Lowenstein Sandler's Insurance Recovery Podcast: Don't Take No For An Answer

Episode 85:
An Update From the Front Lines -- The Current State of Play in the D&O Market

By [Lynda A. Bennett]

MARCH 2024

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Lynda Bennett: Welcome to "Don't Take No For An Answer." I'm your host, Lynda Bennett, Chair of the Insurance Recovery practice here at Lowenstein Sandler. Today, I am very pleased to welcome back Rob Crocitto, president of ARC Excess & Surplus, and Lynn Mirabella, who's a senior broker and partner at ARC Excess & Surplus. Thanks for joining me today.

Rob Crocitto: Hey, Linda. It's nice to be back.

Lynn Mirabella: Thank you for having us.

Lynda Bennett: Pleasure. Today, I had to bring you two experts on to talk about what's going on in the D&O market. As we know, the last four years has been a rollercoaster ride for policyholders. Back during COVID, it was a very hard and difficult market. People had to gulp when they were going into their renewal process. But it seems as though conditions have changed and would love to hear from you two, who are on the front lines of placing coverage on behalf of policyholders, exactly what's going on. Why don't we jump right in?

As we begin 2024 in earnest, why don't you give me some insights on how the renewal season is shaping up for policyholders in the D&O market?

Lynn Mirabella: I can start with the prior company side. In general, premiums, retentions and coverage is pretty flat. In pricing, we're definitely seeing still reductions in the space. We definitely have more flexibility to get reductions in retentions, which has been helpful. On the coverage side, as brokers, our main focus is always to improve coverage. I think for private companies, it's still in a pretty good spot, it's still a soft market.

Lynda Bennett: We're able to negotiate terms and conditions a bit more?

Lynn Mirabella: Yes, that's definitely our focus. Each year we're remaining with the incumbent carrier, our goal is to obviously get the price down as much as we can if it makes sense, but also focus on coverage because my goal is to have the broadest coverage at the best price.

Lynda Bennett: Lynn, would you say that we're really normalizing back to what pricing was pre-COVID-19, or is there any lingering hangover effect from when the world turned upside down in 2020?

Lynn Mirabella: I definitely think we're back to 2018, 2019 rates. I don't think there's going to be much more movement down. I think you're going to start to see a flattening of pricing in the market. Unless there is significant claims on an account, I think you're still going to, at this time, get a few point reduction if it's an easy placement, and I don't want to say anything's easy. If there's high quotes, you might get a larger reduction. It depends on the ability to secure alternate options.

Lynda Bennett: Well, that's good news for risk managers' budgets. That's wonderful to hear. Are you seeing any particular areas that insurers are probing on renewal? A couple of things that I've seen with clients are a few more questions about compliance or privacy, things of that nature.

Lynn Mirabella: Since COVID, I think those COVID questions have gone away. They're not so much focused on the COVID protocols in the office I think there's probably a focus on working from home. I've seen a fluctuation in employee counts, a lot more than I'm used to seeing. At this moment, I don't see much focus, I think you'll start to see a focus on the AI usage with certain larger insureds, I think. But at this time, the smaller space, there's not so much focus on anything that's concerning.

Rob Crocitto: Lynda, if I could just chime in for a minute-

Lynda Bennett: Please.

Rob Crocitto: On the COVID side. I think the biggest hangover we're seeing, for lack of a better term, is that it's very difficult to get some underwriters on the phone on Mondays and Fridays because they're working from home. Otherwise, it's business as usual.

I know Lynn gave you some perspective on the private side. I wanted, if it's all right-

Lynda Bennett: Please.

Rob Crocitto: On the public side that we're seeing is robust competition, especially on the excess placements. As we discussed earlier, there are so many new entrants into the market, and we'll get into that, because those new entrants are definitely going to be improving the buying process for the policyholder because supply and demand, with all this excess capacity that's out there, or extra new capacity that's out there, we're able to essentially use that capacity to effect healthy competition. Many of these new entrants are predominantly focused on excess D&O. Many of them came in with limited staff, limited claims abilities. They basically came in with strong capital, a decent management team. Many of them have phenomenal management teams.

They were really looking to just write excess because it's a one-page excess policy.

Lynda Bennett: If you're lucky.

Rob Crocitto: Now, in order to survive in this business, considering the rate environment we're in, you have to be able to write primary or you're not going to last very long because there's so much competition and the rates that are out there have been diminished.

