

Executive summary

We are pleased to present FINEX's Insurance Company Market Update for Q1 2020. In this issue, we explore the current state of the Directors' & Officers' and Insurance Company Professional Liability (ICPL) insurance marketplace. In addition, we identify new and emerging issues within the insurance company industry and discuss what impact those issues may have on insurance policies.

As Q1 2020 came to a close, the entire world was responding to the unique and unexpected personal and professional challenges presented by the COVID-19 pandemic. Unprecedented in its scope, the virus itself, along with the market volatility that followed, has already had tremendous consequences for virtually all industries and all lines of coverage across the globe. It has been the most significant issue affecting both insurance company and the D&O and ICPL insurance market this quarter and will likely continue to do so for the foreseeable future.

Though the full extent of the virus' impact on D&O and ICPL insurance for insurance companies is yet unknown, we do know that the pandemic has added a new layer of volatility on top of an already challenged insurance environment. Insurance companies are facing greater public scrutiny than ever, as they are subject to a complex set of new mandates which vary across state and continue to evolve over time. As a result, the marketplace is taking a far more cautious approach to the renewal process and are expected to be far more invasive in their underwriting protocols than in years' past. Renewals will be challenging so beginning the renewal process early is critical, as D&O and ICPL carriers will likely seek increases in both premiums and retentions, while carefully managing the limits they will provide and scope of coverage they will afford.

Although the COVID-19 pandemic is the most prominent issue currently, we have not lost sight of the fact that other new and emerging issues are also affecting the insurance company industry. Noteworthy items addressed within this edition include cost of insurance litigation, complex and evolving regulatory framework, social inflation and the effects of climate change on the industry. We discuss these issues in detail and identify the potential implications they may have on an insurance company's risk profile, as well as their D&O and ICPL policies.

There are many challenges facing insurance companies this year. However, we hope this publication offers valuable insights to help you successfully navigate through these turbulent times. Should you have any questions or wish to discuss any of these issues in greater detail, please engage myself or a member of your Willis Towers Watson team.

Kevin Kirby

Insurance Company Market Update

ICPL Insurance Market: 1Q 2020 Update

Cost and retentions



- **Pricing:** Premiums are rising, with even favorable accounts subject to rate increases of 5-15% as a starting point.
 - Those insureds with poor claims experience and/or more challenging risk profiles can expect increases of 15%+.
- Retentions: Substantial pressure is being applied to increase retentions in line with growing legal fees and settlements.
 - Several industry Executives have cited 'social inflation' as a trend impacting settlement amounts which is not likely to subside.

Markets



- Appetite for primary ICPL is segmented by size and type of insurer - there are sufficient candidates for middle market business, but only a select few carriers serve as viable leads for large risks.
- London remains a primary market for Bermudadomiciled insurance companies as well as potential excess capacity for the US.
- The Bermuda market is largely limited to excess participation, though primary may be considered with a minimum retention of \$5m.



- Favorable: subsets include mutual insurers. reinsurers and middle market insurers (less than \$2bn in revenue).
- Unfavorable: life insurers, auto, long term care and P&C insurers with outsized exposure to areas impacted by natural disasters.
- Much of the underwriting process is focused upon geographic diversification of the insured, with an emphasis upon demonstrating an understanding of and process for navigating regulatory hurdles.
- Increased scrutiny on insurers with substantial exposure to COVID-19 both in terms of contractual liability and on the investment side.

Capacity



- Carriers have looked to scale-back limits to no more than \$10m for a single policy, though historical levels of \$15m+ are less prevalent on the E&O than for D&O.
- Primary ICPL remains a loss leader for carriers, relative to other financial institutions, so packaging opportunities on the ICPL in conjunction with more profitable lines of coverage may be necessary to drive meaningful competition.
- Excess layers remain more competitive as a number of markets are willing to attach higher up on programs.

Coverage



- Broad regulatory coverage is of paramount importance, with an increasingly complex supervisory framework among State, Federal and International regimes.
- Sales and marketing coverage for life insurers is difficult to obtain, with many markets solely affording sub-limits, higher split retentions or excluding altogether.
- Starting in the UK and Europe, carriers in the US have begun to address 'silent' cyber through the addition of clarifying language which either affirmatively grants or excludes coverage for claims related to a cyber event. No uniform approach has been adopted to date.
- Mitigation coverage for costs incurred in remediating or mitigating a potential loss is available in the UK marketplace.

Impact of COVID-19



- The impact of the pandemic on Insurance Company D&O and ICPL renewals is yet to be fully determined and is evolving daily.
- Carriers are generally behaving very cautiously, with competition significantly reduced as the appetite to compete for new business has largely dissipated.
- Allow for more time in the renewal process and expect several questions relating to both the impact of, and response to, the pandemic.

