

SAFETY INSURANCE GROUP INC  
Form 10-K  
March 14, 2011

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**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**  
Washington, D.C. 20549  
**FORM 10-K**

(Mark One)

☒ **ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE  
SECURITIES EXCHANGE ACT OF 1934**

**For the fiscal year ended December 31, 2010**

**Or**

☐ **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES  
EXCHANGE ACT OF 1934**

**For the transition period from to  
Commission file number 000-50070**

**SAFETY INSURANCE GROUP, INC.**

(Exact name of registrant as specified in its charter)

**Delaware**  
(State or other jurisdiction of  
incorporation or organization)

**13-4181699**  
(I.R.S. Employer Identification No.)

**20 Custom House Street, Boston, Massachusetts**  
(Address of principal executive offices)

**02110**  
(Zip Code)

**(617) 951-0600**  
(Registrant's telephone number, including area code)

Securities registered pursuant to Section 12(b) of the Act:

**Title of each class**  
Common Shares, \$0.01 par value per share

**Name of each exchange on which registered**  
NASDAQ Global Select Market

Indicate by check mark whether the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes ☐ No ☒

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Indicate by check mark whether the registrant is not required to file reports pursuant to Section 13 of Section 15(d) of the Act. Yes ☐ No ☒

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes ☒ No ☐

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulations S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes ☐ No ☐

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (§ 229.405 of this chapter) is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. ☒

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See definitions of "large accelerated filer," "accelerated filer," and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer ☐      Accelerated filer ☒      Non-accelerated filer ☐      Smaller reporting company ☐  
(Do not check if a  
smaller reporting company)

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes ☐ No ☒

The aggregate market value of the registrant's voting and non-voting common equity (based on the closing sales price on NASDAQ) held by non-affiliates of the registrant as of June 30, 2010, was approximately \$504,336,195.

As of March 9, 2011, there were 15,158,195 Common Shares with a par value of \$0.01 per share outstanding.

### Documents Incorporated by Reference

Portions of the registrant's definitive proxy statement for its Annual Meeting of Shareholders to be held on May 20, 2011, which Safety Insurance Group, Inc. (the "Company", "we", "our", "us") intends to file within 120 days after its December 31, 2010 year-end, are incorporated by reference into Part II and Part III hereof.

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*In this Form 10-K, all dollar amounts are presented in thousands, except average premium, average claim and per claim data, share, and per share data.*

**PART I.**

**ITEM 1. BUSINESS**

**General**

We are a leading provider of private passenger automobile insurance in Massachusetts. In addition to private passenger automobile insurance (which represented 68.7% of our direct written premiums in 2010), we offer a portfolio of property and casualty insurance products, including commercial automobile, homeowners, dwelling fire, umbrella and business owner policies. Operating exclusively in Massachusetts and New Hampshire through our insurance company subsidiaries, Safety Insurance Company ("Safety Insurance"), Safety Indemnity Insurance Company ("Safety Indemnity") and Safety Property and Casualty Insurance Company ("Safety P&C") (together referred to as the "Insurance Subsidiaries"), we have established strong relationships with independent insurance agents, who numbered 783 in 908 locations throughout Massachusetts and 31 locations in New Hampshire during 2010. We have used these relationships and our extensive knowledge of the Massachusetts market to become the second largest private passenger automobile carrier, capturing an approximate 11.4% share of the Massachusetts private passenger automobile insurance market, and the third largest commercial automobile carrier, with an 10.7% share of the Massachusetts commercial automobile insurance market in 2010 according to statistics compiled by Commonwealth Automobile Reinsurers ("CAR"). In addition, we were also ranked the 50<sup>th</sup> largest automobile writer in the country according to A.M. Best, based on 2009 direct written premiums. We were incorporated under the laws of Delaware in 2001, but through our predecessors, we have underwritten insurance in Massachusetts since 1979.

Our Insurance Subsidiaries began writing private passenger automobile and homeowners insurance business in New Hampshire during 2008 and personal umbrella business during 2009. During the years ended December 31, 2010 and 2009, the Company wrote \$2,774 and \$978 in direct written premiums, respectively, and approximately 3,300 and 1,250 policies, respectively, in New Hampshire.

**Website Access to Information**

The Internet address for our website is [www.SafetyInsurance.com](http://www.SafetyInsurance.com). All of our press releases and United States Securities and Exchange Commission ("SEC") reports are available for viewing or download at our website. These documents are made available on our website as soon as reasonably practicable after each press release is made and SEC report is filed with, or furnished to, the SEC. Copies of any current public information about our company are available without charge upon written, telephone, faxed or e-mailed request to the Office of Investor Relations, Safety Insurance Group, Inc., 20 Custom House Street, Boston, MA 02110, Tel: 877-951-2522, Fax: 617-603-4837, or e-mail: [InvestorRelations@SafetyInsurance.com](mailto:InvestorRelations@SafetyInsurance.com). The materials on our website are not part of this report on Form 10-K nor are they incorporated by reference into this report and the URL above is intended to be an inactive textual reference only.

**Our Competitive Strengths**

*We Have Strong Relationships with Independent Agents.* In 2009, independent agents accounted for approximately 78.1% of the Massachusetts automobile insurance market measured by direct written premiums as compared to only about 35.4% nationwide, according to A.M. Best. For that reason, our strategy is centered around, and we sell exclusively through, a network of independent agents, who numbered 783 (of which 2 are Exclusive Representative Producers ["ERPs"] assigned to us under regulations that were phased out April 1, 2009, as discussed below) in 939 locations throughout

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Massachusetts and New Hampshire during 2010. In order to support our independent agents and enhance our relationships with them, we:

provide our agents with a portfolio of property and casualty insurance products at competitive prices to help our agents address effectively the insurance needs of their clients;

provide our agents with a variety of technological resources which enable us to deliver superior service and support to them; and

offer our agents competitive commission schedules and profit sharing programs.

Through these measures, we strive to become the preferred provider of the independent agents in our agency network and capture a growing share of the total insurance business written by these agents in Massachusetts. We must compete with other insurance carriers for the business of independent agents.

*We Have an Uninterrupted Record of Profitable Operations.* In every year since our inception in 1979, we have been profitable. We have achieved our profitability, among other things, by:

maintaining the number of private passenger automobile exposures we underwrite from 470,221 in 2005 to 470,237 in 2010;

maintaining a combined ratio that is typically below industry averages (refer to Insurance Ratios under Item 7 Management's Discussion and Analysis of Financial Condition and Results of Operations for a discussion on insurance ratios);

taking advantage of the institutional knowledge our management has amassed during our long operating history in the Massachusetts market;

introducing new lines and forms of insurance products;

investing in technology to simplify internal processes and enhance our relationships with our agents; and

maintaining a high-quality investment portfolio.

*We Are a Technological Leader.* We have dedicated significant human and financial resources to the development of advanced information systems. Our technology efforts have benefited us in two distinct ways. First, we continue to develop technology that empowers our independent agent customers to make it easier for them to transact business with their clients and with the Insurance Subsidiaries. In our largest business line, private passenger automobile insurance, our agents now submit approximately 99.0% of all applications for new policies or endorsements for existing policies to us electronically through our proprietary information portal, the Agents Virtual Community ("AVC"). Our agents can also submit commercial automobile and homeowners insurance policies electronically over AVC. Second, our investment in technology has allowed us to re-engineer internal back office processes to provide more efficient service at lower cost.

*We Have an Experienced, Committed and Knowledgeable Management Team.* Our senior management team owns approximately 8.0% of the common stock of Safety Insurance Group, Inc. on a fully diluted basis. Our senior management team, led by our President, Chief Executive Officer and Chairman of the Board, David F. Brussard, has an average of over 31 years of industry experience per executive, as well as an average of over 29 years of experience with Safety. The team has demonstrated an ability to operate successfully within the regulated Massachusetts private passenger automobile insurance market.



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**Our Strategy**

To achieve our goal of increasing shareholder value, our strategy is to maintain and develop strong independent agent relationships by providing our agents with a full package of insurance products and information technology services. We believe this strategy will allow us to:

further penetrate the Massachusetts and New Hampshire private passenger, commercial automobile and homeowners insurance markets;

implement rates, forms and billing options that allow us to cross-sell homeowners, dwelling fire, and personal umbrella in the personal lines market and business owner policies, commercial property package and commercial umbrella in the commercial lines market in order to capture a larger share of the total Massachusetts property and casualty insurance business written by each of our independent agents; and

continue to expand our technology to enable independent agents to more easily serve their customers and conduct business with us, thereby strengthening their relationships with us.

**The Massachusetts Property and Casualty Insurance Market**

*Introduction.* We are licensed by the Commissioner of Insurance (the "Commissioner") to transact property and casualty insurance in Massachusetts. All of our business is extensively regulated by the Commissioner.

*The Massachusetts Market for Private Passenger Automobile Insurance.* Private passenger automobile insurance has been heavily regulated in Massachusetts. In many respects, the private passenger automobile insurance market in Massachusetts prior to 2008 was unique, in comparison to other states. This was due to a number of factors, including unusual regulatory conditions, the market dominance of domestic companies, the relative absence of large national companies, and the heavy reliance on independent insurance agents as the market's principal distribution channel. For many insurance companies, these factors presented substantial challenges, but we believe they provided us a competitive advantage, because, as our financial history shows, we have a thorough understanding of this market.

*Changes to the Regulation of Private Passenger Automobile Insurance in Massachusetts.* Since 1977, the Commissioner fixed and established the premium rates that all insurers must use in the Massachusetts private passenger automobile insurance market. Since 1982, CAR has managed the residual market for private passenger automobile insurance using a reinsurance mechanism. On July 16, 2007, the Commissioner issued two decisions that significantly changed these two long standing approaches to how private passenger automobile insurance is regulated in Massachusetts. In the first decision, the Commissioner announced that the Commissioner would not fix and establish the maximum premium rates that can be charged for private passenger automobile insurance policies issued or renewed after April 1, 2008. In a letter accompanying the decision, the Commissioner stated that in place of the "fixed and established" system, that the Commissioner would permit companies to file their own premium rates for approval by the Commissioner, under a system that the Commissioner has characterized as "managed competition" ("Managed Competition").

The Commissioner took additional steps to implement this decision. First, with respect to allowing competitive pricing, the Commissioner promulgated new regulations setting the terms and conditions that insurers must comply with in establishing their rates to be effective April 1, 2008. The regulation contains a list of prohibited factors, including a prohibition of the use of credit information in rating or underwriting. The Commissioner also issued a number of bulletins providing guidance on various issues, including regulatory review standards, discounts, product form, endorsement, and new business application standards and classification plan requirements. Pursuant to this authority, we filed for various rate changes for policies issued and renewed on or after April 1, 2008.

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In the second decision, the Commissioner approved and set a time table for the implementation of new CAR rules pursuant to an assigned risk plan known as the Massachusetts Automobile Insurance Plan ("MAIP") which replaced the former reinsurance program run by CAR. Under these new rules, as of April 1, 2009 we were no longer assigned ERPs whose business we must insure (subject to the option of ceding it to CAR) and instead, we are assigned individual policies by CAR. The MAIP began with business effective on or after April 1, 2008 for new business and those risks that have 10 or more Safe Driver Points. Beginning April 1, 2009, all business was eligible for MAIP except those risks that have no violations or accidents in the preceding three year period (so called "Clean in three" risks). The last policy effective date on which any risk could be ceded to CAR in accordance with the current reinsurance program was March 31, 2009. Under MAIP, policies will be assigned to us for three years, unless the policyholder is offered a voluntary policy by another insurer. We are not able at this time to determine what effect these CAR rules will have on our business over the longer term.

These decisions removed many of the factors that have historically distinguished the Massachusetts private passenger automobile insurance market from the market in other states, including the use of a standard policy form, the use of a single safe driver insurance plan, and the role of ERPs and CAR.

However, certain of the historically unique factors related to the Massachusetts private passenger automobile insurance market have not been eliminated, including compulsory insurance, affinity group marketing, and the prominence of independent agents.

## Products

Historically, we have focused on underwriting private passenger automobile insurance, which is written through our subsidiary, Safety Insurance. In 1989, we formed Safety Indemnity to offer commercial automobile insurance at preferred rates. Since 1997, we have expanded the breadth of our product line in order for agents to address a greater portion of their clients' insurance needs by selling multiple products. Homeowners, business owners policies, personal umbrella, dwelling fire and commercial umbrella insurance are written by Safety Insurance at standard rates, and written by Safety Indemnity at preferred rates. In December 2006, we formed Safety P&C to offer homeowners and commercial automobile insurance at ultra preferred rates.

The table below shows our premiums in each of these product lines for the periods indicated and the portions of our total premiums each product line represented.

Direct Written Premiums	Years Ended December 31,					
	2010		2009		2008	
Private passenger automobile	\$ 415,515	68.7%	\$ 387,604	69.2%	\$ 410,937	71.7%
Commercial automobile	62,658	10.4	67,228	12.0	75,808	13.2
Homeowners	101,594	16.8	82,290	14.7	66,770	11.6
Business owners	15,124	2.5	14,516	2.6	13,742	2.4
Personal umbrella	4,397	0.7	3,459	0.6	2,663	0.5
Dwelling fire	4,926	0.8	3,905	0.7	2,900	0.5
Commercial umbrella	743	0.1	745	0.2	689	0.1
Total	\$ 604,957	100.0%	\$ 559,747	100.0%	\$ 573,509	100.0%

Our product lines are as follows:

*Private Passenger Automobile (68.7% of 2010 direct written premiums).* Private passenger automobile insurance is our primary product, and we support all Massachusetts policy forms and limits of coverage. Private passenger automobile policies provide coverage for bodily injury and property damage to others, no-fault personal injury coverage for the insured/insured's car occupants, and physical damage coverage for an insured's own vehicle for collision or other perils. We have priced our



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private passenger coverage competitively by offering group discounts since 1995 and we currently offer approximately 169 affinity group discount programs ranging from 3% to 8% discounts. Under Massachusetts' Managed Competition regulations, we offer various new discounts including a discount of 10% when a private passenger policy is issued along with an other than private passenger policy with us, a longevity/renewal credit of up to 4% for policyholders who maintain continuous coverage with us, and a 7% e-Customer discount for policyholders who want electronic policy issuance with one combined bill for all of their policies with us. We began using four rating tiers effective January 1, 2010. A Companion Policy Client Tier, which is policyholders who have a non private passenger automobile policy with us, receives a rate decrease of 2.5% from our filed base rates. A Loyal Automobile Client Tier, which is policyholders who have been insured with us for two or more years, receives our filed base rates. A New Insurance Client Tier, which is policyholders with twelve or more months of continuous coverage or who qualify for a multi-car discount, receives a rate increase of 2.5% from our filed base rates. A New Policyholder Tier, which is policyholders who do not qualify for the other three tiers, receives MAIP rates.

*Commercial Automobile (10.4% of 2010 direct written premiums).* Our commercial automobile program supports all Massachusetts policy forms and limits of coverage including endorsements that broaden coverage over and above that offered on the standard Massachusetts policy forms. Commercial automobile policies provide coverage for bodily injury and property damage to others, no-fault personal injury coverage, and physical damage coverage for an insured's own vehicle for collision or other perils resulting from the ownership or use of commercial vehicles in a business. We offer insurance for commercial vehicles used for business purposes such as private passenger-type vehicles, trucks, tractors and trailers, and insure individual vehicles as well as commercial fleets. Commercial automobile policies are written at a standard rate through Safety Insurance. We did not file for Massachusetts commercial automobile insurance rate changes during 2008, 2009 or 2010. Qualifying risks eligible for preferred rates are written through Safety Indemnity which offers rates that are 20% lower than Safety Insurance. Effective December 1, 2007, qualifying risks eligible for ultra preferred rates are written through Safety P&C which offers rates that are 35% lower than Safety Insurance.

*Homeowners (16.8% of 2010 direct written premiums).* We offer a broad selection of coverage forms for qualified policyholders. Homeowners policies provide coverage for losses to a dwelling and its contents from numerous perils, and coverage for liability to others arising from ownership or occupancy. We write policies on homes, condominiums, and apartments. We offer loss-free credits of up to 16% for eight years of loss free experience, an account credit of up to 20% when a home is written together with an automobile, and a 5% e-Customer discount for policyholders who want electronic policy issuance with one combined bill for all of their policies with us. We received approval for a Massachusetts rate increase of 2.3% effective August 1, 2010. All forms of homeowners coverage are written at a standard rate through Safety Insurance. Qualifying risks eligible for preferred rates are written through Safety Indemnity which offers rates that are 13% lower than Safety Insurance. Effective September 1, 2007, qualifying risks eligible for ultra preferred rates are written through Safety P&C which offers rates that are 22% lower than Safety Insurance.

*Business Owners Policies (2.5% of 2010 direct written premiums).* We serve eligible small and medium sized commercial accounts with a program that covers apartments and residential condominiums; mercantile establishments, including limited cooking restaurants; offices, including office condominiums; processing and services businesses; special trade contractors; and wholesaling businesses. Business owner policies provide liability and property coverage for many perils, including business interruption from a covered loss. Equipment breakdown coverage is automatically included, and a wide range of additional coverage is available to qualified customers. We write policies for business owners at standard rates with qualifying risks eligible for preferred lower rates.

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*Commercial Package Policies (Included in our Business Owners Policies direct written premiums).* For larger commercial accounts, or those clients that require more specialized or tailored coverages, we offer a commercial package policy program that covers a more extensive range of business enterprises. Commercial package policies provide any combination of property, general liability, crime and inland marine insurance. Property automatically includes equipment breakdown coverage, and a wide range of additional coverage is available to qualified customers. We write commercial package policies at standard rates with qualifying risks eligible for preferred lower rates.

*Personal Umbrella (0.7% of 2010 direct written premiums).* We offer personal excess liability coverage over and above the limits of individual automobile, watercraft, and homeowner's insurance policies to clients. We offer an account credit of 10% when an umbrella policy is written together with an automobile insurance policy. We write policies at standard rates with limits of \$1,000 to \$5,000.

*Dwelling Fire (0.8% of 2010 direct written premiums).* We underwrite dwelling fire insurance, which is a limited form of a homeowner's policy for non-owner occupied residences. We offer superior construction and protective device credits, with an account credit of 5% when a dwelling fire policy is issued along with an automobile policy. We write all forms of dwelling fire coverage at standard rates with qualifying risks eligible for preferred lower rates.

*Commercial Umbrella (0.1% of 2010 direct written premiums).* We offer an excess liability product to clients for whom we underwrite both commercial automobile and business owner policies. The program is directed at commercial automobile risks with private passenger-type automobiles or light and medium trucks. We write commercial umbrella policies at standard rates with limits ranging from \$1,000 to \$5,000.

*Inland Marine (Included in our Homeowners direct written premiums).* We offer inland marine coverage as an endorsement for all homeowners and business owner policies, and as part of our commercial package policy. Inland marine provides additional coverage for jewelry, fine arts and other items that a homeowners or business owner policy would limit or not cover. Scheduled items valued at more than \$5 must meet our underwriting guidelines and be appraised.

*Watercraft (Included in our Homeowners direct written premiums).* We offer watercraft coverage for small and medium sized pleasure craft with maximum lengths of 32 feet, valued at less than \$75 and maximum speed of 39 knots. We write this coverage as an endorsement to our homeowner's policies.

