Top 10 myths of D&O liability insurance

Squelching frequent misconceptions of this valuable protection.

By Peter R. Taffae

In today's soft directors and officers market, the importance of a long term approach can often be lost in the process of securing coverage. However, history has proven in the past 15-plus years that the D&O market has always been and always will be cyclical. We saw it in 1985, again in 1998 and in 2003 with the valleys not as deep as the peaks were high.

Today, we are seeing substantial decreases in premiums and modest coverage enhancements. Less than three years ago, we saw coverage substantially restricted, premium increases and underwriters withdrawing from the market. Have we learned our lesson?

Following are the top 10 myths of securing D&O insurance.

1. All D&O policies are the same

One of the great attributes of the D&O segment is no two policies are alike. Often, buyers want to view the coverage as a commodity and base their decision on price. That does an injustice to the directors, officers and company, plus hinders opportunities to create coverage that is tailored to the uniqueness of the company and the industry it serves. Each underwriter has designed a policy for an intended objective, with a unique approach to protecting the insured's directors and officers. The obvious differences are policies designed to address: general partnerships, public companies, real estate investment trusts, financial institutions and private companies. The differences within "specifically designed" policies can be paramount to having a claim covered or excluded.

2. Two brokers assures the best deal

It is completely untrue that having more than one broker causes confusion, lack of interest, and the dilemma of who to turn to for unbiased recommendations and analysis. In a commodity-driven auction process, the need for managing the process and analytical requirements do not exist. That is not the case in D&O. Underwriters want to invest their time when they know that the decision-making process will be comprehensive and fair. Most long-term, quality D&O underwriters want to provide value (solid coverage at a fair price), not a cheap product. With the high volume of submissions, underwriters must efficiently invest their time and energies. The best "value added" a broker can provide is a well-managed, controlled marketing process with unbiased comprehensive analysis of all the proposals, followed by the services that might be required in a claim. A good broker will take time to understand the client's business, competitors and industry.

3. Company ratings do not matter

In the past two years, a number of D&O underwriting companies have withdrawn from the market, such as Quanta, Gotham, Genesis, Gulf, etc. D&O coverage is not one you want to lose, and it is often not easily replaced.

Although a rating cannot guarantee the insurer's future commitment, it is one sign of the likelihood of financial longevity. The lifespan of a D&O claim averages three to five years. Be proactive and consider a company's rating when making a buying decision.

On multiple layered programs, a carrier's rating should be a serious part of the decision-making process. Excess D&O policies state that the layer insurance does not apply until the "exhaustion of the underlying limits." Problems can occur when a carrier in the middle of a multi-layered program disappears during the claims settlement process.

4. All excess D&O policies are "follow form" of primary terms

Only one market offers a truly "excess follow form" certificate. The industry's excess policies are four to eight pages for a reason; they have their own terms, conditions and exclusions. And, they are negotiable. Often, brokers do not invest the time to customize excess polices to "mirror" the primary terms.

5. D&O policies are not negotiable

Almost all aspects of the policy are negotiable. There are few exceptions based on reinsurance. Insureds and brokers should set priorities and goals before the process begins, and hopefully the broker has the relationships and contractual expertise to negotiate the wording to enhance the protection.

6. The best coverage is offered by the biggest carriers

The biggest writers have tested policies and often good contractual wordings. Yet many D&O underwriters that are not household names provide broad policies for insureds. Often, companies competing with the "big boys" enhance their wording to compensate for the lack of public perception or a smaller distribution network. In some but not all cases, lesser-known underwriters can form partnerships with their insureds and understand the "risk" better. Carriers, size, reputation and claims handling need to be taken into account. Big does not necessarily mean best. The history to the senior D&O underwriters also should be considered.

7. D&O carriers do not pay claims

At one time this myth might have had validity, but the claims process has improved in the past 15 years. Although there can be challenges, there are no small D&O claims. Insurers, with some assistance from state attorneys general and departments of insurance, have enhanced their claims personnel and aligned their objectives to parallel the insureds. The claims process of D&O litigation is complex and has many constituents. Instead of the insurer being an adversary, it is often in the company's best interest to have a united front with the Ds&Os against the plaintiffs.

8. One carrier is better than two or more on larger programs

There are different philosophies depending on whether the insured is public or private, buying $10 million or $100-plus million in coverage, and the long-term strategy. Some consider layers as the "Great Wall of China" because of potential challenges in claims' settlements. Layering a program often has more advantages than a single layer approach.

9. Continuity with a carrier doesn't matter

All things being equal, it is better to build continuity with a D&O underwriter. Not only will the premium help during a claim, but the issue of coverage continuity has a large effect on the rights of the insureds. The advantages of a renewal (short) application versus the new business (long) application should never be underestimated, especially with public D&O. The nature of D&O claims being catastrophic logically suggest that building a premium war chest makes sense. That said, if switching substantially enhances the contractual wording, quality of insurance company(ies) and long-term strategy, then the quicker the insured makes the move, the faster the advantages will be realized.

10. Switching carriers often won't make a difference

Continuity matters in the underwriting community. When submissions arrive at the underwriters' desk, the history of that insured is available and reviewed. Today's underwriters invest their resources for the best return, and changing the account every year does not send the perception of an inviting opportunity.

That does not mean the insured should not test the market or have an alternative. A broker can provide insight into the competitiveness of the expiring program and the probability of enhancing the insurance. IJ

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