Market Factors Not the Only Driver for D&O Policy Pricing

While the Directors and Officers (D&O) insurance market for Initial Public Offerings (IPO) and **Special Purpose Acquisition Companies (SPAC)** remains challenging in both pricing and capacity, the overall market predictions for public and private D&O insurance are cautiously optimistic as we head into the second and third quarters of 2022.

The D&O market remains in a holding pattern with 5% to 10% price increases as the world continues to experience economic uncertainty in the aftermath of the pandemic. The initial concerns about high volumes of company bankruptcies and/or security claims following COVID-19 have not materialized, and while inflation is a known concern, its impact on the economy is yet unknown.

Thus, insurers and underwriters are taking a more individualized approach to pricing and conditions of D&O policies. The general economic factors at play include the evolving regulatory environment and claims litigation, trends in cybersecurity, and concerns related to employment and management liability, but a company's industry subset and unique business operations activities are what's driving the underwriting decisions on renewals.

Retail agents and brokers looking to obtain the most favorable prices and terms for their insureds should begin the renewal process early to evaluate client exposures related to both general market factors and unique operations.

CONTACT

To learn more about how Amwins can help you place coverage for your clients, reach out to your local Amwins broker.

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Evolving Regulatory Environment & Claims Litigation

The Securities and Exchange Commission (SEC) enforcement activity against publicly traded companies and their subsidiaries declined in 2021, which was not unexpected considering the change in administration.

Activity is expected to resume in 2022, and while the SEC has signaled to investors and the marketplace that it will focus on SPACs and related regulation, that is not the only area likely to face scrutiny.

The Department of Justice (DOJ) and SEC have also stated intentions to monitor the following areas that have a potential impact on D&O policies:

- SEC intends to closely monitor fees charged by private equity firms and hedge funds.
- DOJ will increase vigilance related to corporate crime and specifically individual accountability of senior leadership.
- DOJ continues to crack down on fraud under the False Claims Act (FCA), with a focus on violations related to COVID-19 relief like the Paycheck Protection Program (PPP).
- Legislation and regulatory requirements for board diversity (e.g., California law, SEC support of NASDAQ guidelines) will face legal review. Lawsuits contending that board members breached their fiduciary duties by failing to elect or appoint diverse board members have been largely dismissed, but the issue remains in the public eye.

Trends in Cybersecurity

As cyber losses related to ransomware, social engineering and privacy breaches continue, cyber security controls and disclosures remain an important part of the D&O market.

The decisions related to cyber security—everything from funding the IT department to what coverages to carry for cyber insurance—are often made at the board level for both public and private companies.

In the current market, company cyber security is often viewed as a board responsibility not only as it relates to mitigating risk with security controls, but also as it relates to business continuity planning in the event of a breach.

Even with separate cyber coverage, D&O claims related to cyber are expected to increase in 2022, particularly for financial institutions where social engineering vulnerabilities continue to create costly exposures.

Employment Practices and Management Liability

While employment-related claims are generally covered by EPLI, there has been a growing trend to hold the board of directors responsible for establishing company culture and creating precedent for management practices. For example, directors and officers have been sued for breach of fiduciary duty for failing to monitor company compliance with anti-discrimination laws.

Public awareness of employment issues—for example the spotlight #metoo put on sexual harassment in the workplace—has made insurers increasing leery of mismanagement in private companies and particularly cautious that wrongdoing might be covered up at the executive level.

Current employment-related concerns impacting the D&O market revolve largely around the effects of COVID-19—namely allegations that employers have failed to ensure employee safety or that vaccine policy enforcement has failed to appropriately accommodate employees' needs.

Unique Business Operations

While market trends always influence an insureds' ability to obtain coverage, determining policy pricing, terms and conditions is ultimately dependent on the unique exposures of the insured and the coverages desired.

Among the factors that underwriters will consider when renewing D&O policies is if the company has recently experienced any of the following:

- Substantial fluctuation or variations in financials
  - Increases inspire as many questions as decreases
- A change in company leadership or members of the board
  - Public behavior of potential named insureds
- Seemingly negative news
  - Mass layoffs, locations closing, losing largest client, etc.
- Alterations in company structure
  - Pending sale, Mergers & Acquisitions, IPO

If the company has experienced any noteworthy events, it's important to address them in the submission to answer any questions upfront. Underwriters will Google companies and if they find information that wasn't disclosed by the company, it can raise a red flag for additional undisclosed or underestimated exposures.

Takeaway

While it sometimes seems like insurance forms are one-size-fits-all and market factors alone drive underwriting decisions, it's important to remember that policies can be, and often are, tailored to fit the insureds' needs when unique risks are specifically addressed in the submission process. Working with an Amwins' experienced broker not only gives you access to specialized markets, but also expert guidance to negotiate the most favorable terms for your insured.

About the Author

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