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Private companies see costs rise for directors and officers liability insurance

Despite plentiful capacity, insurers wary of increased exposures

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Employment practices liability claims and mergers and acquisitions are leading to higher rates for mid-market private company directors and officers liability insurance.

Private company D&O coverage, also known as management liability insurance, usually has four components: D&O, EPL, fiduciary and crime coverage.

Observers say one important difference between private and public D&O policies is there is entity coverage available for the former, and most include duty-to-defend provisions.

Experts stress that the value of this coverage is that it protects directors' personal assets (see related story).

“This has been an exciting sector since the end of 2011, and what has been happening now is, most middle-market accounts are getting 5% to 10% increases that may be closer to 5% for the most part,” said Phil Norton, Chicago-based president of the professional liability division at Arthur J. Gallagher & Co.

“There's still a lot of capacity in the marketplace, but the carriers in the market are becoming more selective in where they're willing to put that capacity,” said Debbie Schaffel, Chicago-based managing director for Aon P.L.C.'s financial services group.

Geography is a factor, said Damien Magnuson, senior vice president at Los Angeles-based Executive Perils Inc.

“I'd say in the last year, at least half of the accounts I've worked on have seen an increase; and in California, it's probably 90% of the accounts” because claims are brought more frequently in California and defense costs are “quite a bit higher,” Mr. Magnuson said.

“Costs continue to trend upward and frequency remains a constant,” said Beth Goldberg, New York-based senior vice president and head of middle market at Zurich North America. Overall, the marketplace is managing retentions, attachment points, and terms and conditions, she said.

Ms. Schaffel said insurers also are cutting the limits they offer and requiring more information before underwriting. In addition, while insurers previously would have tended to respond to a threat to move the business elsewhere by backing down on their rate hike demands, now they are much more inclined to say, “If you can move it, move it,” she said.

De'Andre Salter, founder and CEO of Warren, N.J.-based Professional Risk Solutions L.L.C., said while placing $10 million primary coverage on a privately held D&O account would have been “fairly easy” during the softer market, today “the underwriters are managing their limits down to $5 million and less on any individual account, and underwriters are asking more questions” before providing $10 million in capacity.

Observers say rate hikes have been much more significant among private companies than among public firms.

The market was “probably already appropriately priced” for public company claims, while “the private management liability has probably been underpriced for quite some time,” said Bryan Costello, CEO of San Rafael, Calif.-based Costello & Sons Insurance Brokers Inc.

“Historically, the employment practices liability portion of the policy was thought to be the primary driver of claims frequency,” said Alton Moore, San Francisco-based assistant vice president of specialty casualty underwriting at Liberty International Underwriters, a unit of Liberty Mutual Group Inc.

But because of conditions stemming from the 2008 financial crisis, there has been an unanticipated increase in D&O claims, Mr. Moore said. “Many private companies have either gone into bankruptcy proceedings, or full-out liquidation” because of the weak economy, he said.

“Many carriers, including ourselves, are really looking at the financial condition of the organization, and wanting to make sure that they can get through the next 12 to 18 months, especially when you're dealing with more startup organizations,” said Lynette Lyngaas, senior vice president at Rolling Meadows, Ill.-based Monitor Liability Managers L.L.C., an underwriting management unit of W.R. Berkley Corp.

Increased mergers and acquisitions also factor into the rate increases.

M&A-related litigation activity has “been exploding,” with well over 95% of mergers leading to litigation, said Michael B. Chester, a principal with law firm Boundas, Skarzynski, Walsh & Black L.L.C. in New York.

Spiro K. Bantis, a partner with London Fischer L.L.P. in New York, said a frequent source of such claims is minority shareholders against stockholders who have a controlling interest.

Another factor, Mr. Chester said, is “there has been a tremendous amount of regulatory activity that's been going on,” which is affecting even private companies. With increased regulatory activity “comes the potential for more claims against companies.”

Mr. Bantis also pointed to fiduciary coverage's inclusion within mid-market management liability policies.

“You don't have the controls necessary you might have with bigger companies, where you can afford more manpower and there are people watching other people,” Mr. Bantis said. People at mid-market companies may be “left to their own devices and, unfortunately, some of those people turn out to be dishonest.”

Private company D&O also is more challenging to underwrite than public company D&O because there is relatively little public information available, said Michael Richmond, sales executive at the Chicago-based brokerage The Horton Group.
