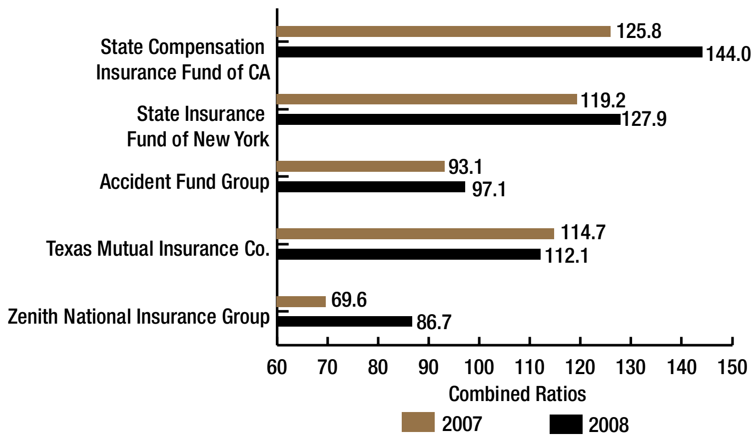
	2007	2008
Pure Loss Ratio	62.7	61.6
Loss-Adjustment Expense (LAE) Ratio	14.6	16.4
Loss & LAE Ratio	77.3	78.0
Underwriting Expense Ratio	23.8	27.0
Policyholder Dividend Ratio	5.4	5.8
Combined Ratio (Reported)	**106.5**	**110.8**

(1) 103 Groups and Unaffiliated Single Companies (Including State Funds)
Source: A.M. Best

Exhibit 5

U.S. Workers' Compensation – Combined Ratios for Top 5 Carriers in A.M. Best Composite[1] (2007-2008)

Ranked by 2008 net premiums written.



(1) 103 Groups and Unaffiliated Single Companies (Including State Funds)
Source: A.M. Best

Exhibit 6

U.S. Workers' Compensation – A.M. Best Composite[1] Change in Policyholders' Surplus (2007-2008)

($ Billions)

	2007	2008	Year/Year % Change
Beginning Policyholders' Surplus (PHS) at Prior Year End	$22.6	$25.1	11.0
Net Income	2.3	0.9	-62.4
Unrealized Capital Gains/(Losses)	0.1	(1.8)	-2,725.7
Contributed Capital	0.3	(0.3)	-207.7
Stockholder Dividends	(0.4)	(0.3)	-30.3
Other Changes	0.2	0.3	41.3
Ending Policyholders' Surplus	25.1	23.9	-4.8
Change in PHS from Prior Year End ($)	$2.5	($1.2)	
Change in PHS from Prior Year End (%)	11.0%	-4.8%	
After-Tax Return on Surplus (ROE)	9.8%	3.6%	

(1) 103 Groups and Unaffiliated Single Companies (Including State Funds)
Note: Figures may not add due to rounding.
Source: A.M. Best

declining approximately 4.8% to $23.9 billion in 2008. The decline in surplus was driven primarily by $1.5 billion in underwriting losses and $1.8 billion in unrealized investment losses. Before 2008, the composite's five-year compounded annual growth rate was nearly 15.0% through 2007, due in large part to a steady stream of investment gains and relatively favorable underwriting results in 2005 and 2006.

The composite's overall profitability measures continued to deteriorate in 2008, as the annualized after-tax return on equity fell to 3.6%, down sharply from 9.8% in 2007 and its high of 15.7% in 2005. A.M. Best expects the workers' compensation composite's performance measures to be pressured through the remainder of 2009 and well into 2010, amid weak economic conditions, sustained competitive market pressures, medical cost inflation, further decreases in premium volume and the continued volatility in the financial markets. Additionally, unlike in past cycles, expense management will be paramount to insurers as they face the prolonged impact of eroding prices and significant declines in top-line growth – without the benefit of meaningful growth in investment income. Management will need to balance costs associated with maintaining quality employees and required improvements to technological platforms.

