IMCC WORKSHOP

The State of the Surety Industry…

…And The Fate of Reclamation Bonds

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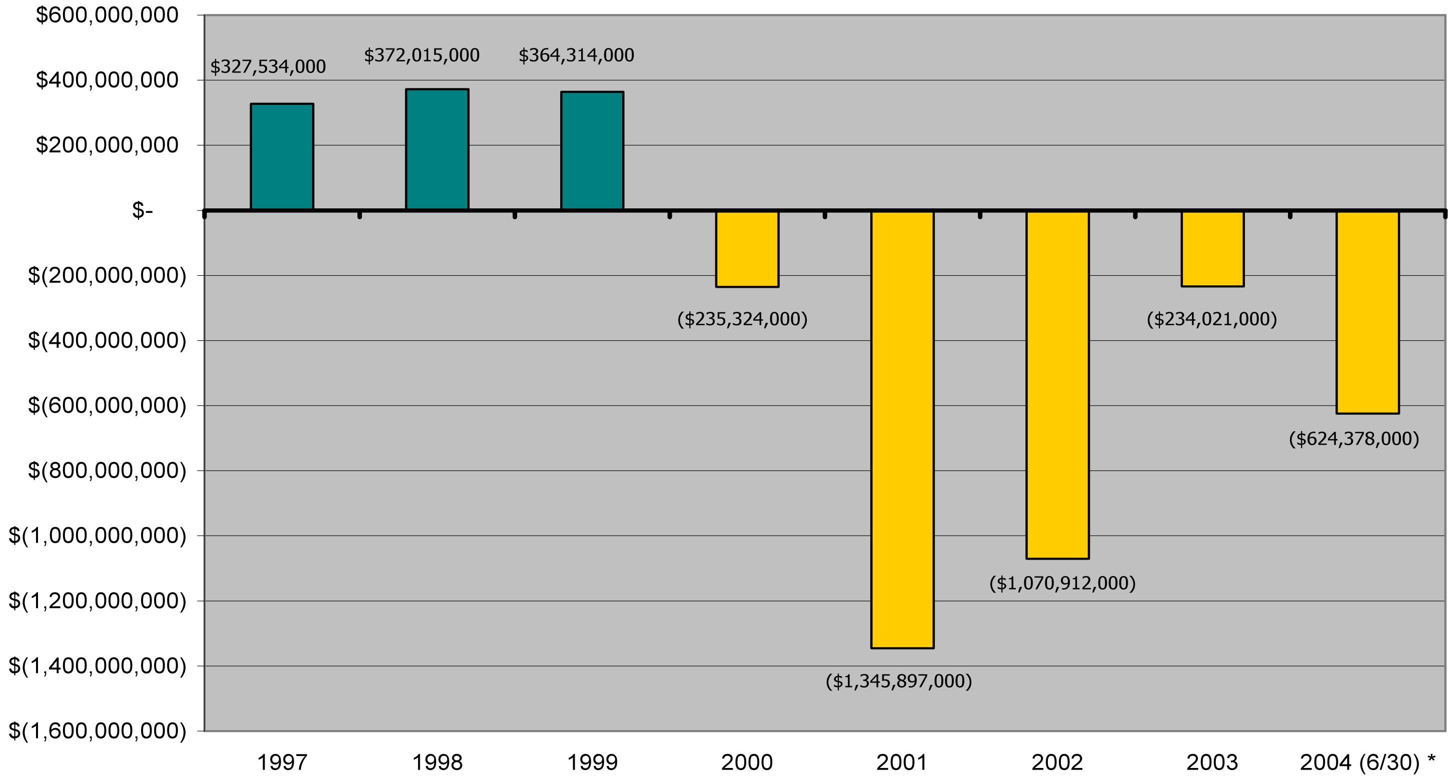
Surety Industry Pre-Tax Underwriting Profit (Loss) 1997 - 2004



