

# Financial Lines Market Update

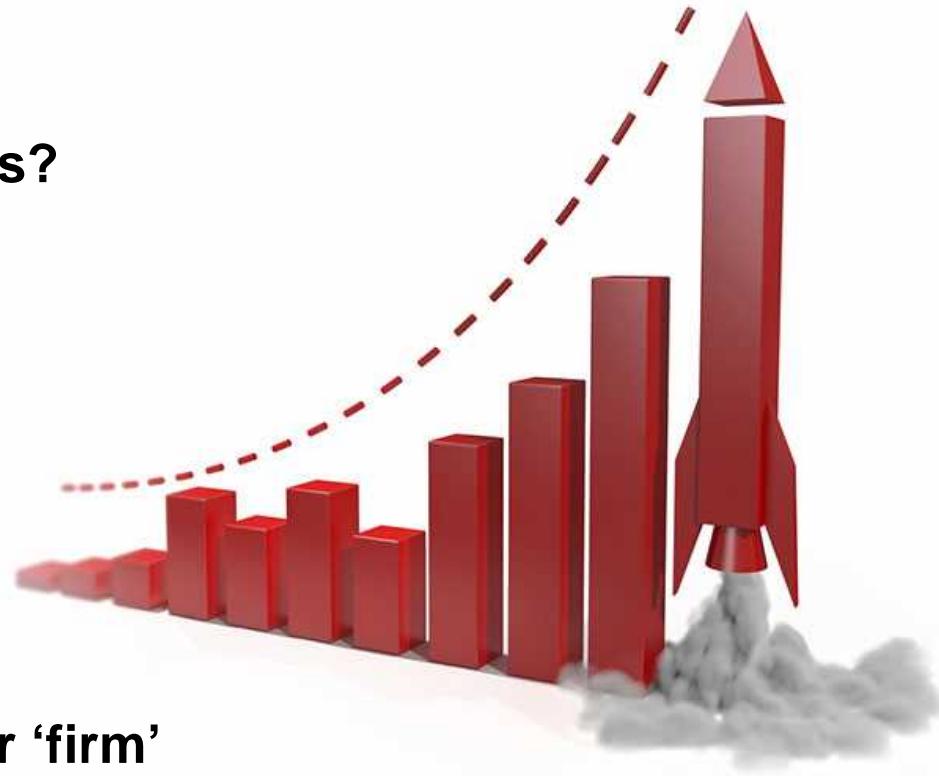


**Are we in the middle of a hard market?**

**Do we have capacity issues?**

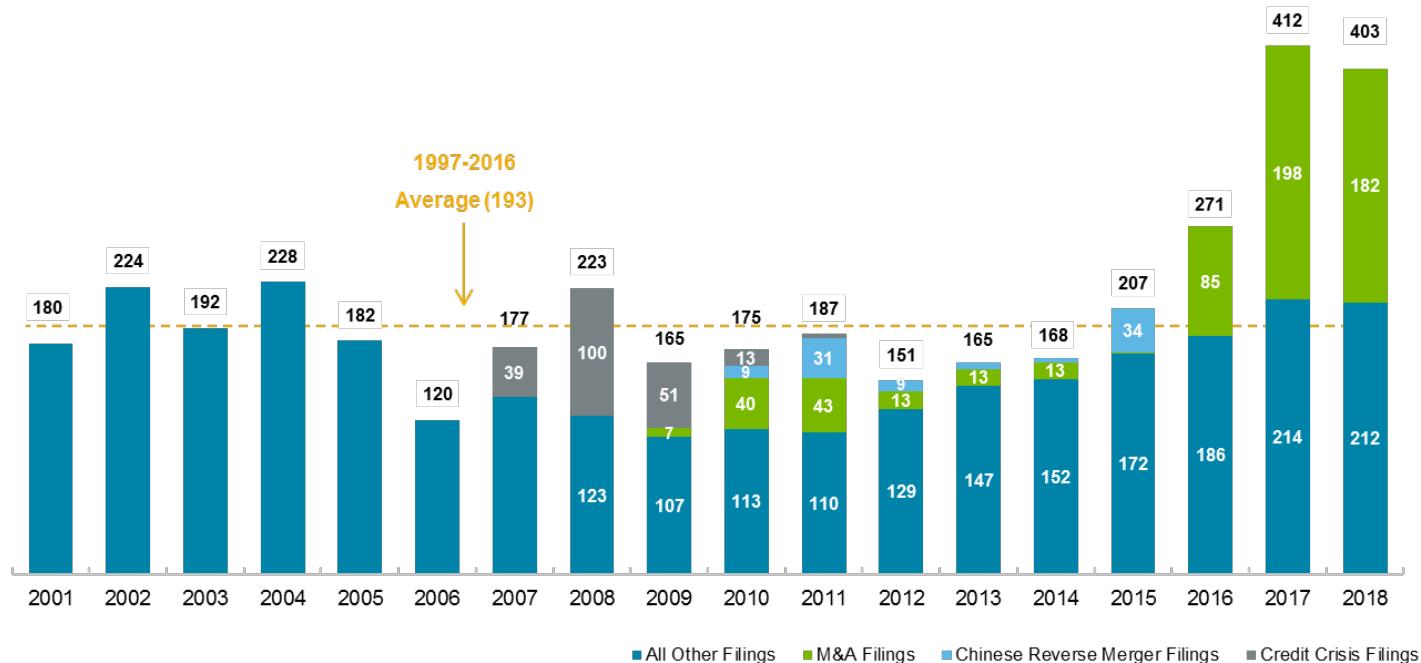
**How is the insurance company sector different from other sectors?**