In the wake of the September 11, 2001 tragedies, the insurance industry is also impacted by terrorism, and we have filed and received approval for a number of terrorism endorsements from the Commissioner, which limit our liability and property exposure according to the Terrorism Risk Insurance Act of 2002, the Terrorism Risk Insurance Extension Act of 2005 and the Terrorism Risk Insurance Program Reauthorization Act of 2007. See "Reinsurance," discussed below.

### **Distribution**

We distribute our products exclusively through independent agents, unlike some of our competitors who use multiple distribution channels. We believe this gives us a competitive advantage with the agents. With the exception of our ERPs, we do not accept business from insurance brokers. Our voluntary agents have authority pursuant to our voluntary agency agreement to bind our Insurance Subsidiaries for any coverage that is within the scope of their authority. We reserve the ability under Massachusetts law to cancel any coverage, other than private passenger automobile insurance, within the first 30 days after it is bound. In total, our independent agents (including our ERPs) numbered 783 and had 944 offices (some agencies have more than one office) and approximately 5,875 customer service representatives during 2010.

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*Voluntary Agents.* In 2010, we obtained approximately 92.4% of our direct written premiums for automobile insurance and 100% of our direct written premiums for all of our other lines of business through our voluntary agents. As of January 31, 2011, we had agreements with 659 voluntary agents. Our voluntary agents are located in all regions of Massachusetts.

We look for agents with profitable portfolios of business. To become a voluntary agent for our Company, we generally require that an agency: (i) have been in business for at least five years; (ii) have exhibited a three year private passenger average ratio of losses, excluding loss adjustment expenses, to net earned premiums ("pure loss ratio") of 65.0% or less on the portion of the agent's portfolio that we would underwrite; (iii) make a commitment for us to underwrite at least 500 policies from the agency during the first twelve months after entering an agreement with us; and (iv) offer multiple product lines. Every year, we review the performance of our agents during the prior year. If an agent fails to meet our profitability standards, we try to work with the agent to improve the profitability of the business it places with us. We generally terminate contracts each year with a few agencies, which, despite our efforts, have been consistently unable to meet our standards. Although independent agents usually represent several unrelated insurers, our goal is to be one of the top two insurance companies represented in each of our agencies, as measured by premiums. No individual agency generated more than 3.6% of our direct written premiums in 2010.

*Exclusive Representative Producers.* In 2010, our ERPs generated approximately 7.6% of our direct written premiums for automobile insurance. As of December 31, 2010, we had two private passenger automobile ERPs. CAR defines ERPs as licensed dwelling fire or casualty insurance agents or brokers who have a place of business in Massachusetts, but have no existing voluntary independent agency relationship with an automobile insurer conducting business in Massachusetts. In addition, we are required by MAIP to write "Clean in three" business from our former ERPs.

Massachusetts law guarantees that CAR provide motor vehicle insurance coverage to all qualified applicants. To facilitate this system, under CAR's prior rules, any qualified licensed insurance producer that is unable to obtain a voluntary automobile relationship with an insurer becomes an ERP and is assigned to an insurer, which is then required to write that agent's policies. As previously noted, the MAIP began April 1, 2008 and was fully implemented by April 1, 2009. Beginning April 1, 2008 all Massachusetts agents (including ERPs) were authorized to submit eligible business to the MAIP for random assignment to a servicing carrier such as Safety Insurance. We began receiving individual policies assigned to us from the MAIP on April 1, 2008. As a result of CAR's new rules, effective April 1, 2009 ERPs were no longer assigned to us or any Massachusetts personal automobile insurer, and we have been instead allocated all residual market business through the MAIP.

CAR runs a reinsurance pool for commercial automobile policies. On January 1, 2006, CAR implemented a Limited Servicing Carrier Program ("LSC") for ceded commercial automobile policies. CAR approved Safety Insurance and five other servicing carriers through a Request for Proposal to process ceded commercial automobile business for a five year term ending January 1, 2011. During 2010 CAR requested bids through a Request for Proposal process that reduced the number of servicing carriers from six to four. CAR approved Safety and three other servicing carriers to process ceded commercial automobile insurance with a delayed effective date of July 1, 2011. Approximately \$95,000 of ceded premium will be spread equitably among the four servicing carriers. Subject to the Commissioner's review, CAR sets the premium rates for commercial automobile policies reinsured through CAR and this reinsurance pool can generate an underwriting result that is a profit or deficit based upon CAR's rate level. This underwriting result is allocated among every Massachusetts commercial automobile insurance company, including us, based on a company's commercial automobile voluntary market share.

CAR also runs a reinsurance pool for Taxi, Limousine and Car Service risks (the "Taxi/Limo Program"). On April 25, 2007, Safety submitted through a Request for Proposal a bid to process a

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portion of the Taxi/Limo Program. CAR approved Safety as one of the two servicing carriers for this program beginning January 1, 2008. During 2010 CAR requested bids through a Request for Proposal process to extend the program another five years. CAR approved Safety as one of the two servicing carriers for this program beginning January 1, 2011. Approximately \$8,000 of ceded premium is spread equitably between the two servicing carriers.

We are assigned independent agents by CAR who can submit commercial business to us in the LSC and Taxi/Limo Program, and we classify those agents as commercial ERPs.

The table below shows our direct written exposures in each of our product lines for the periods indicated and the change in exposures for each product line.

Line of Business	Years Ended December 31,					
	2010		2009		2008	
	Exposures	Change	Exposures	Change	Exposures	Change
Private passenger automobile:						
Voluntary agents	421,139	2.6%	410,405	3.6%	395,989	1.2%
ERPs	31,411	-9.1	34,562	-37.5	55,342	-35.9
MAIP	17,687	73.5	10,195	13.5	8,983	
Total private passenger automobile	470,237	3.3	455,162	-1.1	460,314	-3.6
Commercial automobile:						
Voluntary agents	42,502	-0.4	42,670	-4.5	44,692	-6.0
ERPs	3,699	-18.8	4,556	-16.8	5,474	-10.8
Total commercial automobile	46,201	-2.2	47,226	-5.9	50,166	-6.5
Other:						
Homeowners	117,120	19.6	97,955	23.4	79,359	14.0
Business owners	7,785	8.2	7,198	8.2	6,654	25.9
Personal umbrella	16,515	24.9	13,223	25.6	10,528	20.5
Dwelling fire	4,729	24.8	3,788	30.3	2,908	20.0
Commercial umbrella	530	2.9	515	12.2	459	12.0
Total other	146,679	19.6	122,679	22.8	99,908	15.5
Total	663,117	6.1	625,067	2.4	610,388	-1.2
Total voluntary agents	628,007	7.2	585,949	6.6	549,572	4.6
Total ERPs	35,110	-10.3%	39,118	-35.7%	60,816	-34.2%

Our total written exposures increased by 6.1% for the year ended December 31, 2010. The increase was primarily the result of our voluntary agent written exposures increasing by 7.2%. Our ERP written exposures, which include "Clean in three" exposures written by our former ERPs, decreased by 10.3%. Our private passenger automobile exposures increased by 3.3% in 2010 primarily as a result of the increase in written exposures due to the transition to MAIP effective April 1, 2008 as discussed above. Our commercial automobile exposures decreased by 2.2% in 2010 primarily as a result of reduced exposures from ERPs submitting business through the CAR LSC program, and general economic conditions which reduced the size of the overall commercial automobile market in Massachusetts. Our other than auto exposures increased by 19.6% in 2010 primarily as a result of our voluntary agents' efforts to sell multiple products to their clients and our pricing strategy of offering account discounts to policyholders who insure both their home and automobile with us. In 2010, 37.6% of the private passenger

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automobile exposures we insure had an other than private passenger policy with us, compared to 30.5% and 25.9% in 2009 and 2008, respectively. In addition, 83.9% of our homeowners policyholders had a matching automobile policy with us in 2010 and 2009 compared to 79.2% in 2009.

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**Marketing**

We view the independent agent as our customer and business partner. As a result, a component of our marketing efforts focuses on developing interdependent relationships with leading Massachusetts agents that write profitable business and positioning ourselves as the preferred insurance carrier of those agents, thereby receiving a larger portion of each agent's aggregate business. Our principal marketing strategies to agents are:

to offer a range of products, which we believe enables our agents to meet the insurance needs of their clients, and overcomes the agent's resistance to placing their clients' automobile, homeowners and other coverages with different insurers;

to price our products competitively, including offering discounts when and where appropriate for safer drivers and for affinity groups for our personal automobile products, loss free credits for our homeowner products and also offering account discounts for policyholders that have more than one policy with us;

to design, price and market our products to our agents for their customers to place all their insurance with us;

to offer agents competitive commissions, with incentives for placing their more profitable business with us; and

to provide a level of support and service that enhances the agent's ability to do business with its clients and with us.

Beginning in 2007, we started a comprehensive branding campaign using a variety of radio, television, internet and print advertisements.

*Commission Schedule and Profit Sharing Plan.* We have several programs designed to attract profitable new business from agents by paying them more than the minimum commission the law requires for private passenger auto (which is 13.0% of premiums for 2010 and 2011). We recognize our top performing agents by making them members of either our Chairman's Elite, Chairman's, President's, Executive's or Preferred Agent's Club. In 2010, members of these Clubs received a commission of up to 18.0% of premiums for each new private passenger auto policy and up to 27.0% of premiums for each new homeowner policy.

Further, we have a competitive agency incentive commission program under which we pay agents up to 8.0% of premiums based on the loss ratio on their business.

We have received no inquiries from the Commissioner relative to how we conduct our contingent commissions and profit sharing programs. The Massachusetts Attorney General did question the inclusion of contingent commission expenses in her appeal of our April 1, 2008 private passenger rate filing. The Commissioner ruled on January 25, 2008 that the inclusion of expenses attributable to contingent commissions was reasonable and not prohibited by Massachusetts law.

*Service and Support.* We believe that the level and quality of service and support we provide helps differentiate us from other insurers. We have made a significant investment in information technology designed to facilitate our agents' business. Our AVC website helps agents manage their work efficiently. We provide a substantial amount of information online that agents need to serve their customers, such as information about the status of new policies, bill payments and claims. Providing this type of content reduces the number of customer calls we receive and empowers the agent's customer service representatives by enabling them to respond to customers' inquiries while the customer is on the telephone. Finally, we believe that the knowledge and experience of our employees enhances the quality of support we provide.

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**Underwriting**

Our underwriting department is responsible for a number of key decisions affecting the profitability of our business, including:

pricing of our private passenger automobile product since April 1, 2008;

pricing of our commercial automobile, homeowners, dwelling fire, personal umbrella, business owners policies, commercial umbrella and commercial package products;

determining underwriting guidelines for all our products; and

evaluating whether to accept transfers of a portion of an existing or potential new agent's portfolio from another insurer.

We are organized into three underwriting units, a separate unit for private passenger automobile, a separate unit for all other personal lines underwriting including homeowners, dwelling fire, personal umbrella and inland marine coverages, and a separate unit for commercial lines, including commercial auto, business owners policies, commercial umbrella and commercial package policies.

*Pricing.* Prior to April 1, 2008, our pricing strategy for private passenger automobile insurance primarily depended on the maximum permitted premium rates and minimum permitted commission levels mandated by the Commissioner. Beginning April 1, 2008 subject to the Commissioner's review, we set rates for our private passenger business using industry loss cost data, our own loss experience, residual market deficits, catastrophe modeling and prices charged by our competitors in the Massachusetts market. Beginning April 1, 2008 subject to Commissioner's review, CAR sets the premium rates for personal automobile policies assigned to carriers by the MAIP. However, companies may only charge the insured the lower of the CAR/MAIP rate or the company's competitive voluntary market rate. Safety Insurance's approved rate for three of our four rating tiers is lower than the CAR/MAIP rate. We began using four rating tiers effective January 1, 2010. A Companion Policy Client Tier, which is policyholders that have an other than private passenger automobile policy with us, receives a rate decrease of 2.5% from our filed base rates. A Loyal Automobile Client Tier, which is policyholders who have been insured with Safety two or more years, receives our filed base rates. A New Insurance Client Tier, which is policyholders with 12 or more months of continuous coverage or who qualify for a multi-car discount, receives a rate increase of 2.5% from our filed base rates. A New Policyholder Tier, which is policyholders that don't qualify for the other three tiers, receives MAIP rates. For a discussion of changes since 2008 in our private passenger automobile rates, see Item 7 Management's Discussion and Analysis of Financial Condition and Results of Operations, *Executive Summary and Overview*.

We offer group discounts to members of 169 affinity groups. In general, we target affinity groups with a mature and stable membership base along with favorable driving records, offering between a 3.0% and 8.0% discount (with 4.0% being the average discount offered). Approximately 7.7% of the private passenger exposures we write receive an affinity group discount.

Subject to the Commissioner's review, CAR sets the premium rates for commercial automobile policies reinsured through CAR. Subject to the Commissioner's review, we set rates for commercial automobile policies that are not reinsured through CAR, and for all other insurance lines we offer, including homeowners, dwelling fire, personal umbrella, commercial umbrella, commercial package policies and business owner policies. We base our rates on industry loss cost data, our own loss experience, residual market deficits, catastrophe modeling and prices charged by our competitors in the Massachusetts market. We have three pricing tiers for most products, utilizing Safety Insurance for standard rates, Safety Indemnity for preferred rates and Safety P&C for ultra preferred rates. We received approval for a rate increase of 2.1% for our Safety Insurance commercial automobile line effective December 16, 2004, and did not file for a rate change for the years 2005 through 2010. We received approval for a rate deviation for Safety P&C commercial automobile of 35.0% below our

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comparable Safety Insurance rate. We received approval for a rate increase of 1.6% for our homeowners line effective August 1, 2010.

*CAR Reinsurance Pool.* CAR runs a reinsurance pool for commercial automobile policies and beginning January 1, 2006, we became one of six servicing carriers that can service commercial automobile policies for CAR. In 2010, CAR reduced the number of servicing carriers to four, and CAR has approved Safety and three other servicing carriers effective July 1, 2011 to continue the program. CAR also runs a reinsurance pool for taxi/limousine/car service commercial automobile policies and beginning January 1, 2008, we became one of two servicing carriers that can service these policies for CAR. All commercial automobile business that is not written in the voluntary market is apportioned to one of the four servicing carriers who handle the business on behalf of CAR or to one of the two servicing carriers who handle the business on behalf of CAR for taxi/limousine/car service business. Each Massachusetts commercial automobile insurer must bear a portion of the losses of the total commercial reinsurance pool that is serviced by the approved servicing carriers.

*Bulk Policy Transfers and New Voluntary Agents.* From time to time, we receive proposals from existing voluntary agents to transfer a portfolio of the agent's business from another insurer to us. Our underwriters model the profitability of these portfolios before we accept these transfers. Among other things, we usually require that the private passenger portion of the portfolio have a pure loss ratio of 65.0% or less on the portion of the agent's portfolio that we would underwrite. In addition, we require any new voluntary agent to commit to transfer a portfolio to us consisting of at least 500 policies.

*Policy Processing and Rate Pursuit.* Our underwriting department assists in processing policy applications, endorsements, renewals and cancellations. For many years, we have used and implemented proprietary software that enables agents to connect to our network and enter policy and endorsement applications for private passenger automobile insurance from their office computers. In our private passenger automobile insurance line, our agents now submit approximately 99.0% of all applications for new policies or endorsements for existing policies through our proprietary information portal, the AVC. We also offer propriety software for our commercial automobile and homeowners insurance lines of business that provides the same functionality as that of our personal automobile software.

Our rate pursuit team aggressively monitors all insurance transactions to make sure we receive the correct premium for the risk insured. We accomplish this by verifying Massachusetts pricing criteria, such as proper classification of drivers, the make, model and age of insured vehicles and the availability of discounts. We verify that operators are properly listed and classified, assignment of operators to vehicles, vehicle garaging, vehicle pre-inspection requirements, and in some cases the validity of discounts. In our homeowners and dwelling fire lines, our team has completed a project to update the replacement costs for each dwelling. We use third-party software to assist in these appraisal efforts.

## Technology

The focuses of our information technology effort are:

to constantly reengineer internal processes to allow more efficient operations, resulting in lower operating costs;

to make it easier for independent agents to transact business with us; and

to enable agents to efficiently provide their clients with a high level of service.

We believe that our technology initiatives have increased revenue and decreased costs. For example, these initiatives have allowed us to reduce the number of call-center transactions which we perform, and to transfer many manual processing functions from our internal operations to our independent agents. We also believe that these initiatives have contributed to overall increases in productivity.



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**Internal Applications (Intranet)**

Our employees access our proprietary applications through our corporate intranet. Our intranet applications streamline internal processes and improve overall operational efficiencies in areas including:

*Claims.* Our claims workload management application allows our claims and subrogation adjusters to better manage injury claims. Subrogation refers to the process by which we are reimbursed by other insurers for claims costs we incur due to the fault of their insureds. The use of this application has reduced the time it takes for us to respond to and settle casualty claims, which we believe helps reduce the total amount of our claims expense.

The automated adjuster assignment system categorizes our new claims by severity and assigns them to the appropriate adjuster responsible for investigation. Once assigned, the integrated workload management tools facilitate the work of promptly assigning appraisers, investigating liability, issuing checks and receiving subrogation receipts.

The RadicalGlass.com application allows our claims department to contain glass costs by increasing the windshield repair to replacement ratio. For every windshield that is repaired rather than replaced there is an average savings of approximately \$285 per windshield claim.

Our first VIP Claims Center was introduced during 2006 to provide increased service levels to our independent insurance agents and their clients. We currently operate three VIP Claims Centers which use a network of rental car centers and auto body repair shops to provide a higher level of service to the clients of the independent insurance agents while reducing costs, such as rental expense, through reduced cycle times.

*Billing.* Proprietary billing systems, integrated with the systems of our print and lock-box vendors, expedite the processing and collection of premium receipts and finance charges from agents and policyholders. We believe the sophistication of our direct bill system helps us to limit our bad debt expense. In both 2010 and 2009, our bad debt expense as a percentage of direct written premiums was 0.2%.

**External Applications**

Our Agent Technology offerings are centralized within our agency portal and feature PowerDesk and Safety Express. PowerDesk is a web based application that allows for billing inquiry, payment notification, policy inquiry and claims inquiry. Safety Express provides agents with new business and endorsement entry, real time policy issuance for personal lines, immediate printing of declarations pages in agents' offices, policy downloads to most major agency management systems and data imports from Boston Software's WinRater (Massachusetts) and Vertafore's PL Rater (New Hampshire). In addition, Safety provides its agents with commission downloads for all lines of business, Transformation Station and Transact Now Inquires, e-Claims online claims reporting, e-View daily transaction reports and e-Docs online electronic document file cabinet. Safety also provides online bill pay, (including credit and debit cards), online declarations pages, billing inquiry, claims inquiry, auto claims first notice of loss, and online auto insurance cards to our agent's policyholders through [www.SafetyInsurance.com](http://www.SafetyInsurance.com). Safety has also updated its telephone system to provide a voice activated phone directory, automated billing inquiry and payments, and call center screen pop technology.

**Claims**

Because of the unique differences between the management of casualty claims and property claims, we use separate departments for each of these types of claims.