Workers' Comp Line of Business

A.M. Best data show that NPW in the workers' comp line of business fell for the third consecutive year in 2008, declining approximately 12.0% to $39.7 billion, far greater than the 2.0% decrease experienced by the overall U.S. property/casualty industry. NPW for the workers' comp line has declined nearly 20% since it reached its high of $48.6 billion in 2005. As with the A.M. Best workers' compensation composite, the decline in NPW for the line has been driven primarily by reductions in premium rates, a highly competitive environment, lower exposure levels and rising unemployment. A good portion of the decline in premium volume came from California and Florida, which accounted for approximately 23.0% of all U.S. workers' comp direct premiums written (DPW) in

2008. Collectively, DPW for these two states fell nearly 18.0% to $9.9 billion in 2008, down from $12.1 billion in 2007. While most lines of business have stabilized over the past 12 months, workers' comp rates continue to decline, albeit more slowly than in earlier years. Further contributing to the decline in premiums are reduced exposures related to the escalating unemployment rate, which is expected to exceed 10% by year-end 2009. While job losses have been widespread across all major industries, large declines have been concentrated in manufacturing, professional and business services, and construction.

As of year-end 2008, the top five workers' comp insurance groups/companies by NPW were Liberty Mutual Insurance Companies, American International Group (AIG), Travelers Group, Hartford Insurance Group and the State Compensation Insurance Fund of California. After years of maintaining the top spot, AIG fell to second place in 2008, with NPW declining approximately 25% as the conglomerate sought to re-establish itself in the market. A number of the top 25 workers' comp carriers, which make up more than 70% of total workers' comp NPW, also reported a decrease in the line, with 18 carriers reporting decreased net writings from year-end 2007. W.R. Berkley Group reported the most notable decrease in written premium of 34.2%, followed by SAIF Corp. (-31.0%), Berkshire Hathaway Insurance Group (-29.7%), Zurich Financial Services NA Group (-29.1%) and State Compensation Insurance Fund of California (-26.7%). Farmers Insurance Group reported the most notable increase in NPW in 2008 of 21.8%, driven by the acquisition of the rights to assume and access renewals on Zurich North America Commercial's Small Business Solutions book of business.

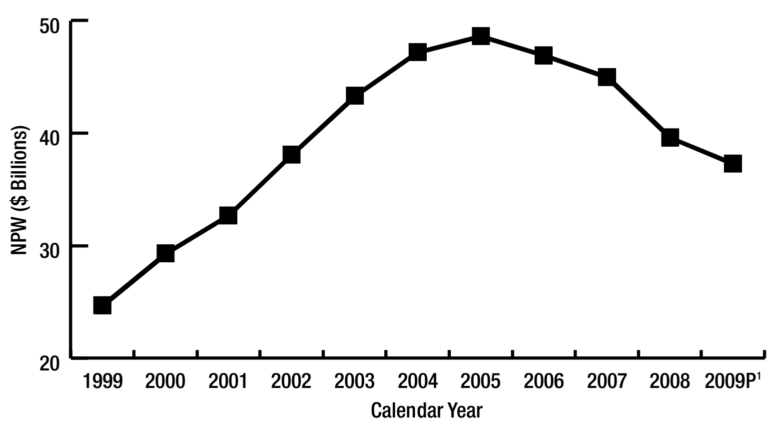
While the underwriting results for the A.M. Best workers' compensation composite deteriorated sharply, the year-over-year underwriting performance of the workers' comp line of business fared much better. According to A.M. Best data, the workers' comp line of business reported a calendar-year combined ratio of 104.4 in 2008, up only slightly from 103.6 in 2007, but up sharply from the recent low of 98.5 reported in 2006. Both the workers' comp line of business and the workers' compensation composite are projected to deteriorate throughout 2009 and well into 2010.

Legislative Reforms

Over the past half decade, a number of states have enacted meaningful workers' comp reforms. These reforms have favorably impacted those states' workers' comp markets, resulting in lower premiums and reduced loss costs and frequency trends. The earlier years of these reforms helped limit the growth rates of loss costs through the management of medical and indemnity portions of workers' comp claims, all while improving workplace safety and focusing on return-to-work programs. Additionally, the reforms have resulted in significant declines in several medical costs, such as physical therapy, chiropractic utilization and outpatient facility fees. However, in more recent years, medical-related expenses started to outpace the decline in claims frequency and reform-related pricing adjustments, causing the workers' comp industry to record an underwriting loss in each of the past two years. While there is concern that the benefit of these reforms may be scaled back, A.M. Best expects the intent of these recent reforms will largely hold and prevent the market from generating losses at the level experienced in the late '90s.