Total Underwriting Loss Since 1997: **$2,446,668,500**

** 2004 data is through June 30 and includes assumptions for LAE and Underwriting Expenses*

Source: The Surety Association of America

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Gross Written Premium
15-Year Industry View

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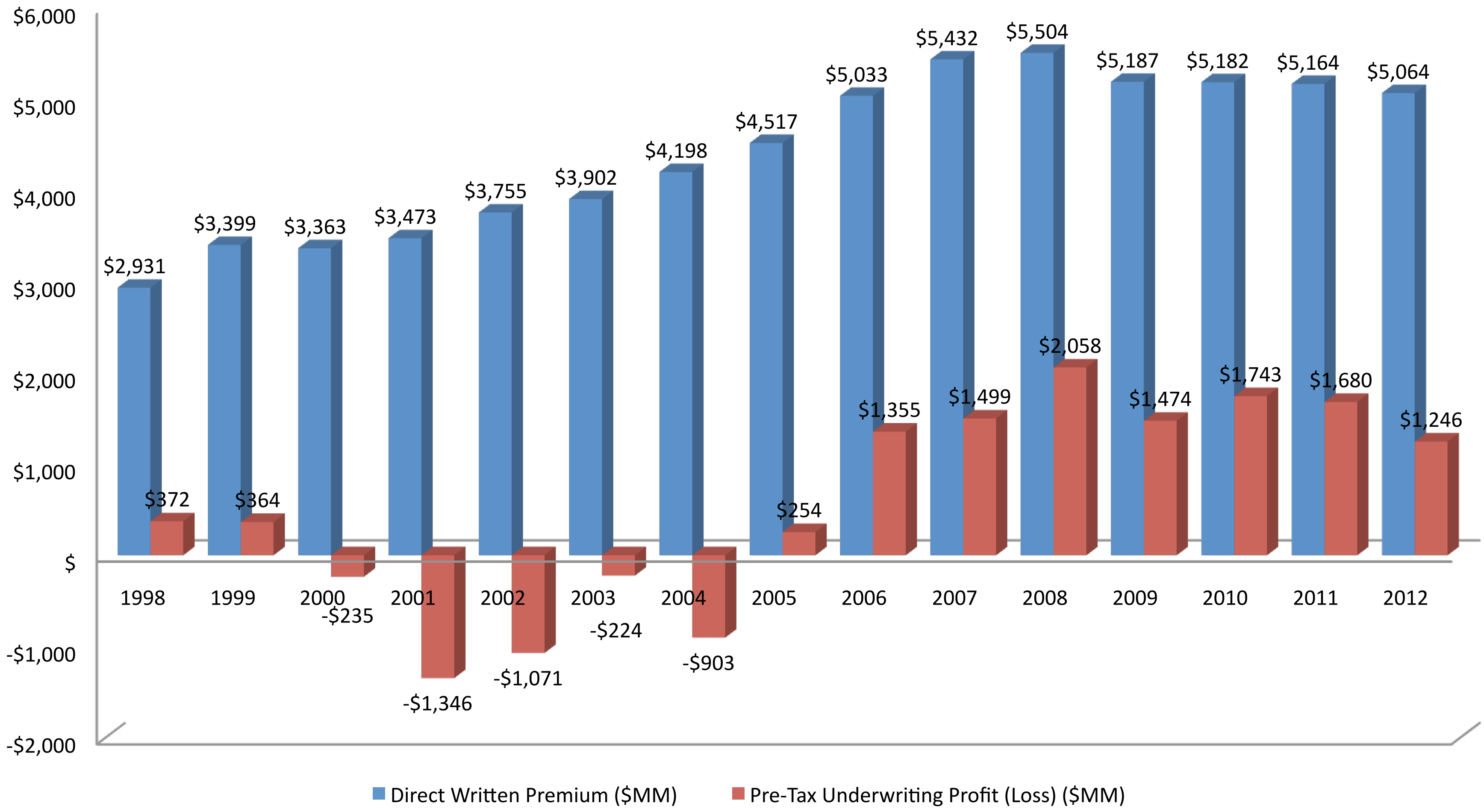