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**Casualty Claims**

We have adopted stringent claims settlement procedures, which include guidelines that establish maximum settlement offers for soft tissue injuries, which constituted approximately 81% of our bodily injury claims in 2010. If we are unable to settle these claims within our guidelines, we generally take the claim to litigation. We believe that these procedures result in providing our adjusters with a uniform approach to negotiation.

We believe an important component of handling claims efficiently is prompt investigation and settlement. We find that faster claims settlements often result in less expensive claims settlements. Our E-Claim reporting system is an online product that reduces the time it takes for agents to notify our adjusters about claims, thereby enabling us to contact third-party claimants and other witnesses quickly. After business hours, we outsource claims adjustment support to an independent firm whose employees contact third-party claimants and other witnesses. We believe that early notification results in our adjusters conducting prompt investigations of claims and compiling more accurate information about those claims. Our claims workload management software also assists our adjusters in handling claims quickly.

We believe the structure of our casualty claims unit allows us to respond quickly to claimants anywhere in the Commonwealth of Massachusetts. Comprising 118 people, the department is organized into distinct claim units that contain loss costs for soft tissue injuries. Field adjusters are located geographically for prompt response to claims, with our litigation unit focused on managing loss costs and litigation expenses for serious injury claims.

Additionally, we utilize a special unit to investigate fraud in connection with casualty claims. This special unit has one manager and nine employees. In cases where adjusters suspect fraud in connection with a claim, we deploy this special unit to conduct investigations. We deny payment to claimants in cases in which we have succeeded in accumulating sufficient evidence of fraud.

**Property Claims**

Our property claims unit handles property claims arising in our private passenger and commercial automobile, homeowners and other insurance lines. Process automation has streamlined our property claims function. Many of our property claims are now handled by the agents through AVC using our Power Desk software application. As agents receive calls from claimants, Power Desk permits the agent to immediately send information related to the claim directly to us and to an independent appraiser selected by the agent to value the claim. Once we receive this information, an automated system redirects the claim to the appropriate internal adjuster responsible for investigating the claim to determine liability. Upon determination of liability, the system automatically begins the process of seeking a subrogation recovery from another insurer, if liable. We believe this process results in a shorter time period from when the claimant first contacts the agent to when the claimant receives a claim payment, while enabling our agents to build credibility with their clients by responding to claims in a timely and efficient manner. We benefit from decreased labor expenses from the need for fewer employees to handle the reduced property claims call volume.

Another important factor in keeping our overall property claims costs low is collecting subrogation recoveries. We track the amounts we pay out in claims costs and identify cases in which we believe we can reclaim some or all of those costs through the use of our automated workload management tools.

**Reserves**

Significant periods of time can elapse between the occurrence of an insured loss, the reporting of the loss to the insurer and the insurer's payment of that loss. To recognize liabilities for unpaid losses, insurers establish reserves as balance sheet liabilities representing estimates of amounts needed to pay

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reported and unreported losses and the expenses associated with investigating and paying the losses, or loss adjustment expenses. Every quarter, we review and establish our reserves. Regulations promulgated by the Commissioner require us to annually obtain a certification from either a qualified actuary or an approved loss reserve specialist who may be one of our employees that our loss and loss adjustment expenses reserves are reasonable.

When a claim is reported, claims personnel establish a "case reserve" for the estimated amount of the ultimate payment. The amount of the reserve is primarily based upon an evaluation of the type of claim involved, the circumstances surrounding each claim and the policy provisions relating to the loss. The estimate reflects informed judgment of such personnel based on general insurance reserving practices and on the experience and knowledge of the claims person. During the loss adjustment period, these estimates are revised as deemed necessary by our claims department based on subsequent developments and periodic reviews of the cases.

In accordance with industry practice, we also maintain reserves for estimated losses incurred but not yet reported. Incurred but not yet reported reserves are determined in accordance with commonly accepted actuarial reserving techniques on the basis of our historical information and experience. We make adjustments to incurred but not yet reported reserves quarterly to take into account changes in the volume of business written, claims frequency and severity, our mix of business, claims processing and other items that can be expected to affect our liability for losses and loss adjustment expenses over time.

When reviewing reserves, we analyze historical data and estimate the impact of various loss development factors, such as our historical loss experience and that of the industry, legislative enactments, judicial decisions, legal developments in imposition of damages, and changes and trends in general economic conditions, including the effects of inflation. There is no precise method, however, for evaluating the impact of any specific factor on the adequacy of reserves, because the eventual development of reserves is affected by many factors. After taking into account all relevant factors, management believes that our provision for unpaid losses and loss adjustment expenses at December 31, 2010 is adequate to cover the ultimate net cost of losses and claims incurred as of that date.

Management determines its loss and loss adjustment expense ("LAE") reserves estimates based upon the analysis of the Company's actuaries. Management has established a process for the Company's actuaries to follow in establishing reasonable reserves. The process consists of meeting with our claims department, establishing ultimate incurred losses by using development models accepted by the actuarial community, and reviewing the analysis with management. The Company's estimate for loss and LAE reserves, net of the effect of ceded reinsurance, ranges from a low of \$311,570 to a high of \$359,802 as of December 31, 2010. The Company's loss and LAE reserves, based on our actuaries' best estimate, were set at \$351,244 as of December 31, 2010. The ultimate liability may be greater or less than reserves carried at the balance sheet date. Establishment of appropriate reserves is an inherently uncertain process, and there can be no certainty that currently established reserves will prove adequate in light of subsequent actual experience. To the extent that reserves are inadequate and are strengthened, the amount of such increase is treated as a charge to earnings in the period that the deficiency is recognized. To the extent that reserves are redundant and are released, the amount of the release is a credit to earnings in the period the redundancy is recognized. We do not discount any of our reserves.

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The following table presents development information on changes in the reserves for losses and LAE of our Insurance Subsidiaries for each year in the three year period ended December 31, 2010.

	Years Ended December 31,		
	2010	2009	2008
Reserves for losses and LAE, beginning of year	\$ 439,706	\$ 467,559	\$ 477,720
Less reinsurance recoverable on unpaid losses and LAE	(64,874)	(76,489)	(84,290)
Net reserves for losses and LAE, beginning of year	374,832	391,070	393,430
Incurred losses and LAE, related to:			
Current year	409,005	390,366	405,761
Prior years	(48,157)	(44,065)	(35,938)
Total incurred losses and LAE	360,848	346,301	369,823
Paid losses and LAE related to:			
Current year	253,476	235,681	229,924
Prior years	130,960	126,858	142,259
Total paid losses and LAE	384,436	362,539	372,183
Net reserves for losses and LAE, end of year	351,244	374,832	391,070
Plus reinsurance recoverables on unpaid losses and LAE	53,147	64,874	76,489
Reserves for losses and LAE, end of year	\$ 404,391	\$ 439,706	\$ 467,559

At the end of each period, the reserves were re-estimated for all prior accident years. Our prior year reserves decreased by \$48,157, \$44,065 and \$35,938, during 2010, 2009 and 2008, respectively. The decrease in prior year reserves during 2010 resulted from re-estimations of prior year ultimate loss and LAE liabilities and is primarily composed of reductions of \$34,248 in our retained automobile reserves, \$7,269 in our retained homeowners and retained all other reserves, and \$5,572 in CAR assumed reserves. It is not appropriate to extrapolate future favorable or unfavorable development of reserves from this past experience.

The following table represents the development of reserves, net of reinsurance, for calendar years 2000 through 2010. The top line of the table shows the reserves at the balance sheet date for each of the indicated years. This represents the estimated amounts of losses and loss adjustment expenses for claims arising in all years that were unpaid at the balance sheet date, including losses that had been incurred but not yet reported to us. The upper portion of the table shows the cumulative amounts paid as of the end of each successive year with respect to those claims. The lower portion of the table shows the re-estimated amount of the previously recorded reserves based on experience as of the end of each succeeding year, including cumulative payments made since the end of the respective year. The estimate changes as more information becomes known about the payments, frequency and severity of claims for individual years. Favorable loss development, shown as a cumulative

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redundancy in the table, exists when the original reserve estimate is greater than the re-estimated reserves at December 31, 2010.

Information with respect to the cumulative development of gross reserves (that is, without deduction for reinsurance ceded) also appears at the bottom portion of the table.

In evaluating the information in the table, it should be noted that each amount entered incorporates the effects of all changes in amounts entered for prior periods. Thus, if the 2004 estimate for a previously incurred loss was \$150,000 and the loss was reserved at \$100,000 in 2000, the \$50,000 deficiency (later estimate minus original estimate) would be included in the cumulative redundancy (deficiency) in each of the years 2000-2004 shown in the table. It should further be noted that the table does not present accident or policy year development data. In addition, conditions and trends that have

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affected the development of liability in the past may not necessarily recur in the future. Accordingly, it is not appropriate to extrapolate future redundancies or deficiencies from the table.

	As of and for the Years Ended December 31,										
	2010	2009	2008	2007	2006	2005	2004	2003	2002	2001	2000
Reserves for losses and LAE originally estimated:	\$ 351,244	\$ 374,832	\$ 391,070	\$ 393,430	\$ 370,980	\$ 370,166	\$ 366,730	\$ 310,012	\$ 266,636	\$ 227,377	\$ 211,834
Cumulative amounts paid as of:											
One year later		130,960	126,858	142,259	122,806	133,213	144,600	150,354	137,092	118,141	114,016
Two years later			189,897	195,798	183,457	187,231	202,435	201,287	199,119	168,344	163,768
Three years later				234,359	212,331	221,390	233,513	232,539	225,350	196,340	185,396
Four years later					233,438	234,705	251,303	247,073	238,087	212,079	194,891
Five years later						244,454	257,061	255,798	243,677	217,009	204,290
Six years later							260,628	258,588	246,488	218,419	206,324
Seven years later								259,553	247,211	219,397	206,801
Eight years later									247,299	219,673	207,180
Nine years later										219,716	207,249
Ten years later											207,370

As of and for the Years Ended December 31,											
	2010	2009	2008	2007	2006	2005	2004	2003	2002	2001	2000
Reserves re-estimated as of:											
One year later	\$ 326,675	\$ 347,004	\$ 357,492	\$ 340,189	\$ 327,419	\$ 327,110	\$ 303,234	\$ 266,817	\$ 225,115	\$ 204,531	
Two years later		307,918	325,317	311,972	310,614	304,891	291,100	269,941	227,764	206,340	
Three years later			297,224	287,875	289,109	297,790	280,507	264,961	231,190	208,587	
Four years later				269,446	274,840	284,542	277,835	260,398	229,699	209,517	
Five years later					264,408	276,272	271,205	257,836	227,428	208,343	
Six years later						270,441	267,764	253,711	225,705	208,232	
Seven years later							264,563	251,656	223,554	207,084	
Eight years later								250,380	222,431	205,891	
Nine years later									221,771	205,240	
Ten years later											204,909
Cumulative redundancy	\$ (48,157)	\$ (83,152)	\$ (96,206)	\$ (101,534)	\$ (105,758)	\$ (96,289)	\$ (45,449)	\$ (16,256)	\$ (5,606)	\$ (6,925)	

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2010

	As of and for the Years Ended December 31,										
	2010	2009	2008	2007	2006	2005	2004	2003	2002	2001	2000
Gross liability-end of year	\$ 404,391	\$ 439,706	\$ 467,559	\$ 477,720	\$ 449,444	\$ 450,716	\$ 450,897	\$ 383,551	\$ 333,297	\$ 302,556	\$ 302,131
Reinsurance recoverables	53,147	64,874	76,489	84,290	78,464	80,550	84,167	73,539	66,661	75,179	90,297
Net liability-end of year	351,244	374,832	391,070	393,430	370,980	370,166	366,730	310,012	266,636	227,377	211,834
Gross estimated liability-latest		385,722	368,894	359,109	325,873	320,979	331,094	326,584	310,816	274,903	271,083
Reinsurance recoverables-latest		59,047	60,976	61,885	56,427	56,571	60,653	62,021	60,436	53,132	66,174
Net estimated liability-latest		\$ 326,675	\$ 307,918	\$ 297,224	\$ 269,446	\$ 264,408	\$ 270,441	\$ 264,563	\$ 250,380	\$ 221,771	\$ 204,909

As the table shows, our net reserves grew at a faster rate than our gross reserves over the ten-year period. As we have grown, we have been able to retain a greater percentage of our direct business. Additionally, in the past we conducted substantial business as a servicing carrier for other insurers, in which we would service the residual market automobile insurance business assigned to other carriers

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for a fee. All business generated through this program was ceded to the other carriers. As we reduced the amount of our servicing carrier business, our proportion of reinsurance ceded diminished.

The table also shows that we have substantially benefited in the current and prior years from releasing redundant reserves. In the years ended December 31, 2010, 2009 and 2008 we decreased loss reserves related to prior years by \$48,157, \$44,065 and \$35,938, respectively. Reserves and development are discussed further in Item 7 Management's Discussion and Analysis of Financial Condition and Results of Operations, *Executive Summary and Overview*.

As a result of our focus on core business lines since our founding in 1979, we believe we have no exposure to asbestos or environmental pollution liabilities.

### **Reinsurance**

We reinsure with other insurance companies a portion of our potential liability under the policies we have underwritten, thereby protecting us against an unexpectedly large loss or a catastrophic occurrence that could produce large losses, primarily in our homeowners line of business. Reinsurance involves an insurance company transferring (ceding) a portion of its exposure on insurance underwritten by it to another insurer (reinsurer). The reinsurer assumes a portion of the exposure in return for a share of the premium. Reinsurance does not legally discharge an insurance company from its primary liability for the full amount of the policies, but it does make the reinsurer liable to the company for the reinsured portion of any loss realized.

We are selective in choosing our reinsurers, seeking only those companies that we consider to be financially stable and adequately capitalized. In an effort to minimize exposure to the insolvency of a reinsurer, we continuously evaluate and review the financial condition of our reinsurers. Swiss Re, our primary reinsurer, maintains an A.M. Best rating of "A" (Excellent). Most of our reinsurers have an A.M. Best rating of "A" (Excellent), however in no case is a reinsurer rated below "A-" (Excellent).

We maintain reinsurance coverage to help lessen the effect of losses from catastrophic events, maintaining coverage that during 2010 protected us in the event of a "140-year storm" (that is, a storm of a severity expected to occur once in a 140 year period). We use various software products to measure our exposure to catastrophe losses and the probable maximum loss to us for catastrophe losses such as hurricanes. The models include estimates for our share of the catastrophe losses generated in the residual market for property insurance by the Massachusetts Property Insurance Underwriting Association ("FAIR Plan"). In 2010, we purchased four layers of excess catastrophe reinsurance providing coverage for property losses in excess of \$30,000 up to a maximum of \$450,000. Our reinsurers' co-participation is 85.0% of \$50,000 for the 1<sup>st</sup> layer, 85.0% of \$70,000 for the 2<sup>nd</sup> layer, 80.0% of \$250,000 for the 3<sup>rd</sup> layer, and 80.0% of \$50,000 for the 4<sup>th</sup> layer.

In the aftermath of Hurricane Katrina in 2005, the reinsurance market has seen from the various software modelers, increases in the estimate of damage from hurricanes in the southern and northeast portions of the United States due to revised estimations of increased hurricane activity and increases in cost of repairs due to increased estimates in the amount of "demand surge" in the periods following a significant event. While we have continued to manage our exposure to catastrophes such as hurricanes, the changes to the various software models during the past few years, and again in 2010, have increased our modeled probable maximum loss due to catastrophic events. We continue to adjust our reinsurance programs as a result of the changes to the models. For 2011, we have purchased four layers of excess catastrophe reinsurance providing coverage for property losses in excess of \$30,000 up to a maximum of \$535,000. Our reinsurers' co-participation is 85.0% of \$50,000 for the 1<sup>st</sup> layer, 85.0% of \$80,000 for the 2<sup>nd</sup> layer, 80.0% of \$250,000 for the 3<sup>rd</sup> layer, and 80.0% of \$125,000 for the 4<sup>th</sup> layer. As a result of these changes to the models, and our revised reinsurance program, we maintain coverage that protects us in the event of a "140-year storm" (that is, a storm of a severity expected to occur once in a 140 year period).



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We also have casualty excess of loss reinsurance for large casualty losses occurring in our automobile, homeowners, dwelling fire, business owners, and commercial package lines of business in excess of \$2,000 up to a maximum of \$10,000. We have property excess of loss reinsurance coverage for large property losses, with coverage in excess of \$2,000 up to a maximum of \$15,000, for our homeowners, business owners, and commercial package policies. In addition, we have a quota share reinsurance agreement for personal and commercial umbrella lines of business under which we ceded 80.0% of the premiums for 2010. Effective January 1, 2011 we have ended our quota share agreement and we have purchased excess of loss reinsurance for umbrella large losses in excess of \$1,000 up to a maximum of \$5,000. We also have various reinsurance agreements with Hartford Steam Boiler Inspection and Insurance Company, of which the primary contract is a quota share agreement under which we cede 100% of the premiums and losses for the equipment breakdown coverage under our business owner policies and commercial package policies.

In the wake of the September 11, 2001 tragedies, reinsurers have begun to exclude coverage for claims in connection with any act of terrorism. Our reinsurance program excludes coverage for acts of terrorism, except for fire or collapse losses as a result of terrorism, under homeowners, dwelling fire, private passenger automobile and commercial automobile policies. For business owner policies and commercial package policies, terrorism is excluded if the total insured value is greater than \$20,000.

The Terrorism Risk Insurance Act of 2002 ("TRIA") was signed into law on November 26, 2002, and expired December 31, 2005. The Terrorism Risk Insurance Extension Act of 2005 was signed into law on December 22, 2005, and expired December 31, 2007. The Terrorism Risk Insurance Extension Act of 2007 ("TRIEA") was signed into law on December 26, 2007 which reauthorized TRIA for seven years, expanded the definition of an "Act of Terrorism" while expanding the private sector role and reducing the federal share of compensation for insured losses under the program. The intent of this legislation is to provide federal assistance to the insurance industry for the needs of commercial insurance policyholders with the potential exposure for losses due to acts of terrorism. The TRIEA provides reinsurance for certified acts of terrorism. Effective January 1, 2008, we began to issue policy endorsements for all commercial policyholders to comply with TRIA after obtaining the Commissioner's approval.

In addition to the above mentioned reinsurance programs and as described in more detail above under *The Massachusetts Property and Casualty Insurance Market*, we are a participant in CAR, the Massachusetts mandated residual market under which premiums, expenses, losses and loss adjustment expenses on ceded business are shared by all insurers writing automobile insurance in Massachusetts. This residual market mechanism is being phased out, as described earlier. We also participate in the Massachusetts Property Insurance Underwriting Association in which premiums, expenses, losses and loss adjustment expenses on homeowners business that cannot be placed in the voluntary market are shared by insurers writing homeowners insurance in Massachusetts. The FAIR Plan has grown dramatically over the past few years as insurance carriers have reduced their exposure to coastal property. The FAIR Plan's exposure to catastrophe losses increased and as a result, the FAIR Plan decided to buy reinsurance to reduce their exposure to catastrophe losses. On July 1, 2010, the FAIR Plan purchased \$1,000,000 of catastrophe reinsurance for property losses in excess of \$200,000. As of December 31, 2010, we had no material amounts recoverable from any reinsurer, excluding \$44,897 recoverable from CAR.