Lynda Bennett: I'm glad that you brought up new entrants though, Rob, because one of the areas that team Lowenstein and team ARC are able to work very closely on is looking at the devil in the details of those new policy forms and the wording.

Eric and I just did a podcast episode on a terrible decision out of the Third Circuit for an eight-layer excess carrier that had really bad language in that policy, and it voided $10 million of coverage. I know that you, Rob, and Lynn, and your entire team know you got to have eyes on the actual words. I always get a little prickly when I hear that we're going to place with a new entrant in the market and it's so important to look at the actual wording of that policy, see that it really is a one-pager and nick in with some endorsements. We've all seen that movie before.

Lynn Mirabella: Yeah.

Rob Crocitto: It's what's you're buying.

Lynda Bennett: Exactly. What about, at a high level in renewal for either public or private companies, ESG and DEI? The last couple of years, we've heard a lot about ESG. DEI initiatives have really come under attack in the wake of the Harvard decision. What are you seeing in terms of interest level on those two areas among underwriters right now?

Rob Crocitto: Yeah, it's going to be much stronger on the public side just because of the size of the companies and the fact that there's an investment community looking at governance, and things along those lines.

Years ago, Lynda, a public company D&O renewal entailed us, the broker, putting the CFO in front of a bunch of underwriters, and he or she would speak of their financial condition, and we'd get quotes. Things have changed a lot. Things have changed a lot over the last few years. So nowadays, to get a real public company D&O renewal done the right way, you need to anticipate what's keeping the underwriters up at night, and it's not just the financial condition but it's whether or not the company's compliant from a DE&I perspective, whether or not it's compliant from an ESG perspective. Whether or not the company's compliant and has the right cyber liability practices and protocols.

The players on a deal have grown from the underwriters, the broker and the CFO, but now we're adding the chief information officer. In many cases, we're adding the general counsel to talk about litigation, or to talk about DE&I

and ESG. In some cases, we're even rolling out the director of human resources, to talk about hiring practices and procedures, which has become so prevalent as of late.

Lynda Bennett: Well, I got to give the shameless plug again, to you and your team, because you do know how to prep clients for those kind of meetings. I always tell clients when you're going into a renewal or you're going into a meeting with a new potential suitor for a carrier, you don't get a second chance to make a first impression. Getting those executives on board in understanding how to speak the language of the underwriters is crucially important, and you guys certainly do that no better than any other brokers I've seen.

Let's talk about other factors here, in the D&O market right now. Are there any industries that you would characterize as particularly challenging to place insurance for right now?

Lynn Mirabella: Yeah, I'll take that one. Basically, I'm like the boots on the ground. Basically, I'm busy placing coverage or securing quotes daily. I definitely think the banking industry is having a tough time, healthcare, crypto, cannabis. The IPO space is still a challenge.

But I also think one thing that's probably going to become a larger problem this year is any political rep. Any space that has exposure to politics is really going to be a challenge and I think the majority of political action committees, for instance, are written on non-profit forms. These non-profit forms tend to be broader, where they not only cover D&O claims, but they cover EPL claims as well. But their pricing is not in line with what private companies are paying. They get one claim, it could be an EPL claim, they're paying $5000 for their policy, their claims are still $1 million. If it's a massive claim, they're very expensive. I think in that space, I think we're going to see an uptick in claim activity.

Lynda Bennett: Lynn, to that point, are you telling me that those companies, like a crypto, or a cannabis are uninsurable? You can't get insurance for them? Or are we talking more about pricing and self-insured retentions?

Rob Crocitto: Yeah. We could get coverage for anything. There's a seat for every butt, it's just a question of how many players are in the space and whether or not the client is in a position to A, afford the coverage, and B, explain to their boards why they're spending so much money protecting themselves individually. They have to explain to the shareholders.

It really comes down to the industry. For instance, the crypto industry, if you had asked me this question two years ago, I would say there's one or two insurance companies that can potentially dabble in it. Now, there's way more than a handful so that environment has loosened up a lot as crypto and blockchain become more of a household name. Cannabis, a couple years ago, was near impossible to get insurance for. Now, we have multiple markets able to do it. But a company that's in the cannabis or crypto space is going to pay a lot more money for its D&O insurance than a manufacturing firm in Michigan. That's the struggle we have, is just making sure that the clients understand because some of these insurance companies, while they're able to write it, they're putting restrictive terms on it.