Exhibit 7

U.S. Workers' Compensation – Line of Business Net Premiums Written (1999-2009P[1])



(1) P = Projected
Sources: Best's Statement File Supplement - Insurance Expense Exhibit (IEE) - P/C, US; State Insurance Fund NY Annual Statement

Exhibit 8

U.S. Workers' Compensation – Line of Business Top 10 Writers (2008)

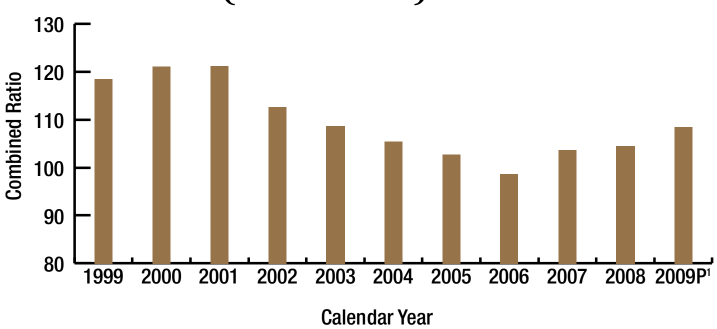
Ranked by 2008 workers' comp net premiums written.

Rank	Group/Unaffilated Single Company	2007 Workers' Comp NPW ($000)	2008 Workers' Comp NPW ($000)	Year-over-Year % Change	2008 Market Share
1	Liberty Mutual Insurance Companies	$5,071,378	$4,819,893	-5.0	12.2%
2	American International Group	6,261,355	4,701,022	-24.9	11.9%
3	Travelers Group	2,300,615	2,488,602	8.2	6.3%
4	Hartford Insurance Group	2,382,609	2,405,007	0.9	6.1%
5	State Compensation Insurance Fund of CA	2,272,842	1,666,499	-26.7	4.2%
6	State Insurance Fund NY (WC)	1,719,136	1,355,121	-21.2	3.4%
7	Zurich Financial Services NA Group	1,484,610	1,052,695	-29.1	2.7%
8	CNA Insurance Companies	998,618	963,987	-3.5	2.4%
9	Accident Fund Group	816,121	864,301	5.9	2.2%
10	Chubb Group of Insurance Companies	825,958	781,653	-5.4	2.0%
	Total Workers' Compensation	**$44,966,544**	**$39,649,463**	**-11.8**	**53.4%**

Sources: Best's Statement File Supplement - Insurance Expense Exhibit (IEE) - P/C – U.S.; State Insurance Fund NY Annual Statement

Exhibit 9

U.S. Workers' Compensation – Line of Business Combined Ratio (1999-2009P[1])



(1) P = Projected
Souce: Best's Statement File Supplement - Insurance Expense Exhibit (IEE) - P/C; State Insurance Fund NY Annual Statement

Exhibit 10

U.S. Workers' Compensation – Rate Changes in Key Markets (2004-2009)

(%)

	California	Florida	New York
1/1/2004	-14.9	0.0	-
7/1/2004	-7.9	-	-
10/1/2004	-	-	0.8
1/1/2005	-2.2	-4.0	-
7/1/2005	-18.0	-	-
10/1/2005	-	-	7.4
1/1/2006	-15.3	-13.4	-
7/1/2006	-16.4	-	-
10/1/2006	-	-	1.1
1/1/2007	-9.5	-12.5	-
7/1/2007	-14.2	-	-
10/1/2007	-	-	-20.5
1/1/2008	0.0	-18.4	-
10/1/2008	-	-	-5.0
1/1/2009	5.0	-18.6	-
10/1/2009	-	-	5.3

Source: State Insurance Departments

Following are three states that had significant reforms:

