

MARKET CONDUCT  
EXAMINATION REPORT OF  
DEVELOPERS SURETY AND INDEMNITY COMPANY  
WEST DES MOINES, IOWA  
AS OF DECEMBER 31, 2009

West Des Moines, Iowa  
March 30, 2011

HONORABLE SUSAN E. VOSS  
Commissioner of Insurance  
State of Iowa  
Des Moines, Iowa

Commissioner:

In accordance with your authorization and pursuant to Iowa statutory provisions, a market conduct examination has been made of the records, business and marketing practices of

DEVELOPERS SURETY AND INDEMNITY COMPANY

WEST DES MOINES, IOWA

AS OF DECEMBER 31, 2009

at its Home Office 1603 22<sup>nd</sup> Street, Suite 200, West Des Moines, Iowa. The principal executive office of the Company is maintained at 17780 Fitch, Suite 200, Irvine, California.

INTRODUCTION

The examination report, containing applicable comments, explanations and findings, is presented herein. In general, this is a report by exception. Comments regarding practices and procedures reviewed during the examination have been omitted from the report if no improprieties were found.

SCOPE OF EXAMINATION

Developers Surety and Indemnity Company, hereinafter referred to as the "Company", was previously examined as of December 31, 2004. This market conduct examination covers the intervening period from December 31, 2004 to the close of business on December 31, 2009. It was conducted and performed solely for the Iowa Insurance Division by its examiners. A general review and survey was made of the Company's marketing operations and treatment of policyholders for statutory compliance during the stated period. Other supporting evidences have been examined and evaluated to the extent deemed necessary.

HISTORY

The Company was incorporated October 10, 1936 as the Mutual Surety Company of Iowa. Amended and Substituted Articles of Incorporation adopted October 10, 1956 changed the corporate title to State Surety Company and the structure was changed from a mutual to a stock company.

On February 1, 1995, Indemnity Company of California and affiliate Developers Insurance Company purchased all the outstanding stock of the State Surety Company. The Company was purchased as an empty shell. This transaction was approved by the Insurance Division of Iowa on January 13, 1995.

The Articles of Incorporation were amended March 10, 1995 changing the name to Developers Surety and Indemnity Company. In addition, the authorized common stock was increased to 5,000 shares with a par value of \$1,000 per share and an aggregate value of \$5,000,000.

Through restructuring of the ultimate parent, all outstanding shares of the Company were transferred to Indemnity Company of California (ICC) and all outstanding shares of ICC were transferred to Developers Insurance Company (DICO). This reorganization was effective August 29, 1997.

Indemnity Company of California made a capital contribution of \$3,865,724 to the Company on December 29, 2000. In addition, ICC paid a dividend of 100% of the Company's outstanding stock shares to Developers Insurance Company (DICO). At the same time the Company and DICO merged with the Company being the surviving entity.

#### RELATED PARTY SERVICE AGREEMENTS

The Company has underwriting management agreements in place, with its parent, Insko Insurance Services, Inc. (Insko), and affiliate, Builders Insurance Services, LLC (BIS), whereby the Company has appointed Insko and BIS to manage its insurance operations. The agreements provide for the appointment and termination of producing agents and brokers and to enter into contracts with such agents and brokers on the Company's behalf. In addition, Insko and BIS will underwrite the policies, collect premiums, issue bonds and or policies, take indemnification agreements from principals, keep all accounting and bookkeeping records, administer and adjust claims, provide office space, administer all Insurance Division matters, draft and print applications for bonds, policies and other forms and all other matters necessary for the Company to engage in business. Settlements shall be made monthly.

Insko and BIS produced written premiums in 2009 of \$50,724,480 and \$3,747,667, respectively.

The Company is responsible for the investment of surplus funds, payment of premium and income taxes and salaries of its Board of Directors, preparation of monthly, quarterly and annual statements, corporate legal fees and costs, and losses and allocated loss expenses.

#### TERRITORY AND PLAN OF OPERATION

The Company continues to expand into a national writer specializing in providing bonding coverages to developers and contractors that require subdivision, performance, contract, license and permit, and miscellaneous bonds. While a material portion of written premium is produced in California, 22%, the Company has expanded its geographical mix and has reduced its concentration in California.

The Company has a distribution network of approximately 4,500 independent producers. As of December 31, 2009, there are 19 branch offices that work with the agency force and perform marketing and underwriting functions. The regional branches are located in the following areas:

Atlanta, GA	Dallas, TX	Houston TX	San Diego, CA
Baltimore, MD	Denver, CO	Phoenix, AZ	Seattle, WA
Boise, ID	Des Moines, IA	Pittsburgh, PA	St. Pete/Tampa, FL
Charleston, SC	Ft. Lauderdale, FL	Portland, OR	Walnut Creek, CA
Chicago, IL	Glendale, CA	Sacramento, CA	

Certificates of Authority evidenced that the Company was authorized to transact business in all 50 states and the District of Columbia at December 31, 2009.

#### ADVERTISING

The Company maintains procedures for the review and compliance approval of all advertising materials. The primary advertising strategy is Company name branding directed towards the agency force.

A sample of advertising materials, utilized during the exam period, was reviewed for statutory compliance with unfair trade practices in accordance with Iowa Administrative Code 191-15.3 (507B). Materials were found to properly represent policy benefit forms or conditions and did not contain terms or expressions that are misleading or ambiguous. The Company also maintains a public website at [www.inscodico.com](http://www.inscodico.com) that contains information about the Company and the offered products.

#### PRODUCERS

Business written is produced through approximately 4,500 independent producers. Background verification and approval is completed for all new appointments and the Company performs an annual review process for proper licensing requirements. Producers must also maintain errors and omissions liability coverage.

Utilizing a written premium data file reconciled for the financial examination, a statistical sample of 46 bond files was reviewed for compliance with Iowa Administrative Code sections 507B.4(14) Unfair Trade Practices, and 191-10 (522B) Producer Appointments. No compliance issues were noted.

#### TREATMENT OF THE POLICYHOLDERS

##### Complaints

The Company has documented complaint procedures and records that are in compliance with Iowa Administrative Code 191-15.13(507B) Complaint and Business Records. All responses are reviewed and approved by a corporate manager. There are no apparent compliance trends in complaints regarding frequency and/or patterns for any specific type of complaint. No complaints were filed in the State of Iowa during the exam period.

##### Claim Practices

Claim processing and adjudication risk mitigation controls were identified and assessed as properly designed and operating effectively. A review was made of claim files for timeliness of acceptance or denial, payment of loss, and unfair claim settlement practices in accordance with Iowa Administrative Code 191-15 (507B). Utilizing a paid claim, expense and reserve data file reconciled for the financial examination, a statistical sample of 66 claim files was reviewed for prompt acknowledgement of the claim upon receiving notification. All files reviewed were found to have notification within the required statutory time period. Thirty-six paid claim transactions contained within the sample were reviewed to determine the Company's practice in the prompt payment of claims. All claims were paid within 7 days sufficient information was received and found to be in statutory compliance for prompt payment. No unfair claim settlement practices were identified.

DIRECT UNDERWRITING EXPERIENCE

<u>Classification</u>	<u>2005</u>	<u>2006</u>	<u>2007</u>
Premiums earned	\$ 47,444,312	\$ 57,302,410	\$ 62,062,229
<u>Incurred deductions</u>			
Losses incurred	\$ 9,226,604	\$ 4,581,334	\$ 8,314,788
Defense and cost containment	3,401,013	3,294,834	3,095,128
Adjusting and other expenses	1,714,000	2,867,000	2,483,000
Commission and brokerage	13,725,624	17,310,527	16,954,718
Taxes, licenses and fees	1,467,590	1,711,213	1,630,130
Other acquisition expenses	6,944,000	9,837,000	10,469,000
General expenses incurred	4,995,000	5,613,000	6,267,000
Total deductions	\$ 41,473,831	\$ 45,214,908	\$ 49,213,764
Underwriting gain (loss)	\$ 5,970,481	\$ 12,087,502	\$ 12,848,465

<u>Classification</u>	<u>2008</u>	<u>2009</u>	<u>Total</u>
Premiums earned	\$ 62,515,660	\$ 61,060,394	\$ 290,385,005
<u>Incurred deductions</u>			
Losses incurred	\$ 8,999,145	\$ 20,051,037	\$ 51,172,908
Defense and cost containment	521,545	3,024,481	13,337,001
Adjusting and other expenses	1,900,000	1,231,000	10,195,000
Commission and brokerage	17,490,164	15,406,513	80,887,546
Taxes, licenses and fees	1,320,221	1,533,559	7,662,713
Other acquisition expenses	12,222,000	11,601,000	51,073,000
General expenses incurred	6,072,000	4,278,000	27,225,000
Total deductions	\$ 48,525,075	\$ 57,125,590	\$ 241,553,168
Underwriting gain (loss)	\$ 13,990,585	\$ 3,934,804	\$ 48,831,837

Expressed in the ratio of incurred deductions to premiums earned the percentages are:

	<u>2005</u>	<u>2006</u>	<u>2007</u>	<u>2008</u>	<u>2009</u>	<u>Average</u>
<u>Incurred deductions</u>						
Losses incurred	19.4%	8.0%	13.4%	14.4%	32.8%	17.6%
Defense and cost containment	7.2	5.7	5.0	0.8	5.0	4.6
Adjusting and other expenses	3.6	5.0	4.0	3.0	2.0	3.5
Commission and brokerage	28.9	30.2	27.3	28.0	25.3	27.9
Taxes, licenses and fees	3.1	3.0	2.6	2.1	2.5	2.6
Other acquisition expenses	14.7	17.2	16.9	19.6	19.0	17.6
General expenses incurred	10.5	9.8	10.1	9.7	7.0	9.4
Total deductions	87.4%	78.9%	79.3%	77.6%	93.6%	83.2%
Underwriting gain (loss)	12.6%	21.1%	20.7%	22.4%	6.4%	16.8%

DIRECT UNDERWRITING EXPERIENCE BY STATE

State	Five-Year Average Earned Premium	Five-Year Operating Ratio	2009 Earned Premium	2009 Operating Ratio
Alabama	\$ 378,311	81.7%	\$ 419,543	76.4%
Alaska	105,343	75.7	261,612	92.9
Arizona	1,171,625	65.8	1,271,221	71.9
Arkansas	106,325	137.1	170,869	202.7
California	17,284,731	74.2	13,804,710	94.8
Colorado	1,162,742	100.4	1,811,175	83.0
Connecticut	108,191	90.4	247,698	114.7
Delaware	86,675	64.4	99,987	51.8
District of Columbia	85,597	63.2	85,503	58.5
Florida	6,326,532	108.2	7,398,551	85.3
Georgia	2,171,490	117.0	2,088,620	200.4
Hawaii	860,043	64.9	1,218,235	57.3
Idaho	406,808	64.6	452,835	51.7
Illinois	1,034,650	80.8	1,213,824	65.2
Indiana	527,070	106.9	341,778	100.6
Iowa	293,635	164.9	414,923	178.3
Kansas	350,180	84.8	301,221	135.3
Kentucky	125,297	116.8	167,751	268.0
Louisiana	284,877	87.8	577,435	83.5
Maine	206	603.5	1,031	192.8
Maryland	2,081,527	73.4	1,818,609	116.7
Massachusetts	194,692	108.0	536,851	117.4
Michigan	205,315	9.8	259,936	70.4
Minnesota	360,405	69.2	411,371	55.5
Mississippi	204,011	68.2	167,414	55.4
Missouri	292,953	158.2	404,719	4.8
Montana	232,723	67.2	315,547	75.4
Nebraska	136,067	73.1	200,658	15.6
Nevada	1,368,490	54.6	1,137,958	59.3
New Hampshire	36,787	65.8	40,189	63.9
New Jersey	685,172	72.8	818,336	94.8
New Mexico	415,782	96.1	522,858	60.8
New York	564,906	62.1	584,670	46.5
North Carolina	513,796	157.1	701,456	308.1
North Dakota	77,313	69.3	120,499	62.7
Ohio	693,781	100.6	1,092,178	103.9
Oklahoma	478,026	53.3	246,287	75.6
Oregon	4,457,053	64.8	4,567,960	74.9
Pennsylvania	1,558,638	95.2	2,092,395	90.0
Rhode Island	5,965	106.9	22,676	95.6
South Carolina	244,471	131.1	455,344	140.5
South Dakota	51,497	70.8	72,134	70.1
Tennessee	309,023	96.5	412,272	222.8
Texas	3,033,620	103.1	3,560,515	70.1
Utah	698,880	90.4	1,284,027	126.8
Vermont	4,540	82.5		
Virginia	1,214,306	82.5	1,092,670	78.7
Washington	4,758,300	68.4	5,294,578	76.1
West Virginia	86,542	117.9	118,945	223.5
Wisconsin	140,891	70.3	168,648	97.5
Wyoming	101,201	70.2	190,172	68.3
Total	\$ 58,077,001	83.2%	\$ 61,060,394	93.6%

Due to the downturn in the real estate market the Company experienced a slight increase in incurred losses during 2009. A significant portion of gross direct claim payments are returned to the Company in the form of salvage and subrogation recoveries and reinsurance cessions.

CONCLUSION

Acknowledgment is hereby made of the cooperation and assistance extended by the officers and employees of the Company during this examination.

In addition to the undersigned, the following examiners participated in the examination and preparation of this report: Randy Guzman, Marvin Minor and Bob Wong, Iowa Senior Insurance Examiners.

Respectfully submitted,

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VIRGINIA R. WEST, CFE  
Examiner-in-Charge  
Insurance Division  
State of Iowa