**How long will this 'hard' or 'firm' market last?**



# Federal Securities Class Actions

- **SCAs:** 403 new SCAs 2018 (2% percent lower than 2017), nearly double the 1997–2017 average
  - U.S.-listed companies ~9% probability of SCA – historic high
  - Large cash settlements in derivative suits



## Note:

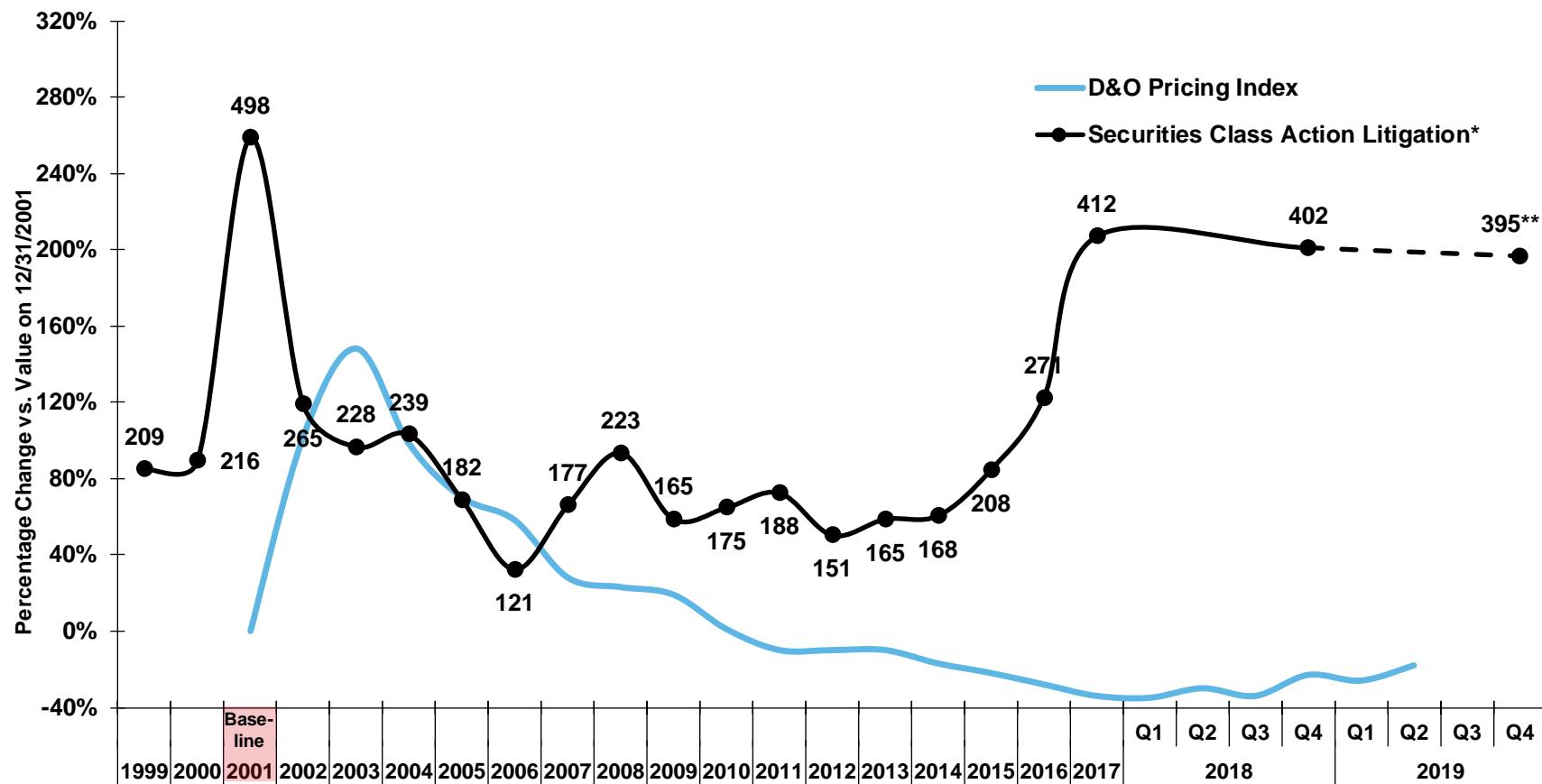
1. There were two cases in 2011 that were both an M&A filing and a Chinese reverse merger filing; these filings were classified as M&A filings in order to avoid double counting "Classic Filings" which exclude IPO Allocation (313), Analyst (68), and Mutual Fund (25) filings.
2. 2007 was the first year that this report began separately identifying these filings

