

ALERT

## Can Rising Prices for Insurance Ever be Good News for My Executive Insurance Program?

by William G. Passannante

Is the recent tightening in the Directors & Officers (D&O) liability insurance market good news for my executive insurance program? D&O liability insurance is sold to protect senior management against claims alleging wrongful acts. For years the market to sell this type of insurance has been popular among sellers of insurance policies. Insurance companies which had never previously participated have been fighting to sell policies and grab market share.

These market conditions helped contribute to a 'soft' market (with little upward pressure on prices) favorable to purchasers of D&O liability insurance policies. Now, for the first time in years, there are indications that substantial hardening is taking place. Indeed, AIG with a U.S. market share of twenty-nine percent (29%) of the primary-level D&O liability business, has indicated that prices for this important coverage have stopped falling and the number of new expanded coverages offered has slowed. Insurance companies have been seeking increases of from ten percent (10%) to forty percent (40%) for certain industries which have suffered losses.

A representative of Marsh Inc., one of the world's largest insurance brokers, has indicated that "[t]he market is in the midst of a correction." There certainly appears to be a concentration among sellers of D&O insurance policies. Tillinghast-Towers Perrin reports that in 1999 the top three insurance companies by premium volume (AIG, Chubb and Lloyd's) controlled sixty-six percent (66%) of the market for D&O policies. Even so, brokers still say that the significant number of competitors selling policies will attenuate any increases.

### *Can Higher D&O Prices Be Good News?*

For years, the soft market has helped keep premium levels down. Some observed that the premiums were so low that insurance companies could not (or would not) pay claims that otherwise should be paid. Lower prices, all other things being equal, are better for the insurance consumer. D&O insurance companies should know better. If they promise to defend and pay D&O claims they should do so. If their under-

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Insurance Alert. Mr. Passannante is also Vice Chair of Anderson Kill's Insurance Coverage Group. He has represented policyholders in litigation and trial in major precedent-setting cases. Mr. Passannante is a Vice Chair of the Professionals, Officers and Directors Liability Committee of the Tort and Insurance Practice Section of the American Bar Association. Mr. Passannante has been a member of the Directors and Officers Liability Committee of the Insurance Committee of the Association of the Bar of the City of New York.

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writers insist on underbidding new-entrants to the D&O insurance industry it should not effect the broad coverage grants sold. If only the reality were so. Higher prices are not good news. But low prices for a D&O policy sold by a company with a rotten claims-paying philosophy is no bargain.

### *Find the Good Insurance*

If you can't get claims defended and paid a D&O policy is worthless. Purchasers of D&O policies should find an insurance company with a fair price and a proper approach to claims handling. The D&O insurance market has been evocative of Sir Thomas Gresham's sixteenth-century observation ("Gresham's Law") that "bad" money drives "good" money out of circulation. Identifying D&O insurance companies that sell "good policies" is one challenge for D&O purchasers.

Policyholders who bring claims under D&O policies frequently find themselves in coverage disputes. Insurance companies have an unfair

advantage because they are familiar with the insurance issues that arise in a D&O claim, but policyholders generally are not. According to the 1999 Tillinghast-Towers Perrin D&O study, companies of all sizes have experienced stable, or increasing, D&O claim frequency in recent years. D&O claims often are significant involving multiple millions of dollars of defense and indemnity expense. Research by National Economic Research Associates indicates that the average cost to settle a federal securities case rose 40% in 1998, to almost \$11 million. Regulation FD has increased uncertainty in this area.

#### Examine the Claims Handling Philosophy

Policyholders should be concerned with the handling and payment of claims, not just lower premiums. Insurance industry sources acknowledge that "overly liberal expansion of D&O policies may come back to haunt insurers when claims come in." Whether your insurance company pays a claim is crucial in many high-stakes D&O claims. A look at D&O litigation shows one extreme of the claims-paying spectrum.

A case decided in March 2000, *TLC Beatrice v. CIGNA*, should make cautious Directors and Officers blanch. The Chairman and CEO of the policyholder was the target of a shareholder's derivative lawsuit. CIGNA, the insurance company, sent repeated letters describing its view that the lawsuit was not covered. The policyholder settled the derivative lawsuit on its own. Remarkably, CIGNA asserted that the policyholder's failure to obtain consent to settle the case eliminated its obligations to the policyholder! The court agreed. This leaves one wondering whether handling the insurance company correspondence differently might have led to a more favorable result. ■

*The information appearing in this newsletter does not constitute legal advice or opinion. Such advice and opinion are provided by the Firm only upon engagement with respect to specific factual situations.*

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