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2017 US EDUCATION INSURANCE MARKET UPDATE WEBCAST

March 23, 2017

Jean Demchak, Paul Sherbine, Mark Turkalo, TJ Campisi, Ken Simek

MARSH & McLENNAN COMPANIES

Jean Demchak, Managing Director Global Education and Public Entity Practice Leader

Jean has a career-long focus on higher education and the public entity sector, with 34 years of industry experience. She has been with Marsh for 30 years and is the senior relationship officer for all education and public sector accounts. Jean is responsible for identifying and responding to the emerging issues facing schools and public entity clients and developing and customizing specialized services to meet their needs. She serves as liaison with the marketplace as well as key organizations in the higher education industry.

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Agenda

- ➢Introduction/panel overview.
- ➢The market information resources/insurer financial review.
- ➢Casualty market including professional liability update:
  - ✓ Higher education.
  - ✓ Primary and secondary schools.
- ➢Property market update (higher education and primary and secondary).
- ➢The Affordable Care Act and the impact on the education sector.
- ➢Q&A.

Marsh Panel Overview

Paul Sherbine, Managing Director
Market Information Group

Paul is the leader of Marsh's Market Information Group and is responsible for the analysis of the insurers Marsh clients use worldwide. He assists clients in assessing the relative strengths or weaknesses of various insurers when structuring their programs. He also makes oral and written presentations to clients and prospects on the importance and methodology of insurer financial analysis.

Paul has been the featured speaker to industry trade groups and other interested parties on Marsh's Market Information Group and the financial standing of the insurance industry in general. Prior to joining Marsh in 1986, Paul was a financial analyst with A.M. Best Company.

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Marsh Panel Overview

Mark Turkalo, Senior Vice President
Education and Public Entity Placement Leader

Mark is a senior placement specialist exclusively responsible for placement of all new and renewal business for the education sector that includes public and independent K-12 schools, vocational and technical schools, community and state colleges, as well as, private and public higher education institutions.

Mark's responsibilities include insurance risk evaluations for Marsh's education clients as well as determination of the best possible risk transfer mechanisms. His background includes placement public entity specialty industry programs. Prior to joining Marsh in 1993, Mark held several underwriting positions for 10 years, specializing in national accounts, cash flow programs, captives and other risk financing techniques.

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Marsh Panel Overview

Thomas (TJ) Campisi, Vice President
US Property Practice

In his role as a property placement specialist, TJ provides clients with advice on program design, placing and servicing programs for global risk management accounts.

Among his areas of expertise are providing solutions for clients in higher education on layered and quota share programs, captive use, and alternative risk finance.

TJ joined Marsh in 2006 and is a located in Marsh's Chicago office.

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Marsh Panel Overview

Ken Simek, Partner
Mercer Consulting

Ken is a partner in Mercer's Chicago office and has been with Mercer for over 20 years. He has more than 25 years of substantial consulting and engagement management experience in human resources strategy, compensation strategy and design, benefits strategy, benefits administration and process, human resources technologies, and benefits outsourcing.

He leads Mercer's Higher Education Industry Practice and is responsible for coordinating, managing, and leading Mercer's client and market strategy for all higher education clients and consulting services. Mercer has over 400 higher education clients that they provide a wide range of consulting services for. Ken also spearheads a private university networking group, which consists of 10 institutions. Throughout the year this group engages in issues analysis, information sharing, and socialization.

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2016 Industry Results
Running on Empty

Paul Sherbine

2016 US Results

- Combined ratio of 101%.
- 2.7% increase in net premiums.
- Policyholders’ surplus of $719 billion, up $29 billion from 2015.
- Net income of $43 billion, down 23% from prior year period.
- Catastrophes added 4.9 points to combined ratio in 2016, as compared to 3.5 points in 2015.
- Net investment income up $600 million to $48 billion, while realized gains fell about $2 billion to $8 billion and unrealized capital gains reported of $11 billion as opposed to losses of $21 billion in 2015.
- Personal lines net premiums written up 5% to $303 billion, with commercial lines increasing 1% to $192 billion.
- Personal lines surplus is about $289 billion, while commercial lines surplus is $292 billion.