Source: Stanford Securities Class Action Clearinghouse - Securities Class Action Filings – 2018 Year in Review

# Claims Frequency vs. D&O Pricing

## Claims Frequency vs. D&O Pricing

Q1 2002 – Q2 2019 | Base year: 2001 = 1.00



\* Stanford Law School's Securities Class Action Clearinghouse as of September 3, 2019. These totals include IPO Allocation, Analyst, and Mutual Fund filings.

\*\* Projected annual filings based on trailing twelve-month totals.

# 2019 D&O Market Snapshot

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- **Event-driven litigation**
  - Cyber-related like Equifax, Yahoo!
  - EPL-related - “Me Too” movement like Fox and Wynn
- **Defense costs are rising;** attorney rates are increasing significantly
- **International marketplace: much higher frequency and severity**
  - High profile non-U.S. traded companies (bribery and corruption scandals)
  - Rising securities class actions in Asia (many of which are insured in London)
  - Filings against non-U.S. domiciled but U.S. traded companies

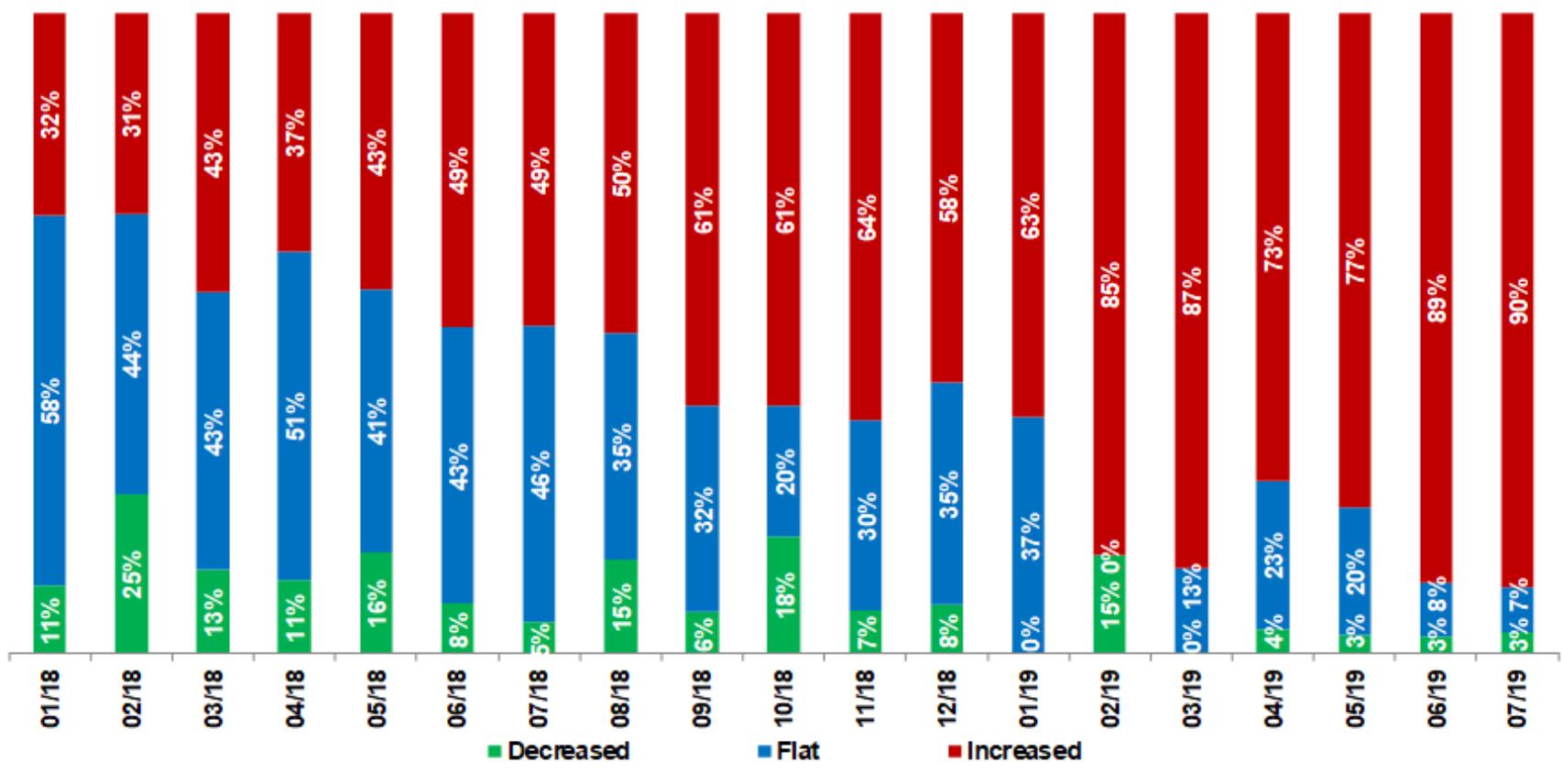
## General Response by Carriers

- Insurers are responding: increased retentions and pricing, reduced capacity
- Excess insurers are also pushing for pricing increases, sometimes greater than the primary
- Some insurers are scrutinizing their overall D&O portfolio and evaluating adjustments

# Primary D&O Pricing – All Industries

## Monthly D&O Pricing Changes

Percentage of clients with Decreases – Flat – Increases (Primary Layers Only – Same Clients/Limits/Deductibles)

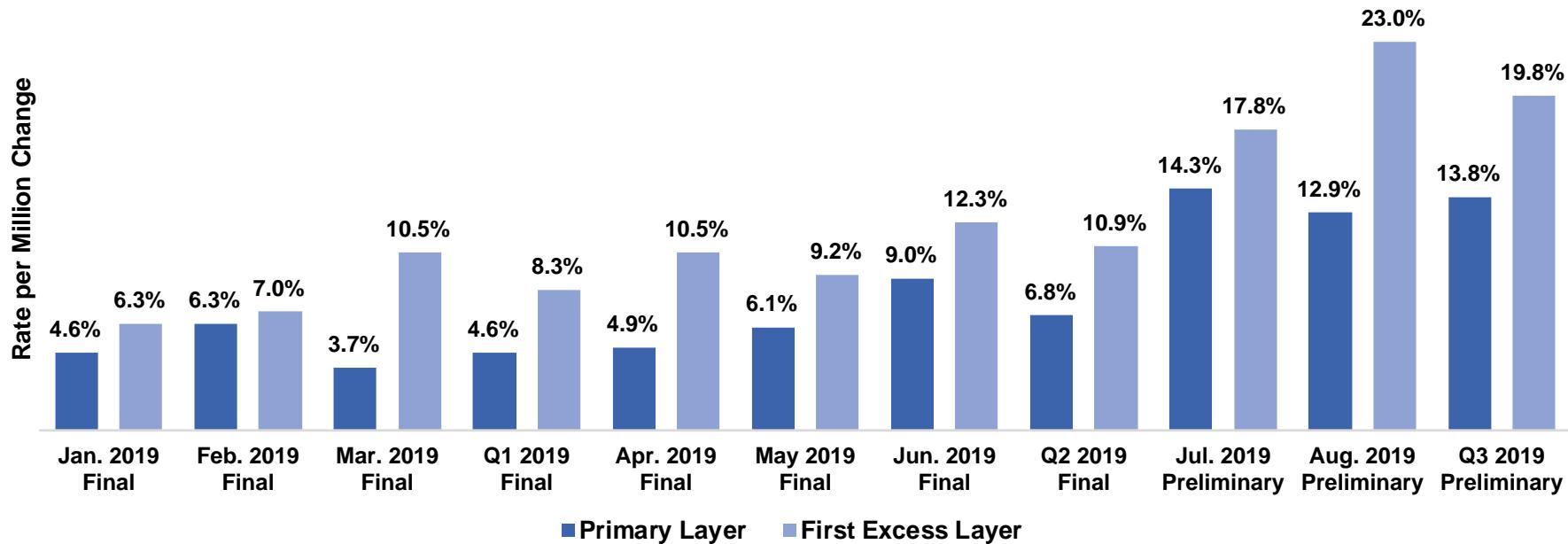


Source: Aon FSG Quarterly D&O Pricing Index

# Primary vs. Excess Pricing – D&O

## “Real Time” Primary and First Excess Layer Pricing

Average rate per million change (Same Clients/Same Limits/Same Retention or Attachment Points)



Data as of September 3, 2019

Source: Aon FSG Quarterly D&O Pricing Index

## Generally speaking...

- **Pