The Case for Higher D&O Rates

By Anthony S. Galban, Vice President and Underwriting Manager for D&O Liability Insurance, CBER

Soft insurance cycles inevitably bring certain books of business to challenging points. In the professional liability insurance marketplace, this is nowhere more true than for the publicly-traded commercial directors and officers (D&O) liability business. For the past several years, due to the competitive environment, this business has sustained substantial expansions of coverage, steep rate reductions, and the erosion of deductibles.

Increased Exposure

These dynamics are not especially spectacular in and of themselves, given the market conditions. However, what is particularly impressive is that, while these dynamics have been taking place, the true exposure base of this business (the market capitalizations of the companies insured) has substantially increasedÐin some cases exponentiallyÐin the face of an unprecedented bull stock market. For publicly traded companies, market cap volatility often provides the foundation for damages, which ultimately impacts claim settlement values.

The importance of this point cannot be overstated. As an analogy, consider the insurance for a fleet of vehicles that has doubled or even tripled in size, and yet has still received a 30% to 50% premium reduction over that time!

Recent Settlements

Recent claims bear out this increased exposure. Several D&O settlements for publicly traded commercial accounts have already rocked the industry, and reflect almost no resemblance to historical claim settlement values. Consider these recent settlements:

- Waste Management $220 million
- Informix $142 million
- Cendant $2.8 billion

What Can Brokers Expect?

As a broker, you can expect underwriters to pursue tougher messages, as we endeavor to recover this business. While such messages will not generally be popular to an audience accustomed to years of sunshine, they are essential if we are to be mutually successful with this

business. You should practice "early awareness" on your renewals, to help in the management of this process. By and large, customers can and will appreciate issues that are articulated in a timely and convincing fashion.

The tougher questions: What to recommend to your clients? How much limit to buy? From whom to buy it? I wish I could provide a formula to answer these questions, but no such formula exists. Given recent claims, the best I can do is suggest that you recommend "as much as you can afford," and to "get it from quality capacity." It's a bit simplistic, but it's also a very real and honest answer.

What About the Competition?

This marketplace seems to be continually reinvigorated with new capacity that has no book, no history, and no claims perspective. Be wary of such capacity. There will always be a cheaper player, but usually it represents more fragile paper and an extremely "mobile" underwriting track record. This is unlikely to be in your valued customers' best interest over time.