## *Insurance Times*: D&O costs skyrocketing

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NEW YORK — Alarming increases in the costs of litigation against directors and officers (D&O) — particularly shareholder litigation — as well as widespread concerns about high-profile bankruptcies and the quality of corporate accounting and financial reporting are among the principal reasons for a dramatic increase (29%) in D&O liability insurance premiums.

These findings are according to Tillinghast - Towers Perrin's 2001 Directors and Officers Liability Survey.

Also, according to the survey, D&O claim frequency has remained stable, yet severity has generally increased, with significant increases for certain types of claims. Among closed claims overall — excluding those closed with no payment — U.S. participants paid an average of $5.65 million to claimants, up more than 75% from the 2000 survey. The average indemnity paid to shareholder claimants was at an all-time high of $17.18 million, compared with $9.62 million last year.

The technology and biotechnology sectors, firms with a recent IPO and those experiencing financial distress were hit especially hard by premium increases.

Discrimination in employment was again cited as the most frequent D&O claim issue, accounting for 46.1% of employee claims and 26.8% of claims overall.

Issues related to financial disclosure continued to be the most common among shareholder claimants, representing 38.8% of shareholder claims and 9.2% of claims overall. Disclosures of publicly traded companies are an area of increased concern among D&O insurers due to the significantly higher cost of claims related to such disclosures, including those associated with stock offerings (e.g., IPOs).

Premiums: A Hard Market

The sharp rise in D&O premiums last year, higher than the 11% average increase reported in the 2000 survey, was the most dramatic increase since the hard market of the mid-1980s. These increases, however, also represent a reversal of five years of significant premium decreases, which, when combined with the growing costs of litigation, turned insurer profits into losses. While the total amount of D&O coverage offered by insurers in 2001 was down only slightly from the record levels reached in 2000, many D&O insurers have become increasingly restrictive as to which potential insureds qualify for their full coverage capacity.

"Current conditions do not signal that there is a crisis in the market," said Mark Larsen, a Tillinghast - Towers Perrin consultant and the survey director.

"However, claim severity trends are likely to continue, given the large number of D&O litigation cases outstanding. Companies should diligently evaluate the adequacy of the amount of D&O insurance they purchase and take a longer-term approach in their negotiations to seek the best value. Business class, merger and acquisition activity and financial strength remain key elements of the premiums being quoted."

Among American respondents, D&O coverage was virtually universal, at 97%. The average amount of coverage purchased was $20.1 million. Policy limits also increased for the seventh straight year, with 15% of U.S. participants obtaining greater limits and less than 5% lowering limits.

"Companies see D&O coverage as a necessity in spite of increasingly stringent underwriting by insurers, which requires many companies to build their D&O insurance program by purchasing smaller layers of insurance than they might wish or by employing quota share arrangements," says Jim Swanke, leader of Tillinghast - Towers Perrin's Strategic Risk Financing practice.

The survey shows a leveling off of the frequency of D&O claims, but an increase in their severity, as indicated by the rise in median and average payments and defense costs. The average indemnity payment among closed employee claims was $0.25 million, up slightly from $0.24 million last year.

Defense costs for closed claims overall increased to $0.54 million from $0.49 million in the 2000 survey. Nearly one-third of all claims filed against U.S. companies are class actions, which are typically expensive to defend and often result in very large payments.

D&O claims were more than twice as likely against companies with a history of merger and acquisition activity, and publicly traded companies were more than twice as likely to experience a claim than their private counterparts, the report said.

According to the report, employment practices liability (EPL) is also a growing concern of U.S. risk managers due to a culmination of statutes enacted since 1990, such as The Americans with Disabilities Act of 1990, The Family and Medical Leave Act of 1993 and The Civil Rights Act of 1991. For example, the Civil Rights Act introduced both punitive damages and jury trials into EPL litigation — an explosive combination.