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Surety Industry
Return On Capital – 1998 - 2012

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Year	Direct Written Premium	Return Expected (Low)	Return Expected (High)	Pre-Tax Underwriting Profit (Loss)
2012	$5,064	$668	$1,519	$1,246
2011	$5,164	$682	$1,549	$1,680
2010	$5,182	$684	$1,555	$1,743
2009	$5,187	$685	$1,556	$1,474
2008	$5,504	$727	$1,651	$2,058
2007	$5,432	$717	$1,630	$1,499
2006	$5,033	$664	$1,510	$1,355
2005	$4,517	$596	$1,355	$254
2004	$4,198	$554	$1,259	-$903
2003	$3,902	$515	$1,171	-$224
2002	$3,755	$496	$1,126	-$1,071
2001	$3,473	$458	$1,042	-$1,346
2000	$3,363	$444	$1,009	-$235
1999	$3,399	$449	$1,020	$364
1998	$2,931	$387	$879	$372
1998-2012	**$66,105**	**$8,726**	**$19,832**	**$8,265**

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Reclamation Bond Results
1998 - 2011

Year	State	Written Premium	Earned Premium	Losses Incurred	Loss Ratio	Industry Loss Ratio
2011	COUNTRYWIDE	79,555,589	73,527,758	(1,264,801)	-1.72%	13.47%
2010	COUNTRYWIDE	68,991,651	69,128,567	(11,180,539)	-16.17%	13.37%
2009	COUNTRYWIDE	67,996,666	65,034,251	1,860,011	2.86%	19.44%
2008	COUNTRYWIDE	63,183,190	57,936,595	(14,772,632)	-25.50%	12.84%
2007	COUNTRYWIDE	53,915,396	52,881,181	3,340,457	6.32%	18.85%
2006	COUNTRYWIDE	51,362,656	50,998,739	(18,505,668)	-36.29%	16.02%
2005	COUNTRYWIDE	46,143,833	61,632,213	10,514,846	17.06%	39.84%
2004	COUNTRYWIDE	78,714,546	73,529,557	27,230,076	37.03%	60.03%
2003	COUNTRYWIDE	70,336,714	65,727,475	24,549,743	37.35%	49.05%
2002	COUNTRYWIDE	56,308,587	47,812,624	13,074,633	27.35%	69.85%
2001	COUNTRYWIDE	37,720,461	34,334,209	11,832,731	34.46%	82.53%
2000	COUNTRYWIDE	29,430,603	29,188,495	12,465,065	42.71%	46.33%
1999	COUNTRYWIDE	23,149,309	28,808,454	8,006,799	27.79%	29.32%
1998	COUNTRYWIDE	31,039,255	30,811,460	21,212,370	68.85%	25.61%

Reclamation	***757,848,456***	***741,351,578***	***88,363,091***	***11.92%***
Surety - All	***61,041,480,000***	***59,261,297,000***	***19,184,526,000***	***32.37%***

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Reclamation Bond Results
Top 20 States By Bond Premium
1995 - 2011