California

California remains the workers' compensation industry's largest market and accounted for 16.2% of the total industry's DPW in 2008. Since California is an open-rate state, insurers are free to set their own rates. Thus far in 2009, most companies have filed for rate increases in the mid-single-digit to teens range, which is above the California Department of Insurance's (DOI) approved 5% increase effective Jan. 1, 2009, but much lower than the Workers' Compensation Insurance Rating Bureau's (WCIRB) recommendation of 16% effective Jan. 1, 2009 and 23.7% effective July 1, 2009. In August, the WCIRB approved a rate filing with a 22.8% increase in the claims cost benchmark to be effective Jan. 1, 2010. Most of the WCIRB's latest requested rate increase reflects rising costs of medical care. The balance is related to decisions by the Workers' Compensation Appeals Board with respect to the Almaraz, Guzman and Ogilvie cases, which take the position that the American Medical Association guidelines are rebuttable under certain conditions in establishing permanent disability (PD) ratings. These decisions currently are up for reconsideration.

Driven by the impact of state legislative reforms, DPW in California has plunged approximately 53% since most of the legislative reforms were implemented in 2004, and the state's loss ratio significantly improved in 2005 and 2006. Since that time, however, the state's loss ratio has trended upward as rising medical costs outpace the decline in frequency. Despite the deterioration, California remained profitable, posting an underwriting gain, albeit smaller, in 2007 and 2008. In 2009, however, early indications are for a significant drop in profitability as reflected in first-quarter results of key writers in the state.

Florida

Since legislative reforms were passed in 2003, the Florida Department of Insurance (DOI) has mandated cumulative manual premium rate declines of approximately 60%, which largely has accounted for the 26% decline in DPW during this time. However, in the first quarter of 2009 the Florida DOI approved a 6.4% rate increase effective April 1, 2009, specifically to cover the expected increased legal costs stemming from the Florida Supreme Court's Emma Murray decision in the forth quarter of 2008. This decision reinstated hourly attorney fees, which have been among the largest cost drivers in the state workers' comp system. However, new legislation enacted by the state (HB 903) in May 2009 effectively reversed this decision, and as a result, the 6.4% increase also was reversed.

Despite the significant rate decreases since the reforms were implemented, the Florida workers' comp market has been favorable, with pure loss ratios in the state continuing to be among the lowest in the United States. However, policyholder dividends have seen increasing use as a competitive tool in recent years, limiting profitability and growth of surplus in this market.

New York

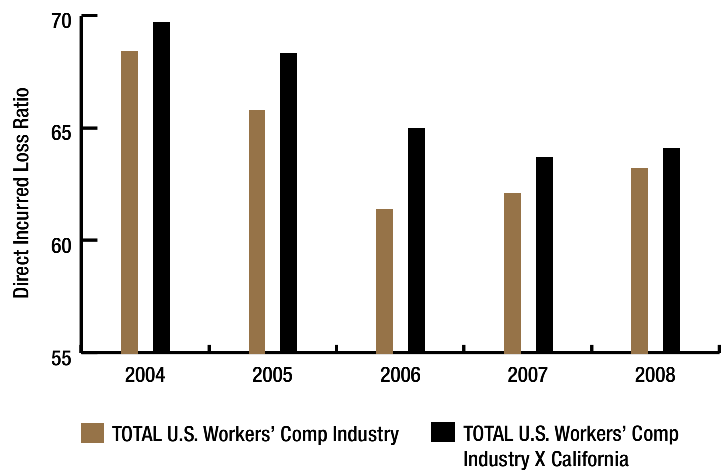
New York legislative reforms in 2007 were enacted to address several key industry concerns, such as raising maximum weekly benefits through 2011 to two-thirds of weekly earnings; resolving disputed claims and processing appeals of decisions more quickly; enhancing enforcement of workers' comp coverage; and reducing fraud. Under the reform act, the Workers' Compensation Board (WCB) was given the authority to use stop-work orders when an employer has no coverage. In 2009, premium rates are projected to fall nearly 5%, bringing the reduction in rates since the reforms were implemented to approximately 25%. The state now sets the base rate, calculated according to loss costs (claim costs only), which represents nearly 75% of the rate. Each company adds a percentage for its administrative costs. While these reforms may be beneficial to New York's workers and employers, it is still unclear whether insurers also will benefit from these reforms.