Source: A.M. Best

2016 Results Deeper Dive

- While personal lines are expected to report an underwriting loss, commercial lines should remain profitable in 2016, with an estimated gain of $2 billion.
  - Expectations for 2017 point to an underwriting loss but still report operating profits.
- Workers' compensation, benefitting from rate increases in the 2011 to 2014 accident years, has led profitability for commercial insurers.
  - Since then, however, rate movement have gone down and has turned negative recently, pointing to deterioration in the future.
- Commercial auto has been a loss leader despite being one of the smaller lines by premium.
  - Economic trends and higher frequency and severity of losses have led to recent rate increases.
- Catastrophe losses should be about $6 billion — 50% more than 2015, but not a rate changer.

Investment Results Continue to Drag Along The Bottom

- Commercial lines net investment income to fall about $1 billion in 2016 to $22.7 billion, with 2017 estimates showing a slight decline.
  - Recent stock rise may change that estimate, which could feed more capital into an already robust industry position.
- Rising investment portfolio has mitigated lower reinvestment yields. Invested assets rose about 4% in 2016.
- Realized gains showed a good increase and will probably be higher than estimates due to stock rally in fourth quarter.
  - With recent stock rally and projected Fed move on interest rates, some insurers shortening portfolio duration.
  - Fairfax plans to shorten to one year to take advantage of rising rates.
- 2017 should be a much different ball game due to business euphoria over projected tax cuts fueling market rally.
  - Any logjam in Congress on tax cuts could negate that by year end.

Mergers Still On The Forefront in 2016 and 2017

- AIG-LAC Eastern Europe Ops/Fairfax
- AWAC/ Fairfax
- Arch/United Guaranty (AIG mortgage insurer)
- Endurance/Sompo
- Ironshore/Liberty Mutual

Merger Breakdowns

- AIG/Fairfax deal: AIG pulls out of countries with little local business. Fairfax see opportunities to expand global footprint.
- AWAC/Fairfax: AWAC seeks broader footprint and access to capital. Fairfax continues to expand footprint, increase invested assets.
- Arch/AIG United Guaranty: AIG seeks cash to dividend to shareholders. Arch seeks broader footprint in mortgage insurance, now over a third of revenue.
- Endurance/Sompo: Endurance seeks large parent for growth and acquisitions. Sompo seeks to greatly expand non-Japanese revenue base and management expertise.
- Ironshore/Liberty Mutual: Ironshore seeks to rid negative rating implications of Chinese parent. Liberty seeks expansion in specialty lines.

What about 2017?

- Mergers expected to continue for many reasons.
  - Revenue expansion.
  - Diversification of earnings — both in coverages and geographies.
  - Smaller players at competitive disadvantage. Bigger means better.
  - Groups with recent difficulties need to streamline operations and concentrate on what they do well.
  - Expense reduction — not a major consideration before, but maybe now.

It Wouldn’t Be A Webinar Without AIG

- 2016 plan seemed to be going along well.
- Icahn rep and Paulson added to board.
- On track for $25 billion in shareholder dividends/buybacks.
- Expense reductions through senior management exodus on track.
- Subsidiary sales generate good liquidity.
- Reductions in unwanted business going as planned.
- Quota share on casualty book with Swiss Re reduces leverage, buttresses capital.
- Reunderwriting of book continues at expected pace.
- Ratings affirmed following acquisition by all rating agencies by end of June 2016.

January 20, 2017 — Another Surprise

- AIG announces adverse loss development reinsurance deal with National Indemnity (Berkshire Hathaway).
- Following year-end actuarial review, findings show continuous and significant reserve development on casualty book across all major lines.
- Adverse development cover meant to stop the bleeding going forward to meet 2017 target profit goals.
- In short: AIG gives Berkshire $10 billion, Berkshire gives AIG $20 billion in cover. AIG to share $5 billion on quota share to make deal $25 billion excess of $25 billion in retained reserves.
- AIG uses Berkshire balance sheet to protect PC results and capital position.

Rating Agency Reactions

- Fitch puts under review with negative implications citing pricing adequacy.
- Moody's considers deal credit positive for insurance operations. Leaves rating at A2 Stable.
- S&P affirms insurer financial strength rating at A+ Stable. Lowers parent debt rating to BBB+. Considers the deal positive for insurance operations.
- A.M. Best puts A Stable rating under review with negative implications due to pricing, reserving, and enterprise risk concerns.
- Following release of results, Fitch affirms A rating with negative outlook.
- Best expected by AIG to finalize review by end of April.
- Of Marsh's major markets, none are rated A+ by S&P, A2 by Moody's, and lower than A by Best.