On March 10, 2005, our Board of Directors adopted a resolution that prohibits Safety from purchasing finite reinsurance (reinsurance that transfers only a relatively finite or limited amount of risk to the reinsurer) without approval by the Board. To date, the Company has never purchased a finite reinsurance contract.

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**Competition**

The property and casualty insurance business is highly competitive and many of our competitors have substantially greater financial and other resources than we do. We compete with both large national writers and smaller regional companies. Our competitors include companies which, like us, serve the independent agency market, as well as companies which sell insurance directly to customers. Direct writers may have certain competitive advantages over agency writers, including increased name recognition, loyalty of the customer base to the insurer rather than to an independent agency and potentially, lower cost structures. A material reduction in the amount of business independent agents sell would adversely affect us. Further, we and others compete on the basis of the commissions and other cash and non-cash incentives provided to agents. Although historically, a number of national insurers that are much larger than we are have chosen not to compete in a material way in the Massachusetts private passenger automobile market, if one or more of these companies decided to aggressively enter the market it could have a material adverse effect on us. The Commissioner announced that Managed Competition reforms were, in part, designed to make Massachusetts more appealing to these companies. Since 2008, new companies have entered the market including Progressive Insurance Company, Peerless (a subsidiary of Liberty Mutual), AIG, Vermont Mutual, Preferred Mutual, IDS, Occidental, GEICO, Harleysville, Foremost and Allstate. These companies include some that would be able to sustain significant losses in order to acquire market share, as well as others which use distribution methods that compete with the independent agent channel. There can be no assurance that we will be able to compete effectively against these companies in the future.

Our principal competitors within the Massachusetts private passenger automobile insurance market are, Commerce Group, Inc., Liberty Mutual (including Peerless) and Arbella Insurance Group, which held 29.9%, 10.9% and 9.7% market shares based on automobile exposures, respectively, in 2010 according to CAR.

**Employees**

At December 31, 2010, we employed 581 employees. Our employees are not covered by any collective bargaining agreement. Management considers our relationship with our employees to be good.

**Investments**

Investment income is an important source of revenue for us and the return on our investment portfolio has a material effect on our net earnings. Our investment objective is to focus on maximizing total returns while investing conservatively. We maintain a high quality investment portfolio consistent with our established investment policy. As of December 31, 2010, all securities in our fixed income securities portfolio were rated investment grade by Moody's, except for one security which represented less than 0.1% of our portfolio and approximately 4.1% of our portfolio which Moody's does not rate. According to our investment guidelines, no more than 2.0% of our portfolio may be invested in the securities of any one issuer (excluding U.S. government backed securities). This one issuer must be rated "A" or above by Moody's. In addition, no more than 0.5% of our portfolio may be invested in securities of any one issuer rated "Baa," or the lowest investment grade assigned by Moody's. We continually monitor the mix of taxable and tax-exempt securities in an attempt to maximize our total after-tax return. Since 1986, we have utilized the services of a third-party investment manager.

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The following table reflects the composition of our investment portfolio as of December 31, 2010 and 2009:

	As of December 31,			
	2010		2009	
	Estimated Fair Value	% of Portfolio	Estimated Fair Value	% of Portfolio
U.S. Treasury Securities	\$ 86,269	8.0%	\$ 12,532	1.2%
Obligations of states and political subdivisions	445,190	41.2	483,421	47.0
Residential mortgage-backed securities(1)	252,661	23.4	300,461	29.2
Commercial mortgage-backed securities	63,591	5.9	72,916	7.1
Other asset-backed securities	17,405	1.6	22,300	2.2
Corporate and other securities	198,121	18.3	126,699	12.3
Subtotal, fixed maturity securities	1,063,237	98.4	1,018,329	99.0
Equity securities(2)	14,624	1.4	9,876	1.0
Other invested assets	2,817	0.2	409	
Totals	\$ 1,080,678	100.0%	\$ 1,028,614	100.0%

(1) Residential mortgage-backed securities consists primarily of obligations of U.S. Government agencies including collateralized mortgage obligations and mortgage-backed securities guaranteed and/or insured by the following issuers: Government National Mortgage Association (GNMA), Federal Home Loan Mortgage Corporation (FHLMC), Federal National Mortgage Association (FNMA) and the Federal Home Loan Bank (FHLB). The total of these fixed maturity securities was \$237,335 and \$289,447 at amortized cost and \$252,592 and \$300,172 at fair value as of December 31, 2010 and 2009, respectively.

(2) Equity securities include interest in mutual funds of \$11,210 and \$9,736 at cost and \$11,699 and \$9,876 at fair value as of December 31, 2010 and 2009, respectively.

The principal risks inherent in holding mortgage-backed securities and other pass-through securities are prepayment and extension risks, which affect the timing of when cash flows will be received. When interest rates decline, mortgages underlying mortgage-backed securities tend to be prepaid more rapidly than anticipated, causing early repayments. When interest rates rise, the underlying mortgages tend to be prepaid at a slower rate than anticipated, causing the principal repayments to be extended. Although early prepayments may result in acceleration of income from recognition of any unamortized discount, the proceeds typically are reinvested at a lower current yield, resulting in a net reduction of future investment income. In addition, in the current market environment, such investments can also contain liquidity risks.

Equity risk is the risk that we will incur economic losses due to adverse changes in equity prices. Our exposure to changes in equity prices results from our holdings of common stock and mutual funds held to fund the executive deferred compensation plan. We continuously evaluate market conditions and we expect in the future to purchase additional equity securities. We principally manage equity price risk through industry and issuer diversification and asset allocation techniques.

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The following table reflects our investment results for each year in the three-year period ended December 31, 2010:

	Years Ended December 31,		
	2010	2009	2008
Average cash and invested securities (at cost)	\$ 1,069,858	\$ 1,061,916	\$ 1,060,554
Net investment income(1)	\$ 41,395	\$ 43,308	\$ 45,771
Net effective yield(2)	3.9%	4.1%	4.3%

(1) After investment expenses, excluding realized investment gains or losses.

(2) Net investment income for the period divided by average invested securities and cash for the same period.

Net effective annual yield declined in 2010 to 3.9% from 4.1% in 2009 and 4.3% in 2008. The 2010 and 2009 decreases primarily resulted from lower short-term interest rates, risk reduction actions related to municipal bonds, and ongoing maintenance of short duration to protect the portfolio from rising interest rates.

As of December 31, 2010, our portfolio of fixed maturity investments was comprised entirely of investment grade corporate fixed maturity securities, U.S. government and agency securities and asset-backed securities, except the few securities not rated by Moody's and one security representing less than 0.1% of our portfolio.

The composition of our fixed income security portfolio by Moody's rating was as follows:

	As of December 31, 2010	
	Estimated Fair Value	Percent
U.S. Treasury securities and obligations of U.S. Government agencies	\$ 349,168	32.8%
Aaa/Aa	491,480	46.2
A	122,440	11.5
Baa	57,054	5.4
Ba	328	
Not rated(1)	42,767	4.1
Total	\$ 1,063,237	100.0%

(1) Not rated by Moody's (Rated investment grade by Standard & Poor's).

Ratings are assigned by Moody's as discussed above. Such ratings are generally assigned upon the issuance of the securities and are subject to revision on the basis of ongoing evaluations. Ratings in the table are as of the date indicated.

Moody's rating system utilizes nine symbols to indicate the relative investment quality of a rated bond. Aaa rated bonds are judged to be of the best quality and are considered to carry the smallest degree of investment risk. Aa rated bonds are also judged to be of high quality by all standards. Together with Aaa bonds, these bonds comprise what are generally known as high grade bonds. Bonds rated A possess many favorable investment attributes and are considered to be upper medium grade obligations. Baa rated bonds are considered as medium grade obligations; they are neither highly protected nor poorly secured. Bonds rated Ba or lower (those rated B, Caa, Ca and C) are considered to be too speculative to be of investment quality.

The Securities Valuation Office of the National Association of Insurance Commissioners (the "SVO") evaluates all public and private bonds purchased as investments by insurance companies. The



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SVO assigns one of six investment categories to each security it reviews. Category 1 is the highest quality rating and Category 6 is the lowest. Categories 1 and 2 are the equivalent of investment grade debt as defined by rating agencies such as Standard & Poor's Ratings Services and Moody's, while Categories 3-6 are the equivalent of below investment grade securities. SVO ratings are reviewed at least annually. At December 31, 2010, 94.4% of our available for sale fixed maturity investments were rated Category 1 and 5.5% were rated Category 2, the two highest ratings assigned by the SVO. One security which represents less than 0.1% of our available for sale fixed maturity investments was rated Category 3 by the SVO.

The following table indicates the composition of our fixed income security portfolio (at carrying value) by time to maturity as of December 31, 2010.

	As of December 31, 2010	
	Estimated Fair Value	Percent
Due in one year or less	\$ 91,803	8.6%
Due after one year through five years	268,862	25.3
Due after five years through ten years	248,919	23.4
Due after ten years through twenty years	111,030	10.4
Due after twenty years	8,966	0.8
Asset-backed securities(1)	333,657	31.5
<b>Total</b>	<b>\$ 1,063,237</b>	<b>100.0%</b>

(1)

Actual maturities of asset-backed securities differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties. Prepayment rates are influenced by a number of factors that cannot be predicted with certainty, including: the relative sensitivity of the underlying mortgages or other collateral to changes in interest rates; a variety of economic, geographic and other factors; and the repayment priority of the securities in the overall securitization structures.

### Ratings

A.M. Best, which rates insurance companies based on factors of concern to policyholders, currently assigns Safety Insurance an "A (Excellent)" rating. Our "A" rating was reaffirmed by A.M. Best on April 27, 2010. Such rating is the third highest rating of 13 ratings that A.M. Best assigns to solvent insurance companies, which currently range from "A++ (Superior)" to "D (Very Vulnerable)." Publications of A.M. Best indicate that the "A" rating is assigned to those companies that in A.M. Best's opinion have a strong ability to meet their obligations to policyholders over a long period of time. In evaluating a company's financial and operating performance, A.M. Best reviews the Company's profitability, leverage and liquidity, as well as its book of business, the adequacy and soundness of its reinsurance, the quality and estimated fair value of its assets, the adequacy of its loss reserves, the adequacy of its surplus, its capital structure, the experience and competence of its management and its market presence. A.M. Best's ratings reflect its opinion of an insurance company's financial strength, operating performance and ability to meet its obligations to policyholders and are not evaluations directed to purchasers of an insurance company's securities.

In assigning Safety Insurance's rating, A.M. Best recognized its strong risk-adjusted capitalization and its favorable operating performance and market position as a leading personal automobile writer in Massachusetts. A.M. Best also noted among our positive attributes: sustained operating profitability in recent years; our disciplined underwriting approach; and expertise in the highly regulated Massachusetts automobile insurance industry. A.M. Best cited other factors that partially offset these positive

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attributes, including our concentration of business in the Massachusetts private passenger automobile market which exposes our business to regulatory actions.

**Supervision and Regulation**

*Introduction.* Our principal operations are conducted through the Insurance Subsidiaries which are subject to comprehensive regulation by the Division of Insurance, of which the Commissioner is the senior official. The Commissioner is appointed by the Governor. We are subject to the authority of the Commissioner in many areas of our business under Massachusetts law, including:

our licenses to transact insurance;

the premium rates and policy forms we may use;

our financial condition including the adequacy of our reserves and provisions for unearned premium;

the solvency standards that we must maintain;

the type and size of investments we may make;

the prescribed or permitted statutory accounting practices we must use; and

the nature of the transactions we may engage in with our affiliates.

In addition, the Commissioner periodically conducts a financial examination of all licensees domiciled in Massachusetts. We were most recently examined for the five-year period ending December 31, 2008. The Division had no material findings as a result of this examination.

*Insurance Holding Company Regulation.* Our principal operating subsidiaries are insurance companies, and therefore we are subject to certain laws in Massachusetts regulating insurance holding company systems. These laws require that we file a registration statement with the Commissioner that discloses the identity, financial condition, capital structure and ownership of each entity within our corporate structure and any transactions among the members of our holding company system. In some instances, we must provide prior notice to the Commissioner for material transactions between our insurance company subsidiaries and other affiliates in our holding company system. These holding company statutes also require, among other things, prior approval of the payment of extraordinary dividends or distributions and any acquisition of a domestic insurer.

*Insurance Regulation Concerning Dividends.* We rely on dividends from the Insurance Subsidiaries for our cash requirements. The insurance holding company law of Massachusetts requires notice to the Commissioner of any dividend to the shareholders of an insurance company. The Insurance Subsidiaries may not make an "extraordinary dividend" until thirty days after the Commissioner has received notice of the intended dividend and has not objected in such time. As historically administered by the Commissioner, this provision requires the prior approval by the Commissioner of an extraordinary dividend. An extraordinary dividend is defined as any dividend or distribution that, together with other distributions made within the preceding twelve months exceeds the greater of 10% of the insurer's surplus as of the preceding December 31, or the insurer's net income for the twelve-month period ending the preceding December 31, in each case determined in accordance with statutory accounting practices. Under Massachusetts law, an insurer may pay cash dividends only from its unassigned funds, also known as its earned surplus, and the insurer's remaining surplus must be both reasonable in relation to its outstanding liabilities and adequate to its financial needs. At year-end 2010, the statutory surplus of Safety Insurance was \$582,432 and its net income for 2010 was \$51,560. A maximum of \$58,243 will be available during 2011 for such dividends without prior approval of the Commissioner.





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*Acquisition of Control of a Massachusetts Domiciled Insurance Company.* Massachusetts law requires advance approval by the Commissioner of any change in control of an insurance company that is domiciled in Massachusetts. That law presumes that control exists where any person, directly or indirectly, owns, controls, holds the power to vote or holds proxies representing 10% or more of our outstanding voting stock. Even persons who do not acquire beneficial ownership of more than 10% of the outstanding shares of our common stock may be deemed to have acquired control if the Commissioner determines that control exists in fact. Any purchaser of shares of common stock representing 10% or more of the voting power of our capital stock will be presumed to have acquired control of the Insurance Subsidiaries unless, following application by that purchaser the Commissioner determines that the acquisition does not constitute a change of control or is otherwise not subject to regulatory review. These requirements may deter, delay or prevent transactions affecting the control of or the ownership of our common stock, including transactions that could be advantageous to our stockholders.

*Protection Against Insurer Insolvency.* Massachusetts law requires that insurers licensed to do business in Massachusetts participate in the Massachusetts Insurers Insolvency Fund ("Insolvency Fund"). The Insolvency Fund must pay any claim up to \$300 of a policyholder of an insolvent insurer if the claim existed prior to the declaration of insolvency or arose within sixty days after the declaration of insolvency. Members of the Insolvency Fund are assessed the amount the Insolvency Fund deems necessary to pay its obligations and expenses in connection with handling covered claims. Subject to certain exceptions, assessments are made in the proportion that each member's net written premiums for the prior calendar year for all property and casualty lines bore to the corresponding net written premiums for Insolvency Fund members for the same period. As a matter of Massachusetts law, insurance rates and premiums include amounts to recoup any amounts paid by insurers for the costs of the Insolvency Fund. By statute, no insurer in Massachusetts may be assessed in any year an amount greater than two percent of that insurer's direct written premium for the calendar year prior to the assessment. We account for allocations from the Insolvency Fund as underwriting expenses. CAR also assesses its members as a result of insurer insolvencies. Because CAR is not able to recover an insolvent company's share of the net CAR losses from the Insolvency Fund, CAR must increase each of its member's share of the deficit in order to compensate for the insolvent carrier's inability to pay its deficit assessment. It is anticipated that there will be future assessments from time to time relating to various insolvencies.

*The Insurance Regulatory Information System.* The Insurance Regulatory Information System ("IRIS") was developed to help state regulators identify companies that may require special financial attention. IRIS consists of a statistical phase and an analytical phase whereby financial examiners review annual statements and financial ratios. The statistical phase consists of 13 key financial ratios based on year-end data that are generated annually from the database of the National Association of Insurance Commissioners ("NAIC"). Each ratio has an established "usual range" of results. These ratios assist state insurance departments in executing their statutory mandate to oversee the financial condition of insurance companies.

A ratio result falling outside the usual range of IRIS ratios is not considered a failing result; rather, unusual values are viewed as part of the regulatory early monitoring system. Furthermore, in some years, it may not be unusual for financially sound companies to have several ratios with results outside the usual ranges. Generally, an insurance company will become subject to regulatory scrutiny if it falls outside the usual ranges of four or more of the ratios. In 2010 and 2009, all our ratios for all our Insurance Subsidiaries were within the normal range. In 2008, all our ratios for all our Insurance Subsidiaries were within the normal range, with the exception of Change in Net Premiums Written for Safety P&C. The unusual value resulted due to a one-time prospective adjustment made to premiums effective January 1, 2007 related to Safety P&C's entry to the intercompany pooling arrangement among the Insurance Subsidiaries.

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*Risk Based Capital Requirements.* The NAIC has adopted a formula and model law to implement risk based capital requirements for most property and casualty insurance companies, which are designed to determine minimum capital requirements and to raise the level of protection that statutory surplus provides for policyholder obligations. The risk based capital formula for property and casualty insurance companies measures three major areas of risk facing property and casualty insurers:

underwriting, which encompasses the risk of adverse loss developments and inadequate pricing;

declines in asset values arising from market and/or credit risk; and

off-balance sheet risk arising from adverse experience from non-controlled assets, guarantees for affiliates or other contingent liabilities and reserve and premium growth.

Under Massachusetts law, insurers having less total adjusted capital than that required by the risk based capital calculation will be subject to varying degrees of regulatory action, depending on the level of capital inadequacy.

The risk based capital law provides for four levels of regulatory action. The extent of regulatory intervention and action increases as the level of total adjusted capital to risk based capital falls. The first level, the company action level, as defined by the NAIC, requires an insurer to submit a plan of corrective actions to the Commissioner if total adjusted capital falls below 200% of the risk based capital amount. The regulatory action level, as defined by the NAIC requires an insurer to submit a plan containing corrective actions and requires the Commissioner to perform an examination or other analysis and issue a corrective order if total adjusted capital falls below 150% of the risk based capital amount. The authorized control level, as defined by the NAIC, authorizes the Commissioner to take whatever regulatory actions he or she considers necessary to protect the best interest of the policyholders and creditors of the insurer which may include the actions necessary to cause the insurer to be placed under regulatory control, i.e., rehabilitation or liquidation, if total adjusted capital falls below 100% of the risk based capital amount. The fourth action level is the mandatory control level, as defined by the NAIC, which requires the Commissioner to place the insurer under regulatory control if total adjusted capital falls below 70% of the risk based capital amount.

The formulas have not been designed to differentiate among adequately capitalized companies that operate with higher levels of capital. Therefore, it is inappropriate and ineffective to use the formulas to rate or to rank these companies. At December 31, 2010, our Insurance Subsidiaries had total adjusted capital in excess of amounts requiring company or regulatory action at any prescribed risk based capital action level.

