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The View From Above
Problems with Pricing Excess D&C

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SCOR
The Art & Science of Risk

Who Am I?

- Andy James!
- Senior Underwriter – Professional Indemnity, SCOR, London
- Catlin 2011-2015, ANV 2015-2017, SCOR 2017-
- Brief stints at XL and AmTrust
- Focus on non-homogenous, large corporate risks at SCOR, not volume business
- Excess only
- All professions but around half are engineers and D&C
- Questions at the end please
- Apologies for the maths, but I promise some magic!

So What *Is* The Market Standard Methodology?

James Villas

- Premium UK housebuilder that builds individually designed, low-rise houses
- Total contract values of up to £1m per unit/development
- Turnover of the company is £100m
- All design is subbed out
- Standard risk management protocols and claims history
- Buys primary £5m and £5m xs £5m on a standard market wording with a normal level of deductible
- Market standard methodology: 'always price the primary first'

		Primary £1m Premium
Turnover	100,000,000	
Notional Fee %	5.0%	
Notional Fee	5,000,000	
Rate	0.5%	25,000
Country, Wording, Deductible, Risk Management, Claims Multipliers	1.0	25,000
ILF		0.3
£5m x £5m Premium		7,500

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Show Me Another One!

SIR AARON MCWILLIAMS

- Troublesome, mid-sized, Jack-the-lad contractor building energy from waste plants in the USA
- Total contract values of around £25m
- As with James Villas:
  - Turnover of the company is £100m
  - All design is subbed out
  - Standard risk management protocols and claims history
  - Buys primary £5m and £5m xs £5m on a standard market wording with a normal level of deductible

		Primary £1m Premium
Turnover	100,000,000	
Notional Fee %	5.0%	
Notional Fee	5,000,000	
Rate	7.5%	375,000
Country Multiplier	2.0	750,000
Wording, Deductible, Risk Management, Claims Multipliers	1.0	750,000
ILF		0.5
£5m x £5m Premium		375,000

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And What's Wrong With That?!

- Nothing…and lots
- Time for some magic!

INTER-SIRJ

	Primary £1m Premium		James Villas		Sir Aaron	
Turnover	200,000,000		100,000,000		100,000,000	
Notional Fee %	5.0%		5.0%		5.0%	
Notional Fee	10,000,000		5,000,000		5,000,000	
Rate	4.0%	400,000	0.5%	25,000	7.5%	375,000
Country Multiplier	1.5	600,000	1.0	25,000	2.0	750,000
Wording, Deductible, RM, Claims Multipliers	1.0	600,000	1.0	25,000	1.0	750,000
Adjusted Rate	6%		0.5%		15%	
ILF		0.4		0.3		0.5
£5 x £5m Premium		240,000		7,500		375,000

- **The broader the work performed, the less reliable a model's pricing is, because models use too many averages**
- **Excess layers are disproportionately affected by this because of a singular ILF applying to all work**

What Else Is Wrong With Market Rating Methodology?

- What about construction values?

	P£1m Premium			James Villas		Sir Aaron	
Turnover	150,000,000			50,000,000		100,000,000	
Notional Fee %	5.0%			5.0%		5.0%	
Notional Fee	7,500,000			2,500,000		5,000,000	
Rate	5.17%	387,500		0.5%	12,500	7.5%	375,000
Country Multiplier	1.667	645,833		1.0	12,500	2.0	750,000
Wording, XS, RM, Claims Multipliers	1.0	645,833		1.0	12,500	1.0	750,000
ILF	0.4			0.3		0.5	
£5 x £5m Premium	258,333	7.6%		3,750		375,000	
Last Year's Price	240,000			7,500		375,000	
Average TCV TY			1,000,000			75,000,000	
Average TCV LY			1,000,000			25,000,000	
£50 x £50m Price	258,333	7.6%		3,750		375,000	
Last Year's Price	240,000			7,500		375,000	

	1st to 2nd XS	2nd to 3rd XS	3rd to 4th XS	4th to 5th XS
Average	99%	90%	83%	97%

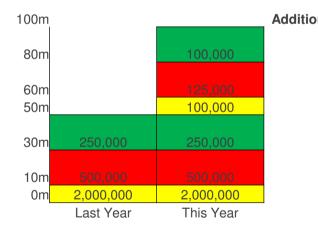- Don't forget about 'gearing'

What Else Is Wrong With Market Rating Methodology?

- Do notional fees really work for excess layers?

	Normal Broker Rate	Suggested 100x100 Rate
Full D&C	10.00%	10.00%
Design only	100.00%	100.00%
Pure construction	1.00%	1.00%
Subbed D&C	5.00%	9.75%

Covered by SPPI	Removed	Included
'Pass Through Costs'	Removed	Included
Homes (in house design)	5.00%	Removed

- And remember that the primary underwriter's interest and yours and not always aligned

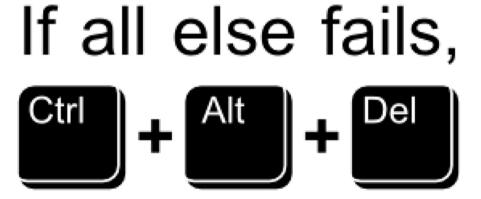|	Additional Premium Required	Rate Decrease
	40%	-28.6%
	25%	-20.0%
	5%	-4.8%

So, What's The Solution?

- Steal what other classes do!
- Price each contract, simulate the losses based on the actual structure and period

Contract Name/Number	Total Contract Value	Contract Start Date	Contract End Date	Insured's Role(s)	Joint Venture Share	Type of Project	Location	Insured Elsewhere?	Cap on Liability?	Liability Cap of Subbed Design?
1	100,000,000	01/01/2014	01/01/2020	Lead Contractor	50%	Bridge	USA	10,000,000	50,000,000	10,000,000
2	5,000,000	01/01/2016	01/06/2020	Lead Contractor	N/A	Offices - Low Rise	UK	N/A	5,000,000	N/A
3	20,000,000	01/01/2015	01/01/2021	Lead Contractor	N/A	Substation	UK	N/A	10,000,000	N/A

Policy Period (Days)	365

SIR	100,000
SIR Agg	500,000
Maintenance SIR	25,000

Limit	Attachment
5,000,000	-
5,000,000	5,000,000

Number of Simulations	100,000

PRICE!

- But, it's a lot of work

- Any shortcuts?...

If all else fails, Ctrl + Alt + Del

Summary and Shortcuts

Problem	Shorcut Solution(s)
Models use too many averages, which distorts the pricing	Break firms into 'chunks' of similar work, particularly very high risk and low risk work
	Use your judgment, not just what the model tells you!
	Use burn-rating where possible (but don't forget to allow for changes in risk and claims inflation!)
ILFs are too blunt a tool for considering contract values	Chunks will help
	Considering gearing could give you an edge, given market dynamics
	Don't let claims loads be limited to the loss-hit layers
	Use your judgment, not just what the model tells you!
Notional fees are a subjective, and probably don't work for XS layers in their current form	Treat subbed fees as in-house
	Don't exclude projects covered under singles or other spurious exclusions from the notionals
	Do exclude low risk work-types, if not rating them separately
Primaries drive the program, which might not be in the excess layers' best interests	The old addage might not be correct; underwrite each layer distinctly