2016 Full Results Released

- Reserve increase is $5.6 billion, much higher than analyst expectations.
  - Workers' compensation has $1.8 billion; excess casualty $1.1 billion; primary casualty $800 million; every other line $400 million each.
  - Already in the money on Berkshire deal. Berkshire has over $4 billion of this amount.
- 242% combined ratio for 4th quarter.
  - Still, balance sheet protection going forward good for policyholders.
  - Not as much protection for shareholders.
- Analysts not confident in management's ability to turn company around.
- Board silent until March 9, 2017:
  - Hancock resigns, will stay until successor found.
  - Wall Street is happy.
  - AIG needs PC person to turn this around.

Casualty Education Market Update

Mark Turkalo

Education Segments

- Colleges and Universities
  - Public
  - Private
  - Doctoral Research Institutions
- Primary and Secondary
  - Public K-12 School Districts
  - Independent Schools
- Other Educational Services
  - For-Profit Institutions
  - Education-Related Human/Social Services
  - Charter Schools
  - Vocational Schools
  - Technical Schools

Higher Education

- Overall, stable but not soft — focus on coverage, service, and price for all core exposures in the primary, lead, and excess layers.
- Severity loss trends continue: Wrongful death claims, discrimination, drowning, law enforcement, registered student organizations, fraternities and sororities, special events on and off campus.
- Disciplined underwriting: Concern regarding athletics, concussion management, use of drones, student transport, and sexual assault claim activity.
- Internship programs, student volunteers, EMTs and professional services (financial, legal, engineering programs).
- Summer sports camps and cert requirements for SML coverage.

Higher Education

- Transportation service providers — MVR reviews.
- Study abroad programs growing with increased litigious legal environment.
- International travel:
  - Local underlying policies DIC/DIL capacity.
  - Chaperones, host families (background checks).
  - Defense Base Act.
  - USL&H: Research vessels.
  - Presumptive injury claims rising in workers' compensation for police and fire.
- Excess workers' compensation rates have stabilized; two-year agreements and policies are available.
- More excess capacity is available.

Higher Education

- Drones: Expansion to provide coverage for UAVs less than 55 lbs. for other than educational/research purposes with no sublimit on the excess.
- Impact of recent National Labor Relations Board decision granting employment status to graduate students and unionization.
- Immunity caps and status of limitations.
- Increased attention to ERM.
- Markets willing to manuscript coverage.
- Emergency preparedness and crisis response: coverage triggers differ among carriers (number of days to report).
- Exclusive benchmarking: EPEDS.

Higher Education: Key Coverage and Issues to Consider

- USL&H self-insured status:
  - Excess workers' compensation policies can provide coverage but only pay state benefits.
  - For Federal benefits (and to avoid possible fines), either apply to be self-insured for USL&H or obtain a guaranteed cost USL&H policy ($10,000 minimum premium).
- Lead Capacity: Few markets provide more than $10 million in limits.
  - UE: $40 million general liability and $40 million educators legal liability.
  - AIG/Lexington: Up to $25 million, but with TBI/CTE exclusion.
- TBI/CTE: What is the future?
  - Lexington, Navigators: Excluding TBI/CTE and requiring minimum attachment points on excess.
- Decline of the for-profit market segment (Corinthian, ITT, Accreditation): Is this the end?
- More marketing? More questions.

Other Education Risks: Market Concerns

- Alcohol/binge drinking.
- Active shooter.
- Campus construction risk.
- Background screenings.
- Campus violence, crisis communications, and disaster planning.
- E-Risk (cyber/network security liability).
- Daycare centers on campus.
- Environmental.
- Minors on campus.
- Pandemics.
- Protests on campus.
- Vehicle operations (15-passenger vans) and fleet safety.
- Autonomous vehicles.
- Sanctuary campuses.
- Student rights (FERPA).