*Regulation of Private Passenger Automobile Insurance in Massachusetts.* Our principal line of business is Massachusetts private passenger automobile insurance. As described in more detail above under *The Massachusetts Property and Casualty Insurance Market*, prior to April 1, 2008, regulation of private passenger automobile insurance in Massachusetts differed significantly from how this line of insurance is regulated in other states. These differences included the requirements that the premium rate we and all insurers must charge was fixed and established by the Commissioner, that our ability and that of our competitors to deviate from the rate set by the Commissioner was restricted, and that some of our insurance producers are assigned to us as a matter of law. Beginning April 1, 2008, Massachusetts moved to Managed Competition and transitioned to an assigned risk plan. See *The Massachusetts Property and Casualty Insurance Market*, as discussed above.

*Dodd-Frank Wall Street Reform and Consumer Protection Act.* On July 21, 2010, the Dodd-Frank Wall Street Reform and Consumer Protection Act (the "Reform Act") was signed into law. The Reform Act makes sweeping changes to the regulation of financial services entities, products and markets. Although the provisions of the bill do not appear to directly affect our business, as detailed regulations are developed to implement the provisions of the bill, there may be changes in the regulatory environment that affect the way we conduct our operations or the cost of compliance, or both.

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The table below sets forth certain information concerning our directors and executive officers as of the date of this annual report.

<b>Name</b>	<b>Age</b>	<b>Position</b>	<b>Years Employed by Safety</b>
David F. Brussard	59	President, Chief Executive Officer and Chairman of the Board	35
William J. Begley, Jr.	56	Vice President, Chief Financial Officer and Secretary	25
James D. Berry	51	Vice President Insurance Operations	28
George M. Murphy	44	Vice President Marketing	22
Robert J. Kerton	64	Vice President Claims	24
David E. Krupa	50	Vice President Claims Operations	28
Daniel D. Loranger	71	Vice President Management Information Systems and Chief Information Officer	30
Edward N. Patrick, Jr.	62	Vice President Underwriting	37
A. Richard Caputo, Jr.	45	Director	
Frederic H. Lindeberg	70	Director	
Peter J. Manning	72	Director	
David K. McKown	73	Director	

*David F. Brussard* was appointed Chairman of the Board in March 2004 and President and Chief Executive Officer ("CEO") in June 2001. Mr. Brussard has served as a Director of the Company since October 2001. Since January 1999, Mr. Brussard has been the CEO and President of the Insurance Subsidiaries. Previously, Mr. Brussard served as Executive Vice President of the Insurance Subsidiaries from 1985 to 1999 and as Chief Financial Officer and Treasurer of the Insurance Subsidiaries from 1979 to 1999. Mr. Brussard has been employed by one or more of our subsidiaries for over 35 years. Mr. Brussard is also Chairman of the Governing Committee and a member of the Budget Committee, Executive Committee and Nominating Committee of the Automobile Insurers Bureau of Massachusetts. Mr. Brussard is also on the Board of Trustees of the Insurance Library Association of Boston.

*William J. Begley, Jr.* was appointed Chief Financial Officer, Vice President and Secretary of the Company on March 4, 2002. Since January 1999, Mr. Begley has been the Chief Financial Officer and Treasurer of the Insurance Subsidiaries. Previously, Mr. Begley served as Assistant Controller of the Insurance Subsidiaries from 1985 to 1987, as Controller from 1987 to 1990 and as Assistant Vice President/Controller from 1990 to 1999. Mr. Begley has been employed by the Insurance Subsidiaries for over 25 years. Mr. Begley also serves on the Audit Committee of Guaranty Fund Management Services, and is a member of the Board of Directors of the Massachusetts Insurers Insolvency Fund.

*James D. Berry, CPCU* was appointed Vice President of Insurance Operations of the Company on October 1, 2005. Mr. Berry has been employed by the Insurance Subsidiaries for over 28 years and has directed the Company's Massachusetts Private Passenger line of business since 2001. Mr. Berry represents Safety on the Computer Sciences Corporation Series II Advisory Council.

*George M. Murphy, CPCU*, was appointed Vice President of Marketing on October 1, 2005. Mr. Murphy has been employed by the Insurance Subsidiaries for over 22 years and most recently served as Director of Marketing.

*Robert J. Kerton* was appointed Vice President of Casualty Claims of the Company on March 4, 2002. Mr. Kerton has served as Vice President of Claims of the Insurance Subsidiaries since 1986 and has been employed by the Insurance Subsidiaries for over 24 years. Mr. Kerton previously served 18 years with Allstate Insurance Company in various Massachusetts claim management assignments.

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Mr. Kerton has served as Chairman of the Claims Committee of the Automobile Insurers Bureau of Massachusetts, and he is a member of the Governing Board of the Massachusetts Insurance Fraud Bureau.

*David E. Krupa, CPCU*, was appointed Vice President of Property Claims of the Company on March 4, 2002. Mr. Krupa has served as Vice President of Claims of the Insurance Subsidiaries since July 1990 and has been employed by the Insurance Subsidiaries for over 28 years. Mr. Krupa was first employed by the Company in 1982 and held a series of management positions in the Claims Department before being appointed Vice President in 1990. Mr. Krupa is a member of the Auto Damage Appraisers Licensing Board of Massachusetts. In addition, Mr. Krupa has been a member of several claims committees both at the Automobile Insurers Bureau of Massachusetts and CAR.

*Daniel D. Loranger* was appointed Vice President of Management Information Systems of the Company on March 4, 2002. Mr. Loranger has served as Vice President of Management Information Systems and Chief Information Officer of the Insurance Subsidiaries since 1980 and has been employed by the Insurance Subsidiaries for over 30 years. Mr. Loranger began his data processing career with Raytheon Manufacturing in 1960.

*Edward N. Patrick, Jr.* was appointed Vice President of Underwriting of the Company on March 4, 2002. Mr. Patrick has served as Vice President of Underwriting of the Insurance Subsidiaries since 1979 and as Secretary since 1999. He has been employed by one or more of our subsidiaries for over 37 years. Mr. Patrick has served on several committees of CAR, including the MAIP Steering, Actuarial, Market Review, Servicing Carrier, Statistical, Automation, Reinsurance and Operations Committee. Mr. Patrick is also on the Board of Directors of the Massachusetts Property Insurance Underwriting Association (FAIR Plan).

*A. Richard Caputo, Jr.* has served as a director of the Company since June 2001. Mr. Caputo is a managing principal of The Jordan Company, a private investment firm, which he has been with since 1990. Mr. Caputo is also a director of TAL International, Inc., Universal Technical Institute, Inc. and various privately held companies.

*Frederic H. Lindeberg* has served as a director of the Company since August 2004. Mr. Lindeberg has had a consulting practice providing taxation, management and investment counsel since 1991, focusing on finance, real estate, manufacturing and retail industries. Mr. Lindeberg retired in 1991 as Partner-In-Charge of various KPMG tax offices, after 24 years of service where he provided both accounting and tax counsel to various clients. Mr. Lindeberg was formerly an adjunct professor at Penn State Graduate School of Business. Mr. Lindeberg is currently a director of TAL International, Inc.

*Peter J. Manning* has served as a director of the Company since September 2003. Mr. Manning retired in 2003 as Vice Chairman of FleetBoston Financial, after 31 years with FleetBoston Financial Corporation (formerly BankBoston) where he also held the positions of Comptroller and Executive Vice President and Chief Financial Officer. Mr. Manning started his career with Coopers & Lybrand in 1962 prior to his 1972 employment with BankBoston. He currently is a director of Thermo Fisher Scientific, the non-profit Catholic Schools Foundation, the Hyde Park Savings Bank and the Lahey Clinic.

*David K. McKown* has served as director of the Company since November 2002. Mr. McKown has been a Senior Advisor to Eaton Vance Management since 2000, focusing on business origination in real estate and asset-based loans. Mr. McKown retired in March 2000 having served as a Group Executive with BankBoston since 1993, where he focused on acquisitions and high-yield bank debt financings. Mr. McKown has been in the banking industry for 51 years, worked for BankBoston for over 32 years and had previously been the head of BankBoston's real estate department, corporate finance

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department, and a managing director of BankBoston's private equity unit. Mr. McKown is currently a director of Global Partners L.P., Newcastle Investment Corp., and various privately held companies.

**ITEM 1A. RISK FACTORS**

*An investment in our common stock involves a number of risks. Any of the risks described below could result in a significant or material adverse effect on our results of operations or financial condition, and a corresponding decline in the market price of our common stock.*

***Because we are primarily a private passenger automobile insurance carrier, our business may be adversely affected by conditions in this industry.***

Approximately 68.7% of our direct written premiums for the year ended December 31, 2010, were generated from private passenger automobile insurance policies. As a result of our focus on that line of business, negative developments in the economic, competitive or regulatory conditions affecting the private passenger automobile insurance industry could have a material adverse effect on our results of operations and financial condition. In addition, these developments would have a disproportionate effect on us, compared to insurers which conduct operations in multiple business lines.

***Because we write insurance principally in Massachusetts, our business may be adversely affected by conditions in Massachusetts, including the potential effect of the Commissioner's new Managed Competition.***

Almost all of our direct written premiums are currently generated in Massachusetts. Our revenues and profitability are therefore subject to prevailing regulatory, economic, demographic, competitive and other conditions in Massachusetts. Changes in any of these conditions could make it more costly or difficult for us to conduct our business. Massachusetts has recently enacted significant changes to the regulatory framework relating to private passenger automobile insurance. These changes include rate competition and restructuring the private passenger automobile insurance residual market. The Commissioner intends that these changes will increase competition and result in lower premiums in private passenger automobile insurance in the state. We cannot estimate how these regulatory changes will affect our private passenger automobile insurance business over the longer term. Adverse results could include loss of market share, decreased revenue, and/or increased costs. Additional competitors have entered the market in response to these changes. In addition, these developments could have a disproportionate effect on us, compared to insurers which conduct operations in multiple states.

***We have exposure to claims related to severe weather conditions, which may result in an increase in claims frequency and severity.***

We are subject to claims arising out of severe weather conditions, such as rainstorms, snowstorms and ice storms, that may have a significant effect on our results of operations and financial condition. The incidence and severity of weather conditions are inherently unpredictable. There is generally an increase in claims frequency and severity under the private passenger automobile insurance we write when severe weather occurs because a higher incidence of vehicular accidents and other insured losses tend to occur as a result of severe weather conditions. In addition, we have exposure to an increase in claims frequency and severity under the homeowners and other property insurance we write because property damage may result from severe weather conditions.

Because some of our insureds live near the Massachusetts coastline, we also have a potential exposure to losses from hurricanes and major coastal storms such as Nor'easters. Although we purchase catastrophe reinsurance to limit our exposure to these types of natural catastrophes, in the event of a major catastrophe resulting in property losses to us in excess of \$535,000 our losses would exceed the limits of this reinsurance in addition to losses from our quota share retention of a portion of the risk up to \$535,000.

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***Climate change may adversely impact our results of operations.***

There are concerns that the increase in weather-related catastrophes and other losses incurred by the industry in recent years may be indicative of changing weather patterns. This change in weather patterns could lead to higher overall losses which we may not be able to recover, particularly in light of the current competitive environment, and higher reinsurance costs. Climate change could also have an impact on issuers of securities in which we invest, resulting in realized and unrealized losses in future periods which could have a material adverse impact on our results of operations and/or financial position.

***If we are not able to attract and retain independent agents, it could adversely affect our business.***

We market our insurance solely through independent agents. We must compete with other insurance carriers for the business of independent agents. Some of our competitors offer a larger variety of products, lower prices for insurance coverage or higher commissions. While we believe that the commissions and services we provide to our agents are competitive with other insurers, changes in commissions, services or products offered by our competitors could make it harder for us to attract and retain independent agents to sell our insurance products.

***Established competitors with greater resources may make it difficult for us to market our products effectively and offer our products at a profit.***

The property and casualty insurance business is highly competitive and many of our competitors have substantially greater financial and other resources than we do. We compete with both large national writers and smaller regional companies. Further, our competitors include other companies which, like us, serve the independent agency market, as well as companies which sell insurance directly to customers. Direct writers may have certain competitive advantages over agency writers, including increased name recognition, loyalty of the customer base to the insurer rather than to an independent agency and, potentially, lower cost structures. A material reduction in the amount of business independent agents sell would directly and negatively affect our profitability and our ability to compete with insurers that do not rely solely on the independent agency market to sell their products. Further, our Company and others compete on the basis of the commissions and other cash and non-cash incentives provided to agents. Although a number of national insurers that are much larger than we are do not currently compete in a material way in the Massachusetts personal auto market, if one or more of these companies decided to aggressively enter the market it could reduce our share of the Massachusetts market and thereby have a material adverse effect on us. These companies include some that would be able to sustain significant losses in order to acquire market share, as well as others which use distribution methods that compete with the independent agent channel. Progressive Corporation, GEICO and Allstate, large insurers that market directly to policyholders rather than through agents, along with other carriers have entered the Massachusetts private passenger automobile insurance market. We are unable to predict the long-term effects on our business of the new Managed Competition regulatory environment.

***As a holding company, Safety Insurance Group, Inc. is dependent on the results of operations of the Safety Insurance Company.***

Safety Insurance Group, Inc. is a company and a legal entity separate and distinct from Safety Insurance Company, our principal operating subsidiary. As a holding company without significant operations of its own, the principal sources of Safety Insurance Group, Inc.'s funds are dividends and other distributions from Safety Insurance Company. Our rights to participate in any distribution of assets of Safety Insurance Company are subject to prior claims of policyholders, creditors and preferred shareholders, if any, of Safety Insurance Company (except to the extent that our rights, if any, as a creditor are recognized). Consequently, our ability to pay debts, expenses and cash dividends to our

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shareholders may be limited. The ability of Safety Insurance Company to pay dividends is subject to limits under Massachusetts insurance law. Further, the ability of Safety Insurance Group, Inc. to pay dividends, and our subsidiaries' ability to incur indebtedness or to use the proceeds of equity offerings, will be subject to limits under our revolving credit facility.

***We are subject to comprehensive regulation by Massachusetts and our ability to earn profits may be restricted by these regulations.***

*General Regulation.* We are subject to regulation by government agencies in Massachusetts, and we must obtain prior approval for certain corporate actions. We must comply with regulations involving:

transactions between an insurance company and any of its affiliates;

the payment of dividends;

the acquisition of an insurance company or of any company controlling an insurance company;

approval or filing of premium rates and policy forms;

solvency standards;

minimum amounts of capital and surplus which must be maintained;

limitations on types and amounts of investments;

restrictions on the size of risks which may be insured by a single company;

limitation of the right to cancel or non-renew policies in some lines;

regulation of the right to withdraw from markets or terminate involvement with agencies;

requirements to participate in residual markets;

licensing of insurers and agents;

deposits of securities for the benefit of policyholders; and

reporting with respect to financial condition.

In addition, insurance department examiners from Massachusetts perform periodic financial and market conduct examinations of insurance companies. Such regulation is generally intended for the protection of policyholders rather than security holders.

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Massachusetts requires that all licensed property and casualty insurers bear a portion of the losses suffered by some insureds as a result of impaired or insolvent insurance companies by participating in the Massachusetts Insurers Insolvency Fund ("Insolvency Fund"). Members of the Insolvency Fund are assessed a proportionate share of the obligations and expenses of the Insolvency Fund in connection with an insolvent insurer. These assessments are made by the Insolvency Fund to cover the cost of paying eligible claims of policyholders of these insolvent insurers, and by CAR, to recover the shares of net CAR losses that would have been assessed to the insolvent companies but for their insolvencies. In addition, Massachusetts has established an underwriting association in order to ensure that property insurance is available for owners of high risk property who are not able to obtain insurance from private insurers. The losses of this underwriting association are shared by all insurers that write property and casualty insurance in Massachusetts. We are assessed from time to time to pay these losses. The effect of these assessments could reduce our profitability in any given period and limit our ability to grow our business.

Because we are unable to predict with certainty changes in the political, economic or regulatory environments in Massachusetts in the future, there can be no assurance that existing insurance-related



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laws and regulations will not become more restrictive in the future or that new restrictive laws will not be enacted and, therefore, it is not possible to predict the potential effects of these laws and regulations on us.

*Massachusetts Personal Auto Regulation.* We have been subject to the extensive regulation of the private passenger automobile insurance industry in Massachusetts. Owners of registered automobiles are required to maintain minimum automobile insurance coverages. Historically, we have been required by law to issue a policy to any applicant who seeks it. Prior to April 1, 2008, we were assigned certain agents that have been unable to obtain a voluntary contract with another insurer. We call these agents ERPs. In addition, we were required to participate in a state mandated reinsurance program run by CAR, to which we ceded certain undesirable risks and from which we are allocated a portion of the program's overall losses. On April 1, 2008, an assigned risk plan ("MAIP") for private passenger automobile insurance started a transition away from the prior system of ERPs assigned to Safety and began the assignment of individual risks to us. The MAIP was fully implemented April 1, 2009 and replaced CAR as the private passenger automobile insurance residual market in Massachusetts. These programs operate at an underwriting deficit and result in expense for us. Our ability to earn profits may be restricted by these requirements.

Our marketing and underwriting strategies had been limited by maximum premium rates and minimum agency commission levels for personal automobile insurance, which were mandated by the Commissioner prior to April 1, 2008. Under Massachusetts' Managed Competition regulations, we decreased our rates an average 6.7% effective in 2008. We filed modifications in our rating structure effective April 1, 2009 that included three rating tiers which resulted in no change in our average total rates. We filed and were approved for a 0.3% decrease in our rates effective June 1, 2009, a 2.9% rate increase in our rates effective October 1, 2009, and a fourth rating tier which resulted in an increase in our rates of 0.4% effective January 1, 2010. We filed and were approved for a 1.9% increase in our rates effective April 19, 2010 and we also filed and were approved for a 0.5% decrease in our rates effective June 15, 2010. In addition, prior to April 1, 2008, the Commissioner annually established the minimum commission rate that insurers must pay their auto insurance agents. The Commissioner approved a commission rate, as a percentage of premiums, of 13.0% in 2007 and we filed for and were approved for a commission rate of 13.0% for 2008, 2009 and 2010 beginning April 1, 2008.

***We may enter new markets and there can be no assurance that our diversification strategy will be effective.***

Although we intend to concentrate on our core businesses in Massachusetts, we also may seek to take advantage of prudent opportunities to expand our core businesses into other states where we believe the independent agent distribution channel is strong. As a result of a number of factors, including the difficulties of finding appropriate expansion opportunities and the challenges of operating in an unfamiliar market, we may not be successful in this diversification. Additionally, in order to carry out any such strategy we would need to obtain the appropriate licenses from the insurance regulatory authority of any such state.

On June 20, 2007, we applied for admission in the State of New Hampshire for a Certificate of Authority to transact insurance business. On October 16, 2007, the State of New Hampshire Insurance Department issued a Certificate of Authority for property and casualty insurance to each of the Insurance Subsidiaries. We began writing business in New Hampshire late in 2008.