Key issues to watch

Cost of Insurance -**Universal Life**



Observation:

With interest rates at historical lows and stock markets in freefall, carriers with Universal Life Insurance exposure are struggling to keep associated cash value accounts above water. In order to sustain the policies, insurers have been forced to adjust the premiums charged to policyholders and have faced significant litigation as a result.



Insurers face challenges both from regulators and from class action policyholder suits as to whether adjustments to premiums are illegal or outside contractual bounds. Several such cases have settled with amounts in excess of \$100M. According to the WSJ, regulatory bodies were already aiming to implement new disclosure rules prior to equity markets being decimated by COVID-19.



Insurance companies need to secure the broadest regulatory and investigations coverage possible. Care must also be taken to limit the applicability of exclusions pertaining to underwriting, contractual liability and inadequacy of reserves. Coverage specific to sales & marketing practices may also be implicated.

Cybersecurity Requirements for Insurers



Observation:

The National Association of Insurance Commissioners (NAIC) proposed a Data Security Model Law in 2019 which has been adopted by 8 states, with other states likely to follow the lead of NY and CA in implementing their own regulations. Outside of the US, General Data Protection Regulation (GDPR) in Europe applies stringent guidelines and threatens substantial penalties for failure to implement appropriate controls and procedures



Failure to juggle an increasingly complex and evolving regulatory framework could result in substantial fines and penalties. Insurers must be able to demonstrate that they have maintained a robust information security program.



Insurers - particularly those operating on a national or international basis - must ensure that all applicable regulations are being accounted for and adhered to. Interplay between the D&O, E&O/ICPL and Cyber insurance policies should be carefully considered, especially where the market may look to address "silent cyber" through an exclusion.

Key issues to watch (continued)

Climate Change



Observation:

Insurance companies face exposure to climate change on multiple fronts. There is risk for P&C carriers which insure against natural disasters, reputational risk in insuring companies connected to fossil fuels and challenges both as an investor (in selecting which firms to invest in) and as an investment (attracting partners seeking ESG adherence). Failing to address any of the foregoing exposures could result in liability for Directors and Officers, coming from regulators, shareholders and potentially sovereign nations as a human rights issue.



Leadership at insurance companies - particularly those which are publicly-traded – may be held liable for taking inadequate steps to prepare against Climate Change risks.



Coverage for investigations and special sublimits like Public Relations Costs and Asset Protection Costs are especially important given the focus on individual accountability. For multinational insurers, those serving unique functions such as the UK's Senior Managers and Certification Regime (SMCR) should affirmatively be granted coverage.

Social Inflation



Observation:

The term "social inflation" has featured prominently in recent earnings calls and commentary among leadership in the P&C insurance industry. Many executives have attributed challenges in profitability to this dynamic, particularly when it comes to commercial auto insurance and general liability.



Social inflation is anticipated to drive an increase in frequency, cost to defend and ultimate settlements for certain classes of business.



Limit purchase should be revisited to account for the substantial increase in settlement values - particularly as it applies to extra-contractual liability.

Conversely, insurers of ICPL are looking to impose higher retentions and premiums to counter this same dynamic.

COVID-19 impacts

COVID-19: Regulatory Environment



Observation:

State mandates, like cost-sharing waivers for healthcare expenses, may lead to significant additional costs for insurers. Several states have explored legislation compelling insurers to reimburse policyholders for claims which are explicitly excluded.

S&P's latest estimates are that the coronavirus could result in \$30bn-\$90bn in insured medical expenses in the US – the higher end of the range representing almost 100% of annual revenues for impacted insurers.



Concern:

As states are applying new mandates around policyholder notification, barring standard cost-sharing practices and potentially requiring insurers to pay uncovered claims, insurance company clients need to stay on top of these evolving requirements for all jurisdictions that they are exposed to.



Insurance companies must have robust processes in place to monitor and adhere to the rapidly changing regulatory landscape. The scope of regulatory coverage under policies remains a key priority to address any potential lapses or oversights.

COVID-19: Sales and Marketing



Observation

The Chairman of the House Oversight and Reform Subcommittee on Economic and Consumer Policy has launched an investigation into travel insurance industry practices after carriers have indicated that coverage may not apply for coronavirus-related claims. Similar exposure may arise for other lines of coverage (ie healthcare and business interruption) where policyholders may have thought coverage would have applied due to advertising practices.



Concern:

With policies (healthcare, travel, etc) being tested more than ever before, the disclosures and representations made in the marketing of products – especially when it comes to individual and unsophisticated customers – may be scrutinized.