Higher Education Indicators

- **General liability** rates continue to increase due to severity, averaging in the low single- to sometimes low double-digit range. Exposure from athletics, student assaults, Title IX , 15-passenger van related accidents, date rapes, fan violence, excessive force by police, pool-related fatalities, suicides, sexual abuse, hazing, and violent acts on and off campus continue to rise.
- **Traumatic brain injury (TBI)** exposure will continue to be underwritten separately and given more scrutiny by all markets regarding intercollegiate football and other sports. A supplemental warranty application remains mandatory and all institutions are required to complete a concussion awareness training or education programs for coaches, athletic trainers, and medical staff.
- **Sexual molestation** claims stemming from childcare operations, summer sport camps, campus housing, fraternities, sororities, and athletics continue to discourage many insurers from offering these essential coverages in the primary, lead, and excess layers. Monoline coverage is available on a limited basis.
- **Drones (UAVs)** policy wording has been expanded to clarify and provide coverage grants in this area focused on educational and research activities.

Higher Education Indicators

- **Educators legal liability (T&O, E&O and EPL)**: After a few years of stabilization, claims in the nonprofit education segments are increasing in severity; retentions and pricing may need to adjusted. Title IX, discrimination and reverse discrimination, harassment, and failure to promote claim development continues. Court cases are pending for special education needs and transgender accommodation.

- **Cyber** exclusions addressing bodily injury and physical damage arising out of access or disclosure of confidential or personal information. Amendments are available. These type of damages were not intended to be covered by general liability as emotional distress claims remain the greatest concern. AIG and Beazley are competitive.

- The **excess workers' compensation** market remains tight, but large rate increases have diminished. Ten years of loss experience is still required and increased retentions are still being considered. Presumptive injury claims for police and fire are prevalent. Multiyear agreements and policies are available to signal a potential softening environment.

Insurance/Reinsurance Marketplace

- Allianz
- Allied World
- Arch
- Aspen
- AXIS
- Beazley
- Berkley
- Berkshire
- Brit
- Chubb
- Church Mutual
- CNA
- Crum & Forster
- Endurance
- Everest
- Genesis
- Great American
- GuideOne
- Hanover
- Hartford
- Hiscox
- Ironshore/Liberty & LIU
- Lexington
- Markel
- Midlands
- Midwest Employers
- Munich Re
- Navigators
- Old Republic
- OneBeacon
- Philadelphia
- PMA
- QBE
- Safety National
- Sentry
- Swiss Re
- Travelers
- United Educators
- Westchester
- XL Catlin
- Zenith
- Zurich

Higher Education Rates

- General liability: Flat to 7% increase.
- Automobile liability: Flat to 5% increase.
- Workers' compensation: 5% decrease to 5% increase.
- Excess workers' compensation: 5% decrease to 10% increase.
- Educators legal liability: Flat to 7% increase.
- Lead umbrella: Flat to 10% increase.
- Excess umbrella: Flat to 5% increase.
- Foreign package: Flat to 5% increase.

Primary and Secondary Education

- Stable but not soft.
- More carriers interested.
- Integrated programs and pools dominate public K-12.
- Guaranteed cost options.
- Capacity available up to $10 million.
- Budget restrictions, reduction in staff = various results.
- Overall poor underwriting experience = volatility.

Primary and Secondary Education

- Rates:
  - General liability: Flat to 5% increase.
  - Automobile liability: Flat to 5% increase.
  - Law Enforcement liability: Flat to 10% increase.
  - School board legal liability: Flat to 5% increase.
  - Lead umbrella: Flat to 10% increase.

- Conclusion:
  - Become acquainted with alternative forms and coverage.
  - Balance the value drivers between coverage, price, and service.