Frequency and Severity Trends

Despite widespread expectations to the contrary, the frequency of workplace injuries has continued its descent, as claim-frequency trends have remained favorable since the

Exhibit 11

U.S. Workers' Compensation – Direct Incurred Loss Ratio (2004-2008)



Souce: Best's State/Line Reports – Property/Casualty – United States

Exhibit 12

U.S. Workers' Compensation – Loss Experience in Top States (2004-2008)

($ Thousands)

State	2008 DPW	% of Total U.S.	Direct Incurred Loss Ratio 2004	2005	2006	2007	2008
California	$7,640,395	16.2%	65.3	59.0	47.9	54.7	58.2
New York	3,500,799	7.4%	74.9	77.3	73.4	68.9	72.8
Texas	2,583,666	5.5%	51.1	57.7	51.3	52.0	46.8
Illinois	2,565,396	5.4%	70.7	74.0	78.7	68.8	77.3
Pennsylvania	2,465,391	5.2%	76.5	72.5	76.4	74.3	65.9
Florida	2,260,668	4.8%	50.4	57.0	45.0	49.4	43.5
New Jersey	1,947,370	4.1%	83.4	85.4	75.1	64.3	65.3
Wisconsin	1,612,927	3.4%	66.4	80.7	66.8	64.2	65.5
North Carolina	1,402,412	3.0%	78.4	84.1	72.8	62.7	66.2
Georgia	1,232,519	2.6%	68.7	63.4	61.4	63.2	71.1
Total U.S.	**$47,146,610**	**100.0%**	**68.4**	**65.8**	**61.4**	**62.1**	**63.2**

Source: Best's State/Line Reports – Property/Casualty – United States early '90s. According to the latest report by the Bureau of Labor Statistics (BLS), there were about 4.0 million occupational injuries and illnesses, or 4.2 cases per 100 equivalent full-time workers, in the private-industry sector in 2007, a decrease from approximately 4.1 million reported in 2006. The 2007 figure was the lowest in the private-industry sector since 2002. In 2008, preliminary results indicate that claim frequency declined an additional 4.0%, according to the National Council on Compensation Insurance's (NCCI) latest review. According to NCCI, workers' comp claim frequency has fallen in all but two of the past 18 years, with 1994 and 1997 seeing very modest increases of 0.3% and 0.5%, respectively. Legislative changes; loss control and safety training in the workplace; technological advances in the workplace and attention to ergonomic design; the continued efforts of insurers, employers, workers and state regulators; and more recently, the state of the economy continue to be the driving forces behind the favorable frequency trends. Claim frequency is expected to continue its descent in 2009, as it generally declines during economic recessions.

In contrast, the severity of claims continues to rise, due primarily to increasing indemnity and medical cost trends. In 2008, NCCI estimates that the average indemnity cost of a claim increased 5.0% to $21,000, while the medical portion of the average claim continued to exceed the cost of indemnity, increasing an estimated 6.0% to $26,000. According to NCCI, medical costs now make up about 58% of total loss costs, whereas 20 years ago, approximately 54% of total lost costs were indemnity related. While reform measures in the workers' comp system have eased severity trends,

Exhibit 13

U.S. Workers' Compensation – Loss & ALAE Reserve Adequacy[1]

($ Billions)

Year	Estimated Reserve Deficiency	Estimated Deficiency Due to Discount	Deficiency/ (Redundancy) Excluding Discount
2008	9.0	16.0	(7.0)
2007	6.0	14.5	(8.5)
2006	6.3	14.9	(8.6)

(1) A.M. Best estimates made at year-end 2006, 2007 and 2008.

as witnessed in California and Florida in recent years, A.M. Best expects the severity of workers' comp claims to continue its upward trend over the long run, due to the sustained increases in indemnity and medical claim costs, as well as inflation.

Loss-Reserve Development

The workers' comp line represents the largest portion of the U.S. property/casualty industry's net loss reserves, representing approximately 23% of the total at year-end 2008. The ultimate costs of workers' comp claims are very difficult to estimate because of the uncertainties associated with their long tail, including such factors as the ongoing and possibly increasing need for medical care; long-term inflation in medical and pharmaceutical costs; the duration of disability; life expectancy; and benefits for dependents. Medical costs for decades have grown at a faster pace than the overall consumer price index (CPI). In prior calendar years, a number of workers' comp insurers were impacted by adverse loss-reserve development in underpriced business written from 1998-2001 during the last soft market; rising medical-cost inflation; increases in the utilization of medical services; and failure to properly reserve for the pricing shortfalls when establishing ultimate loss picks. While modest adverse loss-reserve development on these older accident years is still evident, it has been more than offset by favorable development from the most recent accident years.