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	Premium Written	Premium Earned	Losses Incurred	Loss Ratio
KENTUCKY	$98,098,668	$94,798,582	$26,158,411	27.59%
WEST VIRGINIA	$91,600,667	$88,800,626	$7,750,866	8.73%
PENNSYLVANIA	$84,339,454	$77,000,859	$9,022,991	11.72%
WYOMING	$70,162,838	$67,672,914	$12,092	0.02%
COLORADO	$45,225,866	$42,916,929	$336,188	0.78%
MONTANA	$43,434,809	$40,131,388	$18,529,154	46.17%
VIRGINIA	$40,629,134	$39,524,769	$211,002	0.53%
ILLINOIS	$33,481,102	$31,407,108	$145,530	0.46%
NEVADA	$27,403,184	$26,085,639	$4,551,110	17.45%
CALIFORNIA	$26,455,954	$24,549,206	$1,259,357	5.13%
INDIANA	$26,291,502	$26,327,331	$846,454	3.22%
OHIO	$25,346,478	$24,707,038	$5,406,220	21.88%
ARIZONA	$24,294,016	$24,003,727	$1,312,109	5.47%
TEXAS	$22,134,129	$22,044,111	$0	0.00%
FLORIDA	$19,376,359	$18,528,530	$667,760	3.60%
UTAH	$15,317,811	$14,710,945	$1,189,401	8.09%
NEW YORK	$13,904,222	$13,156,978	$285,488	2.17%
ALABAMA	$11,541,244	$10,782,937	$8,983,900	83.32%
WASHINGTON	$10,660,925	$9,298,790	$7,104	0.08%
NEW MEXICO	$10,408,740	$9,692,329	$0	0.00%
ALL OTHER	*$100,912,481*	*$96,915,201*	*$5,891,742*	*6.08%*
Grand Total	**$841,019,583**	**$803,055,937**	**$92,566,879**	**11.53%**

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Reclamation Bond Results

By Mining Sector
2005 - 2011

	General	Hard Rock	Coal	Aggregates	
	933	980	981	982	Grand Total
2005	-$1,910,406	$3,373,223	$39,604,799	$5,076,217	$46,143,833
2006	-$105,139	$3,529,355	$40,911,939	$7,026,501	$51,362,656
2007	$15,045	$3,662,305	$43,659,264	$6,578,782	$53,915,396
2008	$588,513	$5,891,991	$48,908,412	$7,794,274	$63,183,190
2009	-$17,171	$9,477,701	$50,314,192	$8,221,944	$67,996,666
2010	-$534	$10,942,381	$50,031,382	$8,018,422	$68,991,651
2011	-$3,240	$13,022,040	$58,010,486	$8,526,303	$79,555,589
Grand Total	-$1,432,932	$49,898,996	$331,440,474	$51,242,443	$431,148,981

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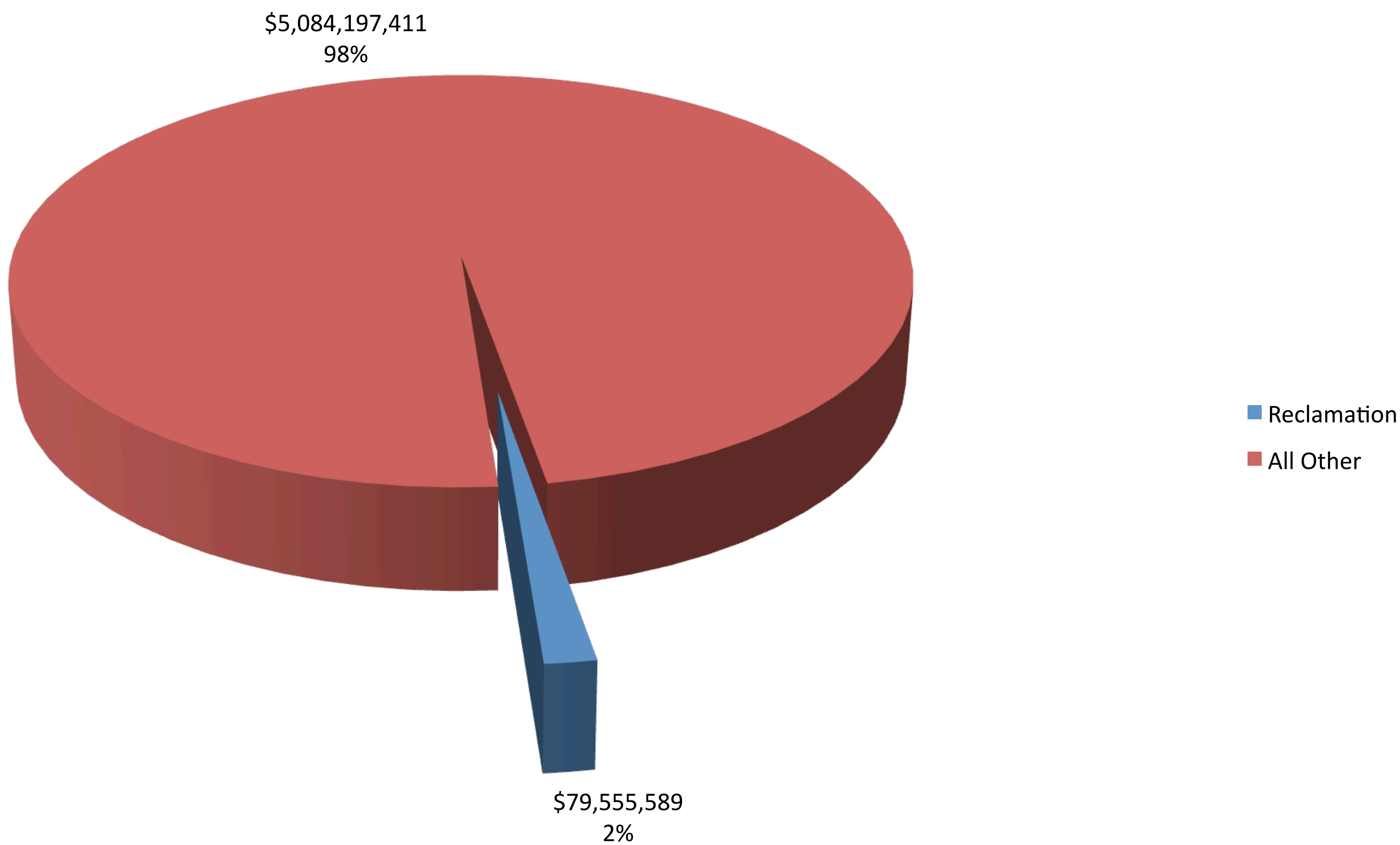
Mining Industry Premium