Property Education Market Update

TJ Campisi

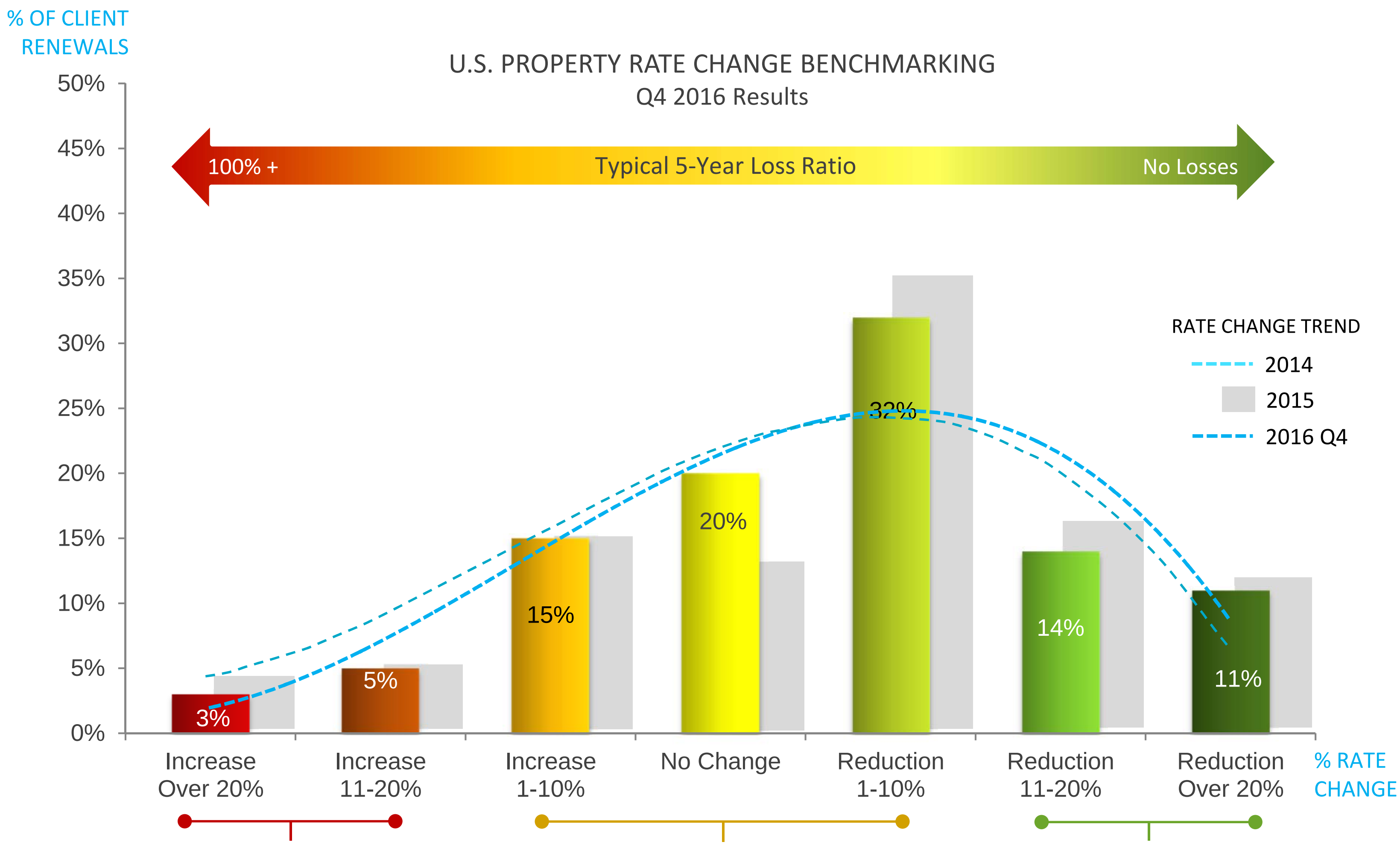
Property Market Conditions

- Favorable trends:
  - Highly competitive market.
  - Low impact losses.
  - More than $719 billion in policyholder surplus.
  - Broadened coverage.
  - Opportunity to lock into long-term contracts.

- Trends to monitor:
  - Insurer reorganizations and focus on expense management.
  - Merger and acquisition activity.
  - Company changes in risk appetite.

Key Market Update

- FM Global: Strong 2016 performance, with 84% combined ratio.
- AIG: Capacity now up to $2.5 billion.
- Zurich: Working capacity between $750 million and $1 billion.
- Travelers: Stable performance and capacity. Working capacity up to $1 billion.
- Swiss Re: Targeting growth in public entity/higher education.
- Chubb: Working capacity up to $650 million.
- Affiliated FM: Generally focused on risks under $500,000 in premium.
- The Hartford: Working capacity of $500 million, can build up to $1 billion.
- CNA: Working capacity of $500 million, can build up to $1 billion.