***Our failure to maintain a commercially acceptable financial strength rating would significantly and negatively affect our ability to implement our business strategy successfully.***

A.M. Best has currently assigned Safety Insurance an "A (Excellent)" rating. An "A" rating is A.M. Best's third highest rating, out of 13 possible rating classifications for solvent companies. An "A" rating is assigned to insurers that in A.M. Best's opinion have a strong ability to meet their ongoing

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obligations to policyholders. Moreover, an "A" rating is assigned to companies that have, on balance, excellent balance sheet strength, operating performance and business profile when compared to the standards established by A.M. Best. A.M. Best bases its ratings on factors that concern policyholders and not upon factors concerning investor protection. Such ratings are subject to change and are not recommendations to buy, sell, or hold securities. An important factor in an insurer's ability to compete effectively is its A.M. Best rating. Our A.M. Best rating is lower than those of some of our competitors. Any future decrease in our rating could affect our competitive position.

***Our losses and loss adjustment expenses may exceed our reserves, which could significantly affect our business.***

The reserves for losses and loss adjustment expenses that we have established are estimates of amounts needed to pay reported and unreported claims and related expenses based on facts and circumstances known to us as of the time we established the reserves. Reserves are based on historical claims information, industry statistics and other factors. The establishment of appropriate reserves is an inherently uncertain process. If our reserves are inadequate and are strengthened, we would have to treat the amount of such increase as a charge to our earnings in the period that the deficiency is recognized. As a result of these factors, there can be no assurance that our ultimate liability will not materially exceed our reserves and have a negative effect on our results of operations and financial condition.

Due to the inherent uncertainty of estimating reserves, it has been necessary, and may over time continue to be necessary, to revise estimated future liabilities as reflected in our reserves for claims and policy expenses. The historic development of reserves for losses and loss adjustment expenses may not necessarily reflect future trends in the development of these amounts. Accordingly, it is not appropriate to extrapolate redundancies or deficiencies based on historical information.

***If we lose key personnel, our ability to implement our business strategy could be delayed or hindered.***

Our future success depends significantly upon the efforts of certain key management personnel, including David F. Brussard, our Chief Executive Officer and President. We have entered into employment agreements with Messrs. Brussard, Begley, Kerton, Krupa, Loranger, Patrick, Murphy, and Berry, the eight members of our Management Team. The loss of key personnel could prevent us from fully implementing our business strategy and could significantly and negatively affect our financial condition and results of operations. As we continue to grow, we will need to recruit and retain additional qualified management personnel, and our ability to do so will depend upon a number of factors, such as our results of operations and prospects and the level of competition then prevailing in the market for qualified personnel.

***Market fluctuations and changes in interest rates can have significant and negative effects on our investment portfolio.***

Our results of operations depend in part on the performance of our invested assets. As of December 31, 2010, based upon fair value measurement, 98.4% of our investment portfolio was invested in fixed maturity securities, 1.4% in common equity securities and 0.2% in other invested assets. Certain risks are inherent in connection with debt securities including loss upon default and price volatility in reaction to changes in interest rates and general market factors.

We have a significant investment portfolio and adverse capital market conditions, including but not limited to volatility and credit spread changes, will impact the liquidity and value of our investments, potentially resulting in higher realized or unrealized losses. Values of our investments can also be impacted by reductions in price transparency and changes in investor confidence and preferences, potentially resulting in higher realized or unrealized losses. If the carrying value of our investments

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exceeds the fair value, and the decline in fair value is deemed to be other-than-temporary, we will be required to write down the value of our investments, which could materially harm our results of operations and financial condition.

Developments in the global financial markets may adversely affect our investment portfolio and overall performance. Global financial markets have recently experienced unprecedented and challenging conditions. If conditions further deteriorate, our business could be affected in different ways. Continued turbulence in the U.S. economy and contraction in the credit markets could adversely affect our profitability, demand for our products or our ability to raise rates, and could also result in declines in market value and future impairments of our investment assets.

***We may not be able to successfully alleviate risk through reinsurance arrangements which could cause us to reduce our premiums written in certain lines or could result in losses.***

In order to reduce risk and to increase our underwriting capacity, we purchase reinsurance. The availability and the cost of reinsurance protection are subject to market conditions, which are outside of our control. As a result, we may not be able to successfully alleviate risk through these arrangements. For example, if reinsurance capacity for homeowner's risks were reduced as a result of terrorist attacks, climate change or other causes, we might seek to reduce the amount of homeowners business we write. In addition, we are subject to credit risk with respect to our reinsurance because the ceding of risk to reinsurers does not relieve us of our liability to our policyholders. A significant reinsurer's insolvency or inability to make payments under the terms of a reinsurance treaty could have a material adverse effect on our results of operations and financial condition.

***There are anti-takeover provisions contained in our organizational documents and in laws of the State of Delaware and the Commonwealth of Massachusetts that could impede an attempt to replace or remove our management or prevent the sale of our company, which could diminish the value of our common stock.***

Our certificate of incorporation, bylaws and the laws of Delaware contain provisions that may delay, deter or prevent a takeover attempt that shareholders might consider in their best interests. For example, our organizational documents provide for a classified board of directors with staggered terms, prevent shareholders from taking action by written consent, prevent shareholders from calling a special meeting of shareholders, provide for supermajority voting requirements to amend our certificate of incorporation and certain provisions of our bylaws and provide for the filling of vacancies on our board of directors by the vote of a majority of the directors then in office. These provisions will render the removal of the incumbent board of directors or management more difficult. In addition, these provisions may prevent shareholders from receiving the benefit of any premium over the market price of our common stock offered by a bidder in a potential takeover. Even in the absence of a takeover attempt, the existence of these provisions may adversely affect the prevailing market price of our common stock if they are viewed as discouraging takeover attempts in the future.

The Massachusetts insurance law prohibits any person from acquiring control of us, and thus indirect control of Safety Insurance Group, Inc., without the prior approval of the Commissioner. That law presumes that control exists where any person, directly or indirectly, owns, controls, holds the power to vote or holds proxies representing 10% or more of our outstanding voting stock. Even persons who do not acquire beneficial ownership of more than 10% of the outstanding shares of our common stock may be deemed to have acquired such control if the Commissioner determines that such control exists in fact. Therefore, any person seeking to acquire a controlling interest in us would face regulatory obstacles which could delay, deter or prevent an acquisition that shareholders might consider in their best interests.

Section 203 of the General Corporation Law of Delaware, the jurisdiction in which the Company is organized, may affect the ability of an "interested stockholder" to engage in certain business

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combinations including mergers, consolidations or acquisitions of additional shares, for a period of three years following the time that the stockholder becomes an interested stockholder. An interested stockholder is defined to include persons owning directly or indirectly 15% or more of the outstanding voting stock of the corporation.

***Future sales of shares of our common stock by our existing shareholders in the public market, or the possibility or perception of such future sales, could adversely affect the market price of our stock.***

Investors currently known to be the beneficial owners of greater than 5.0% of our outstanding common stock hold approximately 30.0% of the common stock of Safety Insurance Group, Inc. on a fully diluted basis. No prediction can be made as to the effect, if any, that future sales of shares by our existing shareholders, or the availability of shares for future sale, will have on the prevailing market price of our common stock from time to time. Sales of substantial amounts of our common stock in the public market by our existing shareholders, or the possibility or perception that such sales could occur, could cause the prevailing market prices for our common stock to decrease. If such sales reduce the market price of our common stock, our ability to raise additional capital in the equity markets may be adversely affected.

***Our business depends on the uninterrupted operation of our systems and business functions, including our information technology, telecommunications and other business systems. Our business continuity and disaster recovery plans may not sufficiently address all contingencies.***

Our business is highly dependent upon our ability to execute, in an efficient and uninterrupted fashion, necessary business functions, such as processing new and renewal business, providing customer service, and processing and paying claims. A shut-down of or inability to access our facility, a power outage, or a failure of one or more of our information technology, telecommunications or other systems could significantly impair our ability to perform such functions on a timely basis. If sustained or repeated, such a business interruption, systems failure or service denial could result in a deterioration in the level of service we provide to our agents and policyholders. We have established a business continuity plan in an effort to ensure the continuation of core business operations in the event that normal business operations could not be performed due to a catastrophic event. While we continue to test and assess our business continuity plan to ensure it meets the needs of our core business operations and addresses multiple business interruption events, there is no assurance that core business operations could be performed upon the occurrence of such an event, which may result in a material adverse effect on our financial position and results of operations.

***If we experience difficulties with outsourcing relationships, our ability to conduct our business might be negatively impacted.***

We outsource certain business and administrative functions to third parties and may do so increasingly in the future. If we fail to develop and implement our outsourcing strategies or our third-party providers fail to perform as anticipated, we may experience operational difficulties, increased costs and a loss of business that may have a material adverse effect on our results of operations or financial condition. By outsourcing certain business and administrative functions to third parties, we may be exposed to enhanced risk of data security breaches. Any breach of data security could damage our reputation and/or result in monetary damages, which, in turn, could have a material adverse effect on our results of operations or financial condition.

***ITEM 1B. UNRESOLVED STAFF COMMENTS***

As of the date of this report, the Company had no unresolved comments from the Commission staff regarding its periodic or current reports under the Exchange Act.

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**ITEM 2. PROPERTIES**

We conduct most of our operations in approximately 104 thousand square feet of leased space at 20 Custom House Street in downtown Boston, Massachusetts. Our lease expires in December 2018.

**ITEM 3. LEGAL PROCEEDINGS**

Our Insurance Subsidiaries are parties to a number of lawsuits arising in the ordinary course of their insurance business. We believe that the ultimate resolution of these lawsuits will not, individually or in the aggregate, have a material adverse effect on our financial condition.

In addition, on November 21, 2008, the Massachusetts Office of the Attorney General (the "AG") delivered a civil investigative demand (the "CID") to Safety Insurance. The CID directed the Company to produce certain information related to its policies and practices in connection with underwriting insurance policies on motorcycles and adjusting total loss claims under such policies. Other insurance companies are also being investigated by the AG related to their policies and practices related to motorcycle insurance.

On January 14, 2010, we announced that we had reached an agreement with the AG to change the way in which we calculated motorcycle premiums for certain types of coverage dating back to January 1, 2002. Under the terms of the settlement, we agreed to pay refunds to certain motorcycle policyholders. We deposited \$7,408 into a trust fund to be used to pay the amount of those refunds and paid \$330 to the Commonwealth of Massachusetts, which included reimbursement of costs and expenses related to the implementation of the settlement by the AG. Of the total settlement to date, \$7,547 was recorded as an increase to Underwriting, operating and other expenses for the year ended December 31, 2009 and \$191 of additional refunds subsequently identified by the AG and deposited to the trust fund by us in July 2010 was recorded as Underwriting, operating and other expenses for the year ended December 31, 2010.

We worked with the Attorney General's office to identify the policies on which refunds would be issued and the amount of refunds to be paid to each individual policyholder. During the quarter ended September 30, 2010, the Company first notified approximately 21 thousand policyholders of the amount of individual refunds offered and requested receipt of appropriate releases from them in order to access the trust fund to issue refund checks. As of March 3, 2011, a total of approximately \$6,219 in refund checks has been issued to about 15 thousand policyholders. The final total of refunds paid may be more or less than currently estimated; however, in management's opinion, any future expenses related to the settlement will not have a material adverse effect upon the overall financial position of the Company.

**ITEM 4. (REMOVED AND RESERVED)**

Table of Contents**PART II.****ITEM 5. MARKET FOR THE REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES**

As of March 9, 2011, there were 24 holders of record of the Company's common stock, par value \$0.01 per share, and we estimate another 8,000 held in "Street Name."

The Company's common stock (symbol: SAFT) is listed on the NASDAQ Global Select Market. The following table sets forth the high and low close prices per share for each full quarterly period within the Company's two most recent fiscal years.

<b>2010</b>	<b>High</b>	<b>Low</b>
<b>First quarter</b>	<b>\$ 39.20</b>	<b>\$ 33.83</b>
<b>Second quarter</b>	<b>\$ 38.57</b>	<b>\$ 35.02</b>
<b>Third quarter</b>	<b>\$ 43.82</b>	<b>\$ 37.28</b>
<b>Fourth quarter</b>	<b>\$ 49.36</b>	<b>\$ 42.20</b>

<b>2009</b>	<b>High</b>	<b>Low</b>
<b>First quarter</b>	<b>\$ 41.34</b>	<b>\$ 28.44</b>
<b>Second quarter</b>	<b>\$ 34.60</b>	<b>\$ 29.87</b>
<b>Third quarter</b>	<b>\$ 34.01</b>	<b>\$ 30.13</b>
<b>Fourth quarter</b>	<b>\$ 37.37</b>	<b>\$ 32.63</b>

The closing price of the Company's common stock on March 9, 2011 was \$47.35 per share.

During 2010, the Company declared and paid four quarterly cash dividends to shareholders, which totaled \$27,098. During 2009, the Company declared and paid four quarterly cash dividends to shareholders, which totaled \$24,840. On February 15, 2011, the Company's Board of Directors declared a quarterly cash dividend of \$0.50 per share to shareholders of record on March 1, 2011, payable on March 15, 2011. The Company plans to continue to declare and pay quarterly cash dividends in 2011, depending on the Company's financial position and the regularity of its cash flows.

The Company relies on dividends from its Insurance Subsidiaries for a portion of its cash requirements. The payment by the Company of any cash dividends to the holders of common stock therefore depends on the receipt of dividend payments from its Insurance Subsidiaries. The payment of dividends by the Insurance Subsidiaries is subject to limitations imposed by Massachusetts law, as discussed in Item 1 Business, Supervision and Regulation, *Insurance Regulation Concerning Dividends*, and also in Item 7 Management's Discussion and Analysis of Financial Condition and Results of Operations, Liquidity and Capital Resources.

The information called for by Item 201 (d) of Regulation S-K regarding securities authorized for issuance under equity compensation plans will be contained in the Company's Proxy Statement for its Annual Meeting of Shareholders, to be held on May 20, 2011 in Boston, MA, which the Company intends to file with the U.S. Securities and Exchange Commission within 120 days after December 31, 2010 (the Company's fiscal year end), and such information is incorporated herein by reference.

On August 3, 2007, the Board of Directors approved a share repurchase program of up to \$30,000 of the Company's outstanding common shares. On March 19, 2009, the Board of Directors increased this existing share repurchase program by authorizing repurchase of up to \$60,000 of the Company's outstanding common shares. On August 4, 2010, the Board of Directors again increased the existing share repurchase program by authorizing repurchase of up to \$90,000 of the Company's outstanding common shares. Under the program, the Company may repurchase shares of its common stock for cash in public or private transactions, in the open market or otherwise, at management's discretion. The timing of such repurchases and actual number of shares repurchased will depend on a variety of factors including price, market conditions and applicable regulatory and corporate requirements. The program does not require the Company to repurchase any specific number of shares and may be modified, suspended or terminated at any time without prior notice.

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During the year ended December 31, 2010, the Company purchased 162,907 of its common shares on the open market under the program at a cost of \$5,814 resulting in total shares purchased of 1,727,455 at a cost of \$55,526 as of December 31, 2010. During the year ended December 31, 2009, the Company purchased 1,332,535 of its common shares on the open market under the program at a cost of \$42,196, resulting in total shares purchased of 1,564,548 at a cost of \$49,712 as of December 31, 2009.

**COMMON STOCK PERFORMANCE GRAPH**

Set forth below is a line graph comparing the dollar change in the cumulative total shareholder return on the Company's Common Stock, for the period beginning on December 31, 2005 and ending on December 31, 2010, with the cumulative total return of the NASDAQ Stock Market Index and a peer group comprised of six selected property & casualty insurance companies over the same period. The peer group consists of Baldwin & Lyons, Inc., the Harleysville Group, Inc., Mercury General Corp., State Auto Financial Corp., Selective Insurance Group, Inc., and Donegal Group, Inc. The graph shows the change in value of an initial \$100 investment on December 31, 2010, assuming re-investment of all dividends.

**Comparative Cumulative Total Returns since December 31, 2005 Among  
Safety Insurance Group, Inc.,  
Property & Casualty Insurance Peer Group and the NASDAQ Stock Market Index**

The foregoing performance graph and data shall not be deemed "filed" as part of this Form 10-K for purposes of Section 18 of the Securities Exchange Act of 1934 or otherwise subject to the liabilities of that section and should not be deemed incorporated by reference into any other filing of the Company under the Securities Act of 1933 or the Securities Exchange Act of 1934, except to the extent the Company specifically incorporates it by reference into such filing.





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The following table sets forth our selected historical consolidated financial data as of and for each of the five years ended December 31, 2010, 2009, 2008, 2007, and 2006.

The selected historical consolidated financial data for the years ended December 31, 2010, 2009 and 2008 and as of December 31, 2010 and 2009 have been derived from the financial statements of Safety Insurance Group, Inc. included in this annual report which have been audited by PricewaterhouseCoopers LLP, an independent registered public accounting firm. The selected historical consolidated financial data for the years ended December 31, 2007 and 2006 and as of December 31, 2008, 2007 and 2006 have been derived from Safety Insurance Group, Inc.'s consolidated financial statements not included in this annual report, which have been audited by PricewaterhouseCoopers LLP.

We have prepared the selected historical consolidated financial data in conformity with U. S. generally accepted accounting principles.

The selected financial data presented below should be read in conjunction with Item 7 Management's Discussion and Analysis of Financial Condition and Results of Operations and the consolidated financial statements and the accompanying notes included in this Form 10-K in order to more fully understand the historical consolidated financial data.

	Years Ended December 31,				
	2010	2009	2008	2007	2006
Direct written premiums	\$ 604,957	\$ 559,747	\$ 573,509	\$ 619,848	\$ 629,511
Net written premiums	576,807	532,629	552,904	600,572	620,908
Net earned premiums	551,950	531,969	576,556	609,208	624,933
Net investment income	41,395	43,308	45,771	44,255	40,293
Net realized gains (losses) on investments	863	(167)	678	(6)	358
Finance and other service income	18,511	16,844	17,995	16,623	15,128
Total revenue	612,719	591,954	641,000	670,080	680,712
Loss and loss adjustment expenses	360,848	346,301	369,823	374,493	353,906
Underwriting, operating and related expenses	172,823	171,124	172,987	170,657	162,220
Interest expenses	88	135	81	83	86
Total expenses	533,759	517,560	542,891	545,233	516,212
Income before income taxes	78,960	74,394	98,109	124,847	164,500
Income tax expense	22,618	20,242	27,851	37,434	52,559
Net income	\$ 56,342	\$ 54,152	\$ 70,258	\$ 87,413	\$ 111,941

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Earnings per weighted average common share:

Basic(1)	\$	3.74	\$	3.49	\$	4.32	\$	5.40	\$	7.02
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Diluted(1)	\$	3.74	\$	3.48	\$	4.31	\$	5.38	\$	6.96
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Cash dividends paid per common share

\$	1.80	\$	1.60	\$	1.60	\$	1.30	\$	0.86
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Number of shares used in computing earnings per share:

Basic(1)	15,065,696	15,533,331	16,265,185	16,189,131	15,953,607
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Diluted(1)	15,084,295	15,552,063	16,308,394	16,251,067	16,079,841
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	Years Ended December 31,				
	2010	2009	2008	2007	2006
<b>Balance Sheet Data:</b>					
Total cash and investment securities	\$ 1,120,969	\$ 1,103,084	\$ 1,071,590	\$ 1,055,316	\$ 966,888
Total assets	1,439,452	1,427,837	1,437,817	1,446,992	1,355,748
Losses and loss adjustment expenses reserves	404,391	439,706	467,559	477,720	449,444
Total liabilities	785,976	807,402	834,446	876,992	859,400
Total shareholders' equity	653,476	620,435	603,371	570,000	496,348
<b>GAAP Ratios:</b>					
Loss ratio(2)	65.4%	65.1%	64.1%	61.5%	56.6%
Expense ratio(2)	31.3	32.2	30.0	28.0	26.0
Combined ratio(2)	96.7%	97.3%	94.1%	89.5%	82.6%

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(1) Earnings per share data and number of shares used in computing shares outstanding for years 2006-2008 have been restated to conform to ASC 260, *Participating Securities and the Two Class Method*. Please refer to Financial Statement footnote 2 for additional details.