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Reclamation Bond Results
Summary

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- Participating in reclamation bond programs has generally been profitable for the sureties
- Sector support has expanded beyond coal. Hard rock mining currently has surety as a viable solution for reclamation security
- Despite state variances in loss ratio, mine location tends not to be a major underwriting factor today
- Reclamation bond premium represents 1.6% of total industry premium. This is up from 1.0% in 2005, but still an extremely small percentage of industry revenue

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Reclamation Bond Results
Behind The Numbers

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- A Surety's first responsibility is to prequalify the bond principal relative to its ability to perform
  - Would results be the same if every operator that wanted a bond received a bond?
- Sureties often take collateral to mitigate risk
  - Would results be the same if every operator received unsecured capacity?
- Sureties often take early steps to mitigate exposure when an operator is not performing?
  - Would results be the same if no action was taken prior to a financial default?

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Reclamation Bond Results

Has Surety Underwriting Improved?

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PAST

- Many surety companies did not have the expertise to evaluate mining companies
- These companies avoided reclamation bond risk
- Reinsurers often included reclamation bond prohibitions in their treaties

TODAY

- Many companies still do not have the expertise to evaluate mining companies
- More and more, these companies are participating on mining risks
- Reinsurer restrictions for reclamation bond risks are much less common

"How do they get the energy out of the coal?"

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Reclamation Capacity
Will Capacity Tighten?

- Will new entrants stay in the space if loss ratios worsen?
  - Dramatic shake out in coal space underway
  - Commodity price swings in Hard Rock space could impact operators on the margin
  - Private equity ownership changes the dynamic of the workout
- Will reinsurers tolerate bankruptcies and/or increased loss activity?
- Will senior management respond to increased financial defaults in the sector by exiting a sector that represents 2% of the industry?

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FMS – Circular 570 (T-Limit)
Are All Sureties Created Equal

[Code of Federal Regulations]
[Title 31, Volume 2, Parts 223]
[Revised as of July 1, 1997]
[CITE: 31CFR223.1-22]

31 CFR, Part 223
REGULATIONS GOVERNING SURETY COMPANIES DOING BUSINESS WITH THE UNITED STATES

Sec. 223.1 Certificate of authority.