Suggestion:

Affirmative coverage for sales & marketing practice remains of paramount importance. This coverage is not widely available among the limited group of carriers willing to write primary, so insurance companies may need to accept either sublimits or higher retentions.

COVID-19 impacts (continued)

COVID-19: Investment Portfolio of Life & Health Insurers



Observation:

While the broader stock market and insurance companies generally have seen exceptional losses, life insurers in particular have been hit very hard. Shareholders have responded, evidenced by the S&P P&C Insurance Index trending down by 16% in March, while the comparable Life & Health Index saw a 29% reduction in value.

Rather than being tied to expected losses on the insurance side, much of the market sentiment is that life insurers have significant exposure on the investment side. Fitch Ratings cut its outlook on the life and health insurance industry to negative, citing lower interest rates and leveraged equity and corporate bond holdings as material challenges for the industry.



Concern-

With shares of public life and health insurers seeing tremendous drops, the likelihood of shareholders bringing suit increases.



Carriers are very wary of life insurers – especially those which are publicly-traded. Clients can expect to see their insurers revisit their total capacity on the D&O side and look to impose higher retentions.

COVID-19: Business Continuity Planning & Disclosures



Observation:

Business continuity planning is being stressed to the maximum and any perceived failures that negatively impact performance of insurance companies could lead to claims for failing to adequately prepare. Lack of accurate risk disclosures and perceived overconcentration to certain industries, classes of business and/or geographies could also lead to D&O claims.



Concern

Shareholders may allege that stated risk factors do not address the significant challenges resulting from the coronavirus outbreak. For publicly-traded insurers, any negative impact upon share price as a result of failure to adequately function during quarantine could give rise to a D&O claim.

From an IT perspective, underwriters are scrutinizing the ability of insurance companies as well as any vital third party services providers (ie TPAs) to operate remotely without a negative impact on service and claims handling.



Clients should be prepared to speak to their carriers regarding the evolving risk landscape and how the company is updating its disclosures to reflect such.

Challenging Venues & Jurisdictions

According to the American Tort Reform Foundation

Top 10 least favorable states, cities, counties and courts

Philadelphia Court of Common Pleas

A preferred jurisdiction for asbestos litigation and home to a \$8bn product liability verdict in 2019.

California

Stance against arbitration and broad application of employment law liability.

New York City

Significant amount of ADA claims against small business as well as consumer suits targeting the food and beverage industries.

Louisiana

Auto insurance outcomes and judicial misconduct.

The City of St. Louis, Missouri

Decisions have ignored state and federal precedent, expanding liability Premises liability, medical liability and nuclear jury verdicts are all on the rise.

Georgia

Premises liability, medical liability and nuclear jury verdicts are all on the rise.

Cook, Madison & St. Clair Counties, Illinois

Prominent venue for no-injury class action lawsuits, asbestos litigation and have been flexible in permitting questionable Biometric Information Privacy Act suits to proceed.

Oklahoma

Questionable handling of opioid litigation and Supreme Court interpretation has expanded liability.

Minnesota Supreme Court / Twin Cities

Expanded medical liability and employer liability under workers' compensation laws, while upholding disputed sanctions against an in-state employer.

New Jersey Legislature

Anti-arbitration and introduced a "Wage Theft" bill with substantial penalties.

Watch list: Colorado Supreme Court, Florida, Maryland General Assembly, Montana Supreme Court, Supreme Court of Pennsylvania, South Carolina Asbestos Litigation and West Virginia Supreme Court of Appeals.

Each applicable policy of insurance must be reviewed to determine the extent, if any, of coverage for COVID-19. Coverage may vary depending on the jurisdiction and circumstances. For global client programs it is critical to consider all local operations and how policies may or may not include COVID-19 coverage. The information contained herein is not intended to constitute legal or other professional advice and should not be relied upon in lieu of consultation with your own legal and/or other professional advisors. Some of the information in this publication may be compiled by third party sources we consider to be reliable, however we do not guarantee and are not responsible for the accuracy of such information. We assume no duty in contract, tort, or otherwise in connection with this publication and expressly disclaim, to the fullest extent permitted by law, any liability in connection with this publication. Willis Towers Watson offers insurance-related services through its appropriately licensed entities in each jurisdiction in which it operates. COVID-19 is a rapidly evolving situation and changes are occurring frequently. Willis Towers Watson does not undertake to update the information included herein after the date of publication. Accordingly, readers should be aware that certain content may have changed since the date of this publication. Please reach out to the author or your Willis Towers Watson contact for more information.

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