Highlights

- Property market pricing softness continued in Q4.
- 57% of Q4 renewals achieved a rate decrease – this was down from Q3 where 60% of renewals had a rate decrease.
- The average change for all companies was a 5.2% rate reduction.
- Despite the favorable pricing environment, 23% of renewals bound with rate increases.
- 68% of clients purchased terrorism cover.

Significant INCREASE Examples

- Clients with adverse loss history.
- Challenging risks – e.g., frame construction.

Nominal Change Examples

- Clients that received a meaningful rate decrease in the prior year(s).
- Insured's in industries where low rates are historically prevalent (e.g., health care).

Significant DECREASE Examples

- Large quota share programs.
- Clients with significant exposure to natural catastrophe risks.
- Special situations – e.g., large loss rolling off of the 5-yr loss record or a large increase in values.

This information includes broad commentary about the property insurance market. Underwriters consider each risk on its own unique merits. Among many factors that may affect an insured's specific outcome are the competiveness of the current rate, account size, scope of marketing effort, risk quality, data quality, geographic considerations and intangible considerations such as insurer relationships. The data excludes renewals with increased deductibles or less limit from expiring.

Renewal Strategies

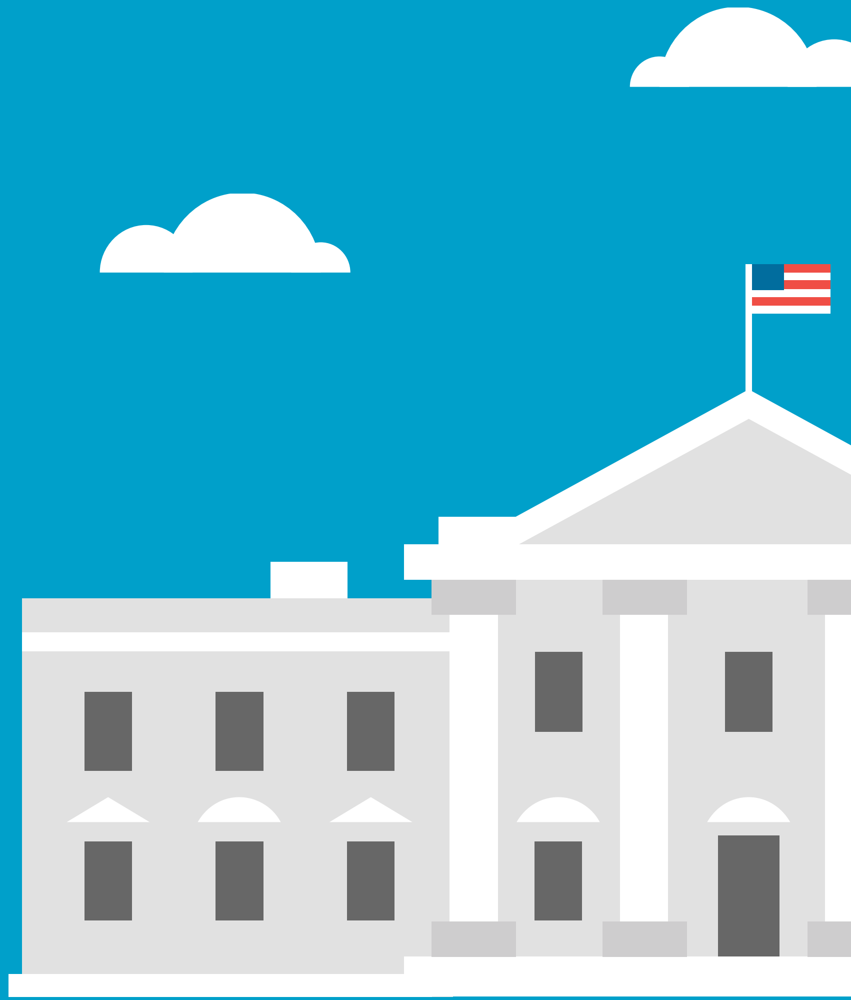
- Start early and be timely.
- Be creative and aggressive.
- Data quality is critical.
- Collect COPE information.
- Generate competition.
- Accommodate engineering surveys.
- Meetings with underwriters.