A.M. Best estimates that the commercial lines segment's core reserve position was deficient by $14.5 billion at year-end 2008, and the workers' comp line was deficient by an estimated $9.0 billion, up from an estimated $6.0 billion in 2007. Included in this 2008 figure was approximately $16.0 billion of statutory discount, indicating that the workers' comp line would have been redundant by approximately $7.0 billion without the discount. A.M. Best remains concerned that a number of companies continue to prematurely release workers' comp loss reserves pertaining to more recent accident years to enhance current-year underwriting results, leaving open the potential for adverse development on these accident years and reduced profitability in future calendar years. A.M. Best expects this current trend of insurers releasing workers' comp reserves in more recent accident years to continue through 2009; however, the cushion has eroded, and the level of loss-reserve deficiency in the workers' comp line will continue to increase. Additionally, any rollback of reforms potentially could expose reserves to sizable strengthening actions, the magnitude of which depends on whether changes are made prospectively or retrospectively.

Terrorism Risk Insurance Program Reauthorization Act (TRIPRA)

On Dec. 26, 2007, then-President George W. Bush signed into law the Terrorism Risk Insurance Program Reauthorization Act of 2007 (TRIPRA), extending the federal "backstop" for terrorism risks through Dec. 31, 2014. TRIPRA eliminated the distinction between domestic and foreign terrorism. For workers' comp exposures located in the United States, the passage of TRIPRA has temporarily reduced A.M. Best's concerns about the U.S. government's long-term commitment to a federal role; however, it is not a permanent solution. While A.M. Best gives credit for TRIPRA protection when evaluating companies' overall capitalization, a stress test continues to be performed for those writing terror-exposed lines to identify those insurers that depend excessively on federal protection. Given some push by President Obama in recent months for reducing the protection offered by TRIPRA, this stress test for terrorism exposures may become the standard method well before TRIPRA expires in 2014. A.M. Best will continue to monitor any changes in federal protection to evaluate insurers' capital at risk for these types of exposures, as well as how companies incorporate these risks into their overall risk management practices.

Outlook

The workers' comp market's results historically have been more volatile than those of most other lines of business, with selected states reporting even wider swings in results. While A.M. Best believes the workers' comp line of business will not experience the same level of losses it did in the late '90s, the segment still faces a great number of challenges over the near term, including the economic pressures that are constricting top-line growth and generating expense pressures; challenges to state reforms; increasing loss-cost trends; and ongoing competitive market conditions as the market struggles to maintain underwriting discipline. While there appear to be early signs of rates stabilizing in the marketplace, most indicators suggest challenging market conditions and competition will be sustained in the workers' comp line through the remainder of 2009 and well into 2010, albeit less intense. Given the delay in price changes, stabilization of rates and potential impacts of reform on pricing likely will not benefit insurers until 2011.

In addition, difficult economic conditions will continue to have a major impact on the workers' comp line through declining payrolls and falling premium volume, as unemployment is expected to remain high until at least 2010. While A.M. Best expects NPW in the workers' comp line to decline approximately 6.0% and the combined ratio to deteriorate above 108.0 in 2009, these results quickly could erode further should management turn its back on underwriting and pricing discipline and prudent reserving. The ability to react quickly to the dynamics of this cyclical market will distinguish those companies that survive the latest round of demands on the industry relatively unscathed and those that face ratings pressure over the near term.

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A.M. Best Company
Ambest Road
Oldwick, New Jersey 08858
Phone: (908) 439-2200
Fax: (908) 439-3296
www.ambest.com

A.M. Best Europe Ltd.
12 Arthur Street, 6th Floor
London, UK EC4R 9AB
Phone: (44) 20 7626 6264
Fax: (44) 20 7626 6265
www.ambest.co.uk

A.M. Best Asia-Pacific Ltd.
Unit 4004 Central Plaza
18 Harbour Road
Wanchai, Hong Kong
Phone: (852) 2827-3400
Fax: (852) 2824 -1833
www.ambest.com.hk