(2) The loss ratio is the ratio of losses and loss adjustment expenses to net earned premiums. The expense ratio, when calculated on a GAAP basis is the ratio of underwriting expense to net earned premiums. The combined ratio is the sum of the loss ratio and the expense ratio. Please refer to *Insurance Ratios* under Item 7 Management's Discussion and Analysis of Financial Condition and Results of Operations for further discussion on our GAAP ratios.

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**ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS**

*The following discussion should be read in conjunction with our accompanying consolidated financial statements and notes thereto, which appear elsewhere in this document. In this discussion, all dollar amounts are presented in thousands, except share and per share data.*

*The following discussion contains forward-looking statements. We intend statements which are not historical in nature to be, and are hereby identified as "forward-looking statements" to be covered by the safe harbor provisions of the Private Securities Litigation Reform Act of 1995. In addition, the Company's senior management may make forward-looking statements orally to analysts, investors, the media and others. This safe harbor requires that we specify important factors that could cause actual results to differ materially from those contained in forward-looking statements made by or on behalf of us. We cannot promise that our expectations in such forward-looking statements will turn out to be correct. Our actual results could be materially different from and worse than our expectations. See "Forward-Looking Statements" below for specific important factors that could cause actual results to differ materially from those contained in forward-looking statements.*

**Executive Summary and Overview**

In this discussion, "Safety" refers to Safety Insurance Group, Inc. and "our Company," "we," "us" and "our" refer to Safety Insurance Group, Inc. and its consolidated subsidiaries. Our subsidiaries consist of Safety Insurance Company ("Safety Insurance"), Safety Indemnity Insurance Company ("Safety Indemnity"), Safety Property and Casualty Insurance Company ("Safety P&C"), Whiteshirts Asset Management Corporation ("WAMC"), and Whiteshirts Management Corporation, which is WAMC's holding company.

We are a leading provider of private passenger automobile insurance in Massachusetts. In addition to private passenger automobile insurance (which represented 68.7% of our direct written premiums in 2010), we offer a portfolio of other insurance products, including commercial automobile (10.4% of 2010 direct written premiums), homeowners (16.8% of 2010 direct written premiums), dwelling fire, umbrella and business owner policies (totaling 4.1% of 2010 direct written premiums). Operating exclusively in Massachusetts and New Hampshire through our insurance company subsidiaries, Safety Insurance, Safety Indemnity, and Safety P&C (together referred to as the "Insurance Subsidiaries"), we have established strong relationships with independent insurance agents, who numbered 783 in 939 locations throughout Massachusetts and New Hampshire during 2010. We have used these relationships and our extensive knowledge of the Massachusetts market to become the second largest private passenger automobile and the third largest commercial automobile insurance carrier in Massachusetts, capturing an approximate 11.4% and 10.7% share, respectively, of the Massachusetts private passenger and commercial automobile markets in 2010, according to the Commonwealth Automobile Reinsurers ("CAR") Cession Volume Analysis Report of March 3, 2011, based on automobile exposures. These statistics total, for each vehicle insured, the number of months during the year insurance for that vehicle is in effect, to arrive at an aggregate number of car-months for each insurer; this aggregate number, divided by 12, equals the insurer's number of car-years, a measure we refer to in this report as automobile exposures.

Our Insurance Subsidiaries began writing private passenger automobile and homeowners insurance business in New Hampshire during 2008 and personal umbrella business during 2009. During the years ended December 31, 2010 and 2009, the Company wrote \$2,774 and \$978 in direct written premiums, respectively, and approximately 3,300 and 1,250 policies, respectively, in New Hampshire.

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*Massachusetts Automobile Insurance Market*

We have been subject to extensive regulation in the private passenger automobile insurance industry in Massachusetts, which represented 68.7% of our direct written premiums in 2010. Owners of registered automobiles in Massachusetts are required to maintain minimum automobile insurance coverage. Prior to April 1, 2008, the Commissioner of Insurance (the "Commissioner") had fixed and established the maximum rates that could be charged for private passenger automobile insurance. Prior to April 1, 2008, as a servicing carrier of CAR, we were required to issue a policy to all qualified applicants. In addition, based on our market share prior to April 1, 2009, we had been assigned certain licensed producers by CAR that were unable to obtain a voluntary contract with another insurer. We call these agents Exclusive Representative Producers, or ERPs.

On July 16, 2007, the Commissioner issued two decisions that significantly changed how private passenger automobile insurance was regulated in Massachusetts. In the first decision, the Commissioner approved and set a time table for the implementation of new CAR rules pursuant to which the reinsurance program run by CAR was replaced with an assigned risk plan, the Massachusetts Automobile Insurance Plan ("MAIP"). Under these new rules, as of April 1, 2009 we are no longer assigned ERPs and instead, we were assigned individual policies by CAR. The MAIP began with business effective on or after April 1, 2008 for new business and those risks that had 10 or more Safe Driver Points. Beginning April 1, 2009, all business was eligible for MAIP except those risks that have no violations or accidents in the preceding three year period (so called "Clean in three" risks). The last policy effective date on which any risk could be ceded to CAR was March 31, 2009.

In the second decision referenced above, the Commissioner announced that she would not fix and establish the maximum premium rates that can be charged for private passenger automobile insurance policies issued or renewed after April 1, 2008. In a letter accompanying the decision, the Commissioner stated that in place of the "fixed and established" system, the Commissioner would institute a system that introduces competitive pricing to the Massachusetts private passenger automobile insurance market, which the Commissioner described as "managed competition" ("Managed Competition"). On October 5, 2007, the Commissioner issued a Competitive Rating Regulation; 211 CMR 79.00: Private Passenger Motor Vehicle Insurance Rates that describes the technical details of Managed Competition.

The Commissioner has also issued a number of bulletins addressing issues related to the implementation of Managed Competition (the "Rating Bulletins").

On May 27, 2010, the Massachusetts Office of the Attorney General (the "AG") issued proposed regulations that, if adopted, would apply to the sale, marketing, claims processing, rating, and underwriting of private passenger automobile insurance offered or provided in the Commonwealth of Massachusetts. The proposed regulations describe various acts by insurers and insurance producers which would be considered to be unfair trade practices, under Massachusetts' unfair trade practices act, M.G.L. c. 93A. The AG held two public hearings on the proposed regulations in June 2010, and may issue final regulations later in 2011. We are not able at this time to determine what effect these proposed regulations will have on our business over the long term.

CAR runs a reinsurance pool for commercial automobile policies and beginning January 1, 2006, CAR implemented a Limited Servicing Carrier Program ("LSC") for ceded commercial automobile policies. CAR approved Safety Insurance and five other servicing carriers through a Request for Proposal to process ceded commercial automobile business, which was spread equitably among the six servicing carriers. In 2010 CAR reduced the number of servicing carriers to four, and CAR has approved Safety and three other servicing carriers effective July 1, 2011 to continue the program. Subject to the Commissioner's review, CAR sets the premium rates for commercial automobile policies reinsured through CAR and this reinsurance pool can generate an underwriting result that is a profit or deficit based upon CAR's rate level. This underwriting result is allocated among every Massachusetts

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commercial automobile insurance company, including us, based on a company's commercial automobile voluntary market share.

CAR also runs a reinsurance pool for Taxi, Limousine and Car Service risks (the "Taxi/Limo Program"). On April 25, 2007, Safety submitted through a Request for Proposal a bid to process a portion of the Taxi/Limo Program. CAR approved Safety as one of the two servicing carriers for this program beginning January 1, 2008, and CAR has again approved Safety beginning January 1, 2011 as one of the two servicing carriers.

Under Managed Competition, we decreased our rates an average 6.7% in 2008. During 2009, we increased our rates an average of 2.6% in a series of rate filings during the year. We began using three rating tiers effective April 1, 2009. We filed and were approved for a 0.3% rate decrease effective June 1, 2009 and a 2.9% rate increase effective October 1, 2009. We filed and were approved for a rate increase of 0.4% and began using four rating tiers effective January 1, 2010. A Companion Policy Client Tier, which is policyholders who have an other than private passenger automobile policy with us, receives a rate decrease of 2.5% from our filed base rates. A Loyal Automobile Client Tier, which is policyholders who have been insured with Safety two or more years, receives our filed base rates. A New Insurance Client Tier, which is policyholders with twelve or more months of continuous coverage or who qualify for a multi-car discount, receives a rate increase of 2.5% from our filed base rates. A New Policyholder Tier, which is policyholders who do not qualify for the other three tiers, receives MAIP rates. We filed and were approved for a 1.9% increase in our rates effective April 19, 2010 and we also filed and were approved for a 0.5% decrease in our rates effective June 15, 2010. Our rates include a 13.0% commission rate for agents. Our direct written premiums increased by 8.1% in 2010 primarily as a result of increased exposures and average written premium per exposure in our private passenger and homeowner lines of business.

### *Statutory Accounting Principles*

Our results are reported in accordance with GAAP, which differ from amounts reported in accordance with statutory accounting principles ("SAP") as prescribed by insurance regulatory authorities, which in general reflect a liquidating, rather than going concern concept of accounting. Specifically, under GAAP:

Policy acquisition costs such as commissions, premium taxes and other variable costs incurred in connection with writing new and renewal business are capitalized and amortized on a pro rata basis over the period in which the related premiums are earned, rather than expensed as incurred, as required by SAP.

Certain assets are included in the consolidated balance sheets whereas, under SAP, such assets are designated as "non admitted assets," and charged directly against statutory surplus. These assets consist primarily of premium receivables that are outstanding over ninety days, federal deferred tax assets in excess of statutory limitations, furniture, equipment, leasehold improvements and prepaid expenses.

Amounts related to ceded reinsurance are shown gross of ceded unearned premiums and reinsurance recoverables, rather than netted against unearned premium reserves and loss and loss adjustment expense reserves, respectively, as required by SAP.

Fixed maturities securities, which are classified as available-for-sale, are reported at current fair values, rather than at amortized cost, or the lower of amortized cost or market, depending on the specific type of security, as required by SAP.

The differing treatment of income and expense items results in a corresponding difference in federal income tax expense. Changes in deferred income taxes are reflected as an item of income tax benefit or expense, rather than recorded directly to surplus as regards policyholders,

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as required by SAP. Admittance testing may result in a charge to unassigned surplus for non-admitted portions of deferred tax assets. Under GAAP reporting, a valuation allowance may be recorded against the deferred tax asset and reflected as an expense.

### *Insurance Ratios*

The property and casualty insurance industry uses the combined ratio as a measure of underwriting profitability. The combined ratio is the sum of the loss ratio (losses and loss adjustment expenses incurred as a percent of net earned premiums) plus the expense ratio (underwriting expenses as a percent of net earned premiums, calculated on a GAAP basis). The combined ratio reflects only underwriting results and does not include income from investments or finance and other service income. Underwriting profitability is subject to significant fluctuations due to competition, catastrophic events, weather, economic and social conditions, and other factors.

Our GAAP insurance ratios are outlined in the following table:

	Years Ended December 31,		
	2010	2009	2008
<b>GAAP Ratios:</b>			
Loss Ratio	<b>65.4%</b>	65.1%	64.1%
Expense Ratio	<b>31.3</b>	32.2	30.0
Combined Ratio	<b>96.7%</b>	97.3%	94.1%

### *Stock-Based Compensation*

On June 25, 2002, the Board of Directors of the Company (the "Board") adopted the 2002 Management Omnibus Incentive Plan (the "Incentive Plan"). The Incentive Plan provides for a variety of awards, including nonqualified stock options ("NQSOs"), stock appreciation rights and restricted stock ("RS") awards.

On March 10, 2006, the Board approved amendments to the Incentive Plan, subject to shareholder approval, to (i) increase the number of shares of common stock available for issuance by 1,250,000 shares, (ii) remove obsolete provisions, and (iii) make other non-material changes. A total of 1,250,000 shares of common stock had previously been authorized for issuance under the Incentive Plan. The Incentive Plan, as amended, was approved by the shareholders at the 2006 Annual Meeting of Shareholders which was held on May 19, 2006. Under the Incentive Plan, as amended, the maximum number of shares of common stock with respect to which awards may be granted is 2,500,000. As of December 31, 2010, there were 813,484 shares available for future grant. The Board and the Compensation Committee intend to issue more awards under the Incentive Plan in the future. Grants outstanding under the Incentive Plan as of December 31, 2010, were comprised of 301,501 restricted shares and 151,003 nonqualified stock options.

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Grants made under the Incentive Plan are as follows:

Type of Equity Awarded	Effective Date	Number of Awards Granted	Exercise Price(1) or Fair Value(2) per Share	Vesting Terms	Expiration Date
NQSOs	November 27, 2002	379,000	\$ 12.00(1)	5 years, 20% annually	November 27, 2012
NQSOs	February 20, 2003	99,000	\$ 13.30(1)	5 years, 20% annually	February 20, 2013
NQSOs	March 31, 2003	292,000	\$ 13.03(1)	3 years, 30%-30%-40%	March 31, 2013
NQSOs	August 21, 2003	10,000	\$ 15.89(1)	5 years, 20% annually	August 21, 2013
NQSOs	March 25, 2004	111,000	\$ 18.50(1)	5 years, 20% annually	March 25, 2014
RS	March 25, 2004	70,271	\$ 18.50(2)	3 years, 30%-30%-40%	N/A
NQSOs	August 30, 2004	10,000	\$ 21.40(1)	5 years, 20% annually	August 30, 2014
NQSOs	March 16, 2005	78,000	\$ 35.23(1)	5 years, 20% annually	March 16, 2015
RS	March 16, 2005	56,770	\$ 35.23(2)	3 years, 30%-30%-40%	N/A
RS	March 16, 2005	4,000	\$ 35.23(2)	No vesting period(3)	N/A
NQSOs	March 10, 2006	126,225	\$ 42.85(1)	5 years, 20% annually	March 10, 2016
RS	March 10, 2006	58,342	\$ 42.85(2)	3 years, 30%-30%-40%	N/A
RS	March 10, 2006	4,000	\$ 42.85(2)	No vesting period(3)	N/A
RS	February 26, 2007	65,760	\$ 45.62(2)	3 years, 30%-30%-40%	N/A
RS	February 26, 2007	4,000	\$ 45.62(2)	No vesting period(3)	N/A
RS	March 22, 2007	49,971	\$ 38.78(2)	5 years, 20% annually	N/A
RS	March 10, 2008	76,816	\$ 35.80(2)	3 years, 30%-30%-40%	N/A
RS	March 10, 2008	4,000	\$ 35.80(2)	No vesting period(3)	N/A
RS	March 20, 2008	45,779	\$ 34.37(2)	5 years, 20% annually	N/A
RS	March 9, 2009	95,953	\$ 28.66(2)	3 years, 30%-30%-40%	N/A
RS	March 9, 2009	4,000	\$ 28.66(2)	No vesting period(3)	N/A
RS	March 19, 2009	38,046	\$ 33.24(2)	5 years, 20% annually	N/A
RS	March 9, 2010	77,360	\$ 38.78(2)	3 years, 30%-30%-40%	N/A
RS	March 9, 2010	4,000	\$ 38.78(2)	No vesting period(3)	N/A
RS	March 23, 2010	25,590	\$ 38.09(2)	5 years, 20% annually	N/A

- (1) The exercise price of the options grant effective on November 27, 2002, is equal to the IPO price of our stock on that same day. The exercise price of the remaining option grants is equal to the closing price of our common stock on the grant date.
- (2) The fair value per share of the restricted stock grant is equal to the closing price of the Company's common stock on the grant date.
- (3) The shares cannot be sold, assigned, pledged, or otherwise transferred, encumbered or disposed of until the recipient is no longer a member of our Board of Directors.

## Reinsurance

We reinsure with other insurance companies a portion of our potential liability under the policies we have underwritten, thereby protecting us against an unexpectedly large loss or a catastrophic occurrence that could produce large losses, primarily in our homeowners line of business. We use various software products to measure our exposure to catastrophe losses and the probable maximum loss to us for catastrophe losses such as hurricanes. The models include estimates for our share of the catastrophe losses generated in the residual market for property insurance by the Massachusetts Property Insurance Underwriting Association ("FAIR Plan"). In the aftermath of Hurricane Katrina in 2005, the reinsurance market has seen from the various software modelers, increases in the estimate of damage from hurricanes in the southern and northeast portions of the United States due to revised estimations of increased hurricane activity and increases in the estimation of demand surge



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in the periods following a significant event. We continue to adjust our reinsurance programs as a result of the changes to the models and the number of homes we write. As of January 1, 2011, our catastrophe

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reinsurance provides gross per occurrence reinsurance coverage up to \$535,000. As a result of the changes to the models, and our revised reinsurance program, our catastrophe reinsurance in 2011 protects us in the event of a "140-year storm" (that is, a storm of a severity expected to occur once in a 140-year period). Swiss Re, our primary reinsurer, maintains an A.M. Best rating of "A" (Excellent). Most of our other reinsurers have an A.M. Best rating of "A" (Excellent) however in no case is a reinsurer rated below "A-" (Excellent).

We are a participant in CAR, a state-established body that runs the residual market reinsurance programs for both private passenger and commercial automobile insurance in Massachusetts under which premiums, expenses, losses and loss adjustment expenses on ceded business are shared by all insurers writing automobile insurance in Massachusetts. We also participate in the FAIR Plan in which premiums, expenses, losses and loss adjustment expenses on homeowners business that cannot be placed in the voluntary market are shared by all insurers writing homeowners insurance in Massachusetts. The FAIR Plan has grown dramatically over the past few years as insurance carriers have reduced their exposure to coastal property. The FAIR Plan's exposure to catastrophe losses increased and as a result, the FAIR Plan decided to buy reinsurance to reduce their exposure to catastrophe losses. On July 1, 2010, the FAIR Plan purchased \$1,000,000 of catastrophe reinsurance for property losses in excess of \$200,000. At December 31, 2010, we had no material amounts recoverable from any reinsurer, excluding \$44,897 recoverable from CAR.

On March 10, 2005, our Board of Directors adopted a resolution that prohibits Safety from purchasing finite reinsurance (reinsurance that transfers only a finite or limited amount of risk to the reinsurer) without approval by the Board. To date, the Company has never purchased a finite reinsurance contract.

*Effects of Inflation*

We do not believe that inflation has had a material effect on our consolidated results of operations, except insofar as inflation may affect interest rates.

**Critical Accounting Policies and Estimates**

*Loss and Loss Adjustment Expense Reserves.*

Significant periods of time can elapse between the occurrence of an insured loss, the reporting to us of that loss and our final payment of that loss. To recognize liabilities for unpaid losses, we establish reserves as balance sheet liabilities. Our reserves represent estimates of amounts needed to pay reported and unreported losses and the expenses of investigating and paying those losses, or loss adjustment expenses. Every quarter, we review our previously established reserves and adjust them, if necessary.