Lynda Bennett: Right. Yeah. Well, they're insurance companies so they like to follow the money, but they're going to price the risk. Those couple of industries are what some plaintiff's lawyers look at as target rich environments, we'll call it.

All right. How is the industry responding to the heightened regulatory environment that companies are facing right now? We're seeing a lot of activity not only in SEC, FTC. Washington's active. How is the D&O market responding to that?

Lynn Mirabella: Yeah. I think on the underwriting side, there's definitely certain classes of business that are being underwritten more stringently. They're definitely putting sub-limits of coverage on certain coverages. Antitrust, books and records, derivative demand investigations. They're still sub-limiting those coverages and they know that it's a real exposure. We definitely have a struggle to get those coverages up as high as we can get them on larger towers, let's say. The carriers are definitely pushing back on that, as they have done in the past, too.

Rob Crocitto: Yeah. And onto what Lynn's saying, remember, a books and records demand is covered under the derivative investigative sub-limit. These are limits that are provided, typically in a policy, at no additional cost, in a public D&O policy, and there's sub-limits that are provided on a first dollar basis. We're starting to see a real uptick in these claims. I think the struggle is going to become where we used to be able to get, let's just say the primary company's putting up a $5 million limit with a $1 million, or let's just say $500,000 derivative investigative sub-limit that's picking up the books and records demand. We used to be able to get companies to throw in a 5X of five and stack a $250,000 derivative investigative sub-limit over that at not additional cost. I think the excess market is still soft enough that we'll be able to get it done, but I think there's going to be a lot more underwriting around this free coverage that's being given.

Lynda Bennett: Right. Policyholders need to know to ask. Once again, not all brokers are created equal. ARC certainly is attuned to this, but other brokers, not so much.

I'm going to wrap it up with another burning question. What's going on with AI? How are D&O insurers and underwriters reacting to this? Are they paying attention to it? It seems like we can't open our Google News without hearing about the latest problem that AI is causing or disrupting in our society. How are D&O insurers thinking about this?

Lynn Mirabella: I think this year is going to be the year that they're going to start to look at this definitely more closely. I think you may see a supplemental application in the works. I think they might start to really ask questions around it, because knowing how these EPL applications, and I'll speak about the EPL because I think it's going to be an issue on the employment practice side more right now than on the DO side. But, I don't thinks these applications are equipped, the ones that are in the market that are being used with the clients. They're not equipped to ask the right questions at this time. I think what we're going to see is a supplemental application designed and it's going to be out there. I think this is the year that the carriers are probably going to start to focus on the AI exposure of their clients.

Lynda Bennett: Maybe they're using ChatGPT to formulate that application for us, Lynn. Who knows?

Lynn Mirabella: They are. They probably are.

Rob Crocitto: I wouldn't doubt that. Lynn gave it to you from a private company perspective. On the public company side, there is no renewal application. The underwriters rely on what's publicly disclosed with the SEC, 10K, 10Q, and the other public filings. We all know that, when a company makes a public disclosure about anything, the street reacts. What a company discloses about its AI is being carefully looked at by underwriters now. If a company's just saying, "Oh yeah, we're very active in AI and we use it all the time," when there's no detail behind it, there's no explanation, underwriters are digging in on this. They want to see exactly how it's being used and what these companies are doing from a disclosure standpoint, to make sure that what they are in fact doing is being adequately disclosed, so that obviously, when something's not adequately disclosed, it could lead to litigation.

It's something that's being looked at definitely more closely on the public side. Just as Lynn said, on the private side, I think we can expect some more detailed underwriting questionnaires around the topic versus relying on public disclosures on the public side.

Lynda Bennett: That's a great point, Rob, because we can be certain that the plaintiff's bar is going to be carefully combing through public disclosures with a particular eye towards AI.

Well, I really want to thank both of you, Rob and Lynn, for coming on today to share your knowledge. I think it's great news for policyholders that the market is soft right now and the prices are coming down, and negotiability of terms is coming up. We will certainly have you back to let us know how things are going later in the year. But really appreciate your time today, and all of your insights and expertise. Thanks for joining us.

Rob Crocitto: Thanks, Lynda.

Lynn Mirabella: Thank you, Lynda.

Lynda Bennett: All right, we'll see everybody next time.

Lynn Mirabella: You, too.

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