The regulations in this part will govern the issuance by the Secretary of the Treasury of certificates of authority to bonding companies to do business with the United States as sureties on, or reinsurers of, recognizances, stipulations, bonds, and undertakings, hereinafter sometimes called obligations, under the provisions of the Act of July 30, 1947 (61 Stat. 646, as amended; 6 U.S.C. 6-13), and the acceptance of such obligations from such companies so long as they continue to hold said certificates of authority.

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Sec. 223.3 Issuance of certificates of authority.

(a) If, from the evidence submitted in the manner and form herein required, subject to the guidelines referred to in Sec. 223.9 the Secretary of the Treasury shall be satisfied that such company has authority under its charter or articles of incorporation to do the business provided for by the Act referred to in Sec. 223.1, and **if the Secretary of the Treasury shall be satisfied from such company's financial statement** and from any further evidence or information he may require, and from such examination of the company, at its own expense, as he may cause to be made, that such company has a capital fully paid up in cash of not less than $250,000, **is solvent and financially and otherwise qualified to do the business provided for in said Act**, and is able to keep and perform its contracts, he will, subject to the further conditions herein contained, issue a certificate of authority to such company, under the seal of the Treasury Department, to qualify as surety on obligations permitted or required by the laws of the United States to be given with one or more sureties, for a term expiring on the last day of June next following. The certificate of authority shall be renewed annually on the first day of July, so long as the company remains qualified under the law and the regulations in this part, and transmits to the Assistant Commissioner, Comptroller by March 1 each year the fee in accordance with the provisions of Sec. 223.22 (a)(3).

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Sec. 223.9 Valuation of assets and liabilities.

In determining the financial condition of every such company, **its assets and liabilities will be computed in accordance with the guidelines contained in the Treasury's current Annual Letter to Executive Heads of Surety Companies**. However, the Secretary of the Treasury may value the assets and liabilities of such companies in his discretion. Credit will be allowed for reinsurance in all classes of risks if the reinsuring company holds a certificate of authority from the Secretary of the Treasury, or has been recognized as an admitted reinsurer in accord with Sec. 223.12.

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Sec. 223.10 Limitation of risk.

Except as provided in Sec. 223.11, ***no company holding a certificate of authority shall underwrite any risk on any bond or policy*** on behalf of any individual, firm, association, or corporation, whether or not the United States is interested as a party thereto, ***the amount of which is greater than 10 percent of the paid-up capital and surplus of such company, as determined by the Secretary of the Treasury***. That figure is hereinafter referred to as the underwriting limitation.

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Notes

(b) ***The Underwriting Limitations published herein are on a per bond basis. Treasury requirements do not limit the penal sum (face amount) of bonds which surety companies may provide.*** However, when the penal sum exceeds a company's Underwriting Limitation, the excess must be protected by co-insurance, reinsurance, or other methods in accordance with 31 CFR Section 223.10, Section 223.11. Treasury refers to a bond of this type as an Excess Risk. When Excess Risks on bonds in favor of the United States are protected by reinsurance, such reinsurance is to be effected by use of a Federal reinsurance form to be filed with the bond or within 45 days thereafter. In protecting such excess risks, the underwriting limitation in force on the day in which the bond was provided will govern absolutely. For further assistance, contact the Surety Bond Branch at (202) 874-6850.

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Sec. 223.11 Limitation of risk: Protective methods.

The limitation of risk prescribed in Sec. 223.10 may be complied with by the following methods:

(a) Coinsurance
(b) Reinsurance
(c) Other methods

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FMS – Circular 570 (T-Limit)
Other Independent Measures Of Financial Strength

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- A.M. Best – Claims Paying Ratings
- S&P/ Moody's – Debt Ratings

Note: Many small to mid-size companies do not have S&P or Moody's ratings. That is not, in and of itself, an indication of weak financial condition.

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