When a claim is reported, claims personnel establish a "case reserve" for the estimated amount of the ultimate payment. The amount of the reserve is primarily based upon an evaluation of the type of claim involved, the circumstances surrounding each claim and the policy provisions relating to the loss. The estimate reflects the informed judgment of such personnel based on general insurance reserving practices and on the experience and knowledge of the claims person. During the loss adjustment period, these estimates are revised as deemed necessary by our claims department based on subsequent developments and periodic reviews of the cases.

In accordance with industry practice, we also maintain reserves for estimated losses incurred but not yet reported ("IBNR"). IBNR reserves are determined in accordance with commonly accepted actuarial reserving techniques on the basis of our historical information and experience. We review and make adjustments to incurred but not yet reported reserves quarterly.

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When reviewing reserves, we analyze historical data and estimate the impact of various loss development factors, such as our historical loss experience and that of the industry, trends in claims frequency and severity, our mix of business, our claims processing procedures, legislative enactments, judicial decisions, legal developments in imposition of damages, and changes and trends in general economic conditions, including the effects of inflation. A change in any of these factors from the assumption implicit in our estimate can cause our actual loss experience to be better or worse than our reserves, and the difference can be material. There is no precise method, however, for evaluating the impact of any specific factor on the adequacy of reserves, because the eventual development of reserves is affected by many factors.

Management determines our loss and LAE reserves estimate based upon the analysis of our actuaries. A reasonable estimate is derived by selecting a point estimate within a range of indications as calculated by our actuaries using generally accepted actuarial techniques. The key assumption in most actuarial analysis is that past patterns of frequency and severity will repeat in the future, unless a significant change in the factors described above takes place. Our key factors and resulting assumptions are the ultimate frequency and severity of claims, based upon the most recent ten years of claims reported to the Company, and the data CAR reports to us to calculate our share of the residual market, as of the date of the applicable balance sheet. For each accident year and each coverage within a line of business our actuaries calculate the ultimate losses incurred. Our total reserves are the difference between the ultimate losses incurred and the cumulative loss and loss adjustment payments made to date. Our IBNR reserves are calculated as the difference between our total reserves and the outstanding case reserves at the end of the accounting period. To determine ultimate losses, our actuaries calculate a range of indications and select a point estimation using such actuarial techniques as:

*Paid Loss Indications:* This method projects ultimate loss estimates based upon extrapolations of historic paid loss trends. This method tends to be used on short tail lines such as automobile physical damage.

*Incurred Loss Indications:* This method projects ultimate loss estimates based upon extrapolations of historic incurred loss trends. This method tends to be used on long tail lines of business such as automobile liability and homeowner's liability.

*Bornhuetter-Ferguson Indications:* This method projects ultimate loss estimates based upon extrapolations of an expected amount of IBNR, which is added to current incurred losses or paid losses. This method tends to be used on small, immature, or volatile lines of business, such as our BOP and umbrella lines of business.

*Bodily Injury Code Indications:* This method projects ultimate loss estimates for our private passenger and commercial automobile bodily injury coverage based upon extrapolations of the historic number of accidents and the historic number of bodily injury claims per accident. Projected ultimate bodily injury claims are then segregated into expected claims by type of injury (e.g. soft tissue injury vs. hard tissue injury) based on past experience. An ultimate severity, or average paid loss amounts, is estimated based upon extrapolating historic trends. Projected ultimate loss estimates using this method are the aggregate of estimated losses by injury type.

Such techniques assume that past experience, adjusted for the effects of current developments and anticipated trends, is an appropriate basis for predicting our ultimate losses, total reserves and resulting IBNR reserves. It is possible that the final outcome may fall above or below these amounts as a result of a number of factors, including immature data, sparse data, or significant growth in a line of business. Using these methodologies, our actuaries established a range of reasonably possible estimations for net reserves of approximately \$311,570 to \$359,802 as of December 31, 2010 compared to a range of \$332,854 to \$378,692 for 2009. In general, the low and high values of the ranges represent reasonable minimum and maximum values of the indications based on the techniques described above. Our

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selected point estimate of net loss and LAE reserves based upon the analysis of our actuaries was \$351,244 as of December 31, 2010 compared to \$374,832 for December 31, 2009. We have recorded reserves closer to the high in the ranges of our projections.

The following tables present the point estimation of the recorded reserves and the range of estimations by line of business for net loss and LAE reserves as of December 31, 2010 and December 31, 2009.

Line of Business	As of December 31, 2010		
	Low	Recorded	High
Private passenger automobile	\$ 213,803	\$ 240,129	\$ 244,749
Commercial automobile	40,413	45,772	46,483
Homeowners	38,814	44,741	47,181
All other	18,540	20,602	21,389
<b>Total</b>	<b>\$ 311,570</b>	<b>\$ 351,244</b>	<b>\$ 359,802</b>

Line of Business	As of December 31, 2009		
	Low	Recorded	High
Private passenger automobile	\$ 228,414	\$ 258,552	\$ 258,843
Commercial automobile	48,556	54,785	55,272
Homeowners	39,967	42,750	44,223
All other	15,917	18,745	20,354
<b>Total</b>	<b>\$ 332,854</b>	<b>\$ 374,832</b>	<b>\$ 378,692</b>

The following tables present our total net reserves and the corresponding case reserves and IBNR reserves for each line of business as of December 31, 2010 and December 31, 2009.

Line of Business	As of December 31, 2010		
	Case	IBNR	Total
Private passenger automobile	\$ 230,330	\$ 50	\$ 230,380
CAR assumed private passenger auto	7,274	2,475	9,749
Commercial automobile	30,424	4,143	34,567
CAR assumed commercial automobile	7,325	3,880	11,205
Homeowners	25,117	8,467	33,584
FAIR Plan assumed homeowners	5,567	5,590	11,157
All other	11,452	9,150	20,602

Total net reserves for losses and LAE                      \$ 317,489    \$ 33,755    \$ 351,244

Line of Business	As of December 31, 2009		
	Case	IBNR	Total
Private passenger automobile	\$ 220,907	\$ 16,812	\$ 237,719
CAR assumed private passenger auto	15,402	5,431	20,833
Commercial automobile	32,287	7,867	40,154
CAR assumed commercial automobile	8,063	6,568	14,631
Homeowners	16,268	9,262	25,530
FAIR Plan assumed homeowners	5,218	12,002	17,220
All other	7,967	10,778	18,745

Total net reserves for losses and LAE                      \$ 306,112    \$ 68,720    \$ 374,832



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Our IBNR reserves consist of our estimate of the total loss reserves required less our case reserves. The IBNR reserves for CAR assumed private passenger and commercial automobile business are 25.4% and 34.6%, respectively, of our total reserves for CAR assumed private passenger and commercial automobile business as of December 31, 2010 due to the reporting delays in the information we receive from CAR, as described further in the section on *CAR Loss and Loss Adjustment Expense Reserves*. Our IBNR reserves for FAIR Plan assumed homeowners are 51.3% of our total reserves for FAIR Plan assumed homeowners at December 31, 2010 due to similar reporting delays in the information we receive from FAIR Plan.

The following tables present information by line of business for our total net reserves and the corresponding retained (i.e. direct less ceded) reserves and assumed reserves as of December 31, 2010 and December 31, 2009.

Line of Business	As of December 31, 2010		
	Retained	Assumed	Net
Private passenger automobile	\$ 230,380		
CAR assumed private passenger automobile		\$ 9,749	
Net private passenger automobile			\$ 240,129
Commercial automobile	34,567		
CAR assumed commercial automobile		11,205	
Net commercial automobile			45,772
Homeowners	33,584		
FAIR Plan assumed homeowners		11,157	
Net homeowners			44,741
All other	20,602		20,602
Total net reserves for losses and LAE	\$ 319,133	\$ 32,111	\$ 351,244

Line of Business	As of December 31, 2009		
	Retained	Assumed	Net
Private passenger automobile	\$ 237,719		
CAR assumed private passenger automobile		\$ 20,833	
Net private passenger automobile			\$ 258,552
Commercial automobile	40,154		
CAR assumed commercial automobile		14,631	
Net commercial automobile			54,785
Homeowners	25,530		
FAIR Plan assumed homeowners		17,220	
Net homeowners			42,750
All other	18,745		18,745
Total net reserves for losses and LAE	\$ 322,148	\$ 52,684	\$ 374,832

### *CAR Loss and Loss Adjustment Expense Reserves*

We are a participant in CAR and assume a portion of losses and LAE on business ceded by the industry participants to CAR. We estimate reserves for assumed losses and LAE that have not yet been reported to us by CAR. Our estimations are based upon the same factors we use for our own reserves, plus additional factors due to the nature of and the information we receive from CAR. The portion of reserves based upon CAR estimates for private passenger automobile line of business has declined substantially over time as a result of the institution of the MAIP and phase-out of the private passenger automobile CAR reinsurance pool on April 1, 2009, as described elsewhere in this report.

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The CAR deficit, which consists of premium ceded to CAR less CAR losses and LAE, is allocated among every automobile insurance company writing business in Massachusetts based on a complex formula (the "Participation Ratio") that takes into consideration a company's voluntary market share, the amount of business it cedes to CAR and credits the company earns under a system CAR has designed to encourage carriers to voluntarily write business in selected under-priced classes and territories.

We receive a Settlement of Balances report from CAR that reports our share of CAR premium, losses and LAE on a lagged basis, seventy-five days after the end of every quarter. CAR-published financial data is always at least one quarter behind the financial data we report. For example, when we reported our financial results for the year ended December 31, 2009, we had nine months of reported 2009 CAR financial data, and we had to estimate and record as IBNR reserves what CAR would report to us for the last three months of the year.

We receive our final calendar year Participation Ratio report from CAR eight months after the end of that year, and thus we have to estimate for six quarters our share of the CAR deficit. For example, for the year ended December 31, 2009 we had to estimate our 2009 policy year CAR Participation Ratio beginning with the first quarter of 2009 through the second quarter of 2010.

Because of the lag in CAR estimates, and in order to try to validate to the extent possible the information CAR does provide, we must try to estimate the effects of the actions of our competitors in order to establish our Participation Ratio. Before final Participation Ratios are available, we estimate the size of CAR and the resulting deficit based on historical analysis of CAR results and estimations of our competitors' cession strategies. Even after our final Participation Ratio is available from CAR, we must continue to estimate the size of CAR and the resulting deficit based upon data published by CAR and our own continuing analysis. As a result, changes in our reserves for CAR may continue to occur until all claims are finally settled. The Loss Reserving Committee at CAR meets 70 days after the end of each quarter to estimate the CAR deficit for all active policy years and publishes estimations, which we use to estimate our share of the deficit. The estimation that CAR calculates is based on data it collects from 19 servicing carriers which settle, reserve and report claims using a variety of methods. Any delays or errors in the collection of this data could have a significant impact on the accuracy of CAR's estimations.

Although we rely to a significant extent in setting our reserves on the information CAR provides, we are cautious in our use of that information, both because of the delays described above and because the CAR estimates incorporate data CAR receives from all other CAR servicing carriers in Massachusetts. We do not have direct access to that data or firsthand knowledge of how those carriers are currently conducting their operations. As a result, we are cautious in recording CAR reserves for the calendar years for which we have to estimate our Participation Ratio and these reserves are subject to significant judgments and estimates.

*Sensitivity Analysis*

Establishment of appropriate reserves is an inherently uncertain process. There can be no certainty that currently established reserves based on our key assumptions regarding frequency and severity in our lines of business, or our assumptions regarding our share of the CAR loss will prove adequate in light of subsequent actual experience. To the extent that reserves are inadequate and are strengthened, the amount of such increase is treated as a charge to earnings in the period that the deficiency is recognized. To the extent that reserves are redundant and are released, the amount of the release is a credit to earnings in the period the redundancy is recognized. For the year ended December 31, 2010, a 1 percentage-point change in the loss and LAE ratio would result in a change in reserves of \$5,519. Each 1 percentage-point change in the loss and loss expense ratio would have had a \$3,588 effect on net income, or \$0.24 per diluted share.

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Our assumptions consider that past experience, adjusted for the effects of current developments and anticipated trends, are an appropriate basis for establishing our reserves. Our individual key assumptions could each have a reasonable possible range of plus or minus 5 percentage-points for each estimation, although there is no guarantee that our assumptions will not have more than a 5 percentage point variation. The following sensitivity tables present information for each of our primary lines of business on the effect each 1 percentage-point change in each of our key assumptions on unpaid frequency and severity could have on our retained (i.e., direct minus ceded) loss and LAE reserves and net income for the year ended December 31, 2010. In evaluating the information in the table, it should be noted that a 1 percentage-point change in a single assumption would change estimated reserves by 1 percentage-point. A 1 percentage-point change in both our key assumptions would change estimated reserves within a range of plus or minus 2 percentage-points.

	-1 Percent Change in Frequency	No Change in Frequency	+1 Percent Change in Frequency
<b>Private passenger automobile direct minus ceded loss and LAE reserves</b>			
-1 Percent Change in Severity			
Estimated decrease in reserves	\$ (4,608)	\$ (2,304)	\$
Estimated increase in net income	2,995	1,498	
No Change in Severity			
Estimated (decrease) increase in reserves	(2,304)		2,304
Estimated increase (decrease) in net income	1,498		(1,498)
+1 Percent Change in Severity			
Estimated increase in reserves		2,304	4,608
Estimated decrease in net income		(1,498)	(2,995)
<b>Commercial automobile direct minus ceded loss and LAE reserves</b>			
-1 Percent Change in Severity			
Estimated decrease in reserves	(691)	(346)	
Estimated increase in net income	449	225	
No Change in Severity			
Estimated (decrease) increase in reserves	(346)		346
Estimated increase (decrease) in net income	225		(225)
+1 Percent Change in Severity			
Estimated increase in reserves		346	691
Estimated decrease in net income		(225)	(449)
<b>Homeowners direct minus ceded loss and LAE reserves</b>			
-1 Percent Change in Severity			
Estimated decrease in reserves	(672)	(336)	
Estimated increase in net income	437	218	
No Change in Severity			
Estimated (decrease) increase in reserves	(336)		336
Estimated increase (decrease) in net income	218		(218)
+1 Percent Change in Severity			
Estimated increase in reserves		336	672
Estimated decrease in net income		(218)	(437)
<b>All other direct minus ceded loss and LAE reserves</b>			
-1 Percent Change in Severity			
Estimated decrease in reserves	(412)	(206)	
Estimated increase in net income	268	134	
No Change in Severity			
Estimated (decrease) increase in reserves	(206)		206
Estimated increase (decrease) in net income	134		(134)
+1 Percent Change in Severity			
Estimated increase in reserves		206	412
Estimated decrease in net income		(134)	(268)



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Our estimated share of CAR loss and LAE reserves is based on assumptions about our Participation Ratio, the size of CAR, and the resulting deficit (similar assumptions apply with respect to the FAIR Plan). Our assumptions consider that past experience, adjusted for the effects of current developments and anticipated trends, is an appropriate basis for establishing our CAR reserves. Each of our assumptions could have a reasonably possible range of plus or minus 5 percentage-points for each estimation.

The following sensitivity table presents information of the effect each 1 percentage-point change in our assumptions on our share of reserves for CAR and other residual markets could have on our assumed loss and LAE reserves and net income for the year ended December 31, 2010. In evaluating the information in the table, it should be noted that a 1 percentage-point change in our assumptions would change estimated reserves by 1 percentage-point.

	-1 Percent Change in Estimation	+1 Percent Change in Estimation
<b>CAR assumed private passenger automobile</b>		
Estimated (decrease) increase in reserves	\$ (97)	\$ 97
Estimated increase (decrease) in net income	63	(63)
<b>CAR assumed commercial automobile</b>		
Estimated (decrease) increase in reserves	(112)	112
Estimated increase (decrease) in net income	73	(73)
<b>FAIR Plan assumed homeowners</b>		
Estimated (decrease) increase in reserves	(112)	112
Estimated increase (decrease) in net income	73	(73)

### Reserve Development Summary

The changes we have recorded in our reserves in the past illustrate the uncertainty of estimating reserves. Our prior year reserves decreased by \$48,157, \$44,065 and \$35,938 for the years ended December 31, 2010, 2009 and 2008, respectively.

The following table presents a comparison of prior year development of our net reserves for losses and LAE for the years ended December 31, 2010, 2009 and 2008. Each accident year represents all claims for an annual accounting period in which loss events occurred, regardless of when the losses are actually reported, booked or paid. Our financial statements reflect the aggregate results of the current and all prior accident years.

Accident Year	Years Ended December 31,		
	2010	2009	2008
2000 & prior	\$ (600)	\$ (620)	\$ (1,192)
2001	(496)	(1,004)	(958)
2002	(1,031)	(1,431)	(1,973)
2003	(1,669)	(1,385)	(2,507)
2004	(2,147)	(3,827)	(6,619)
2005	(4,488)	(5,999)	(8,258)
2006	(7,996)	(9,829)	(6,714)
2007	(9,662)	(8,079)	(7,717)
2008	(10,992)	(11,891)	
2009	(9,076)		
All prior years	\$ (48,157)	\$ (44,065)	\$ (35,938)

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The decreases in prior years reserves during the 2010, 2009 and 2008 periods resulted from re-estimations of prior year ultimate loss and LAE liabilities. The 2010 decrease is primarily composed of reductions of \$34,248 in our retained automobile reserves, \$7,269 in our retained homeowners and all other reserves and \$5,572 in CAR assumed reserves. The 2009 decrease is primarily composed of reductions of \$24,979 in our retained automobile reserves and \$11,551 in CAR assumed reserves and \$6,103 in our retained homeowners and all other reserves. The 2008 decrease is primarily composed of reductions of \$21,752 in our retained automobile reserves and \$8,905 in CAR assumed reserves.

The following table presents information by line of business for prior year development of our net reserves for losses and LAE for the year ended December 31, 2010.

Accident Year	Private Passenger Automobile	Commercial Automobile	Homeowners	All Other	Total
2000 & prior	\$ (532)	\$ (52)	\$ 13	\$ (29)	\$ (600)
2001	(338)	(26)	(28)	(104)	(496)
2002	(641)	(124)	(56)	(210)	(1,031)
2003	(1,008)	(285)	(27)	(349)	(1,669)
2004	(1,091)	(633)	(51)	(372)	(2,147)
2005	(3,095)	(634)	(389)	(370)	(4,488)
2006	(4,600)	(2,079)	(870)	(447)	(7,996)
2007	(6,426)	(1,267)	(1,417)	(552)	(9,662)
2008	(7,660)	(1,402)	(869)	(1,061)	(10,992)
2009	(6,553)	(1,374)	(831)	(318)	(9,076)
All prior years	\$ (31,944)	\$ (7,876)	\$ (4,525)	\$ (3,812)	\$ (48,157)

To further clarify the effects of changes in our reserve estimates for CAR and other residual markets, the next two tables break out the information in the table above by source of the business (i.e., non-residual market vs. residual market).

The following table presents information by line of business for prior year development of retained reserves for losses and LAE for the year ended December 31, 2010; that is, all our reserves except for business ceded or assumed from CAR and other residual markets.