The Affordable Care Act and the Impact on the Education Sector

Ken Simek

ACA Repeal and Replace: President Trump's Positions

- Ensure Americans with preexisting conditions have access to coverage.
- Help Americans purchase coverage through the use of tax credits and expanded health savings accounts.
- Give states the resources and flexibility they need with Medicaid "to make sure no one is left out".
- Implement legal reforms to protect patients and doctors from unnecessary costs (presumably medical tort reform).
- Reduce "artificially high" cost of drugs.
- Allow sale of health insurance across state lines.

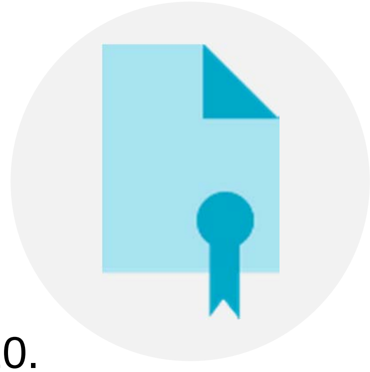


GOP's Repeal AND Replace Drive

- Congress moving to repeal, replace ACA provisions under budget "reconciliation."
  - Process allows legislation to pass Senate with simple majority.
  - Restricted to provisions that affect federal spending, revenues (taxes), and debt limit.
  - Extraneous provisions cannot be included; these need 60 Senate votes to pass.
- House, Senate GOP leaders want to move "three buckets" of reforms:
  - Include as much "repeal and replace" as possible in reconciliation bill.
  - Legislation and regulation to prevent individual market collapse.
  - Enact "replace" provisions not eligible for reconciliation with help from Democrats.
- House leaders released ACA repeal and replace budget reconciliation bills — The American Health Care Act — on March 6.
  - House leadership planning for a full House vote by the end of March.

ACA Repeal and Replace: The American HEALTH Care Act

- The “Cadillac” tax remains, although delayed from 2020 to 2026.
  - The “leaked” cap on the employee tax exclusion was not included.
  - Employer and individual mandate penalties eliminated for 2016 and later years.
    - Individuals or small groups with coverage gaps would pay 30% premium surcharge beginning as earlier as 2018.
  - Age-based tax credits starting in 2020.
    - Credits begin to phase out for those making more than $75,000 per year ($150,000 joint filers).
    - No credits for those with access to employer coverage.
    - Can be used for unsubsidized COBRA coverage.
  - Other ACA taxes repealed for years beginning after 2017.
  - HSA enhancements:
    - Increase limits to max deductible/out-of-pocket limits for HDHPs.
    - $6,550 single/$13,100 family for 2018.
  - Medicaid expansion eliminated after 2019.
  - Employer’s ACA reporting not addressed; new W-2 reporting starts in 2020.



Reconciliation: What's in the American HEALTH Care Act?

TARGETS FOR ELIMINATION	TARGETS TO MAINTAIN
• Individual mandate. • Employer mandate (including 30 hours requirement). • Exchange-based premium tax credit and cost-sharing subsidies (transition period 2017-19; elimination after 2019). • Restrictions on HSAs, FSAs (allow OTC reimbursements, eliminate FSA cap, etc.). • Requirement that tax deduction for retiree drug costs be reduced for Retiree Drug Subsidy payments. • Medical device tax, annual fee on health insurance providers, Rx fee. • Medicaid expansion (after 2019).	• Cadillac tax (delayed from 2020 to 2026). • Ban on lifetime/annual dollar limits. • Plan eligibility to age 26. • Ban on insurers charging more or denying coverage based on pre-existing conditions. • Caps on OOP expenditures. • Some form of employer reporting requirements.. • Essential benefit provisions.

Questions

*1 For Telephone Questions

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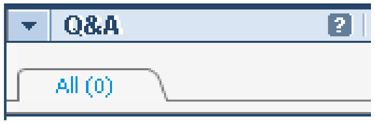
To submit a question while in full-screen mode, use the Q&A button on the bottom right-hand side of your screen.

To submit a question while in half-screen mode, use the Q&A tab on the bottom right-hand side of your screen.



<u>We are very interested in your opinion!</u>

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Please remember to take our survey when you receive the follow-up email to confirm:

- Did the presentation meet your expectations?
- Did you find it informative?
- What you would like to see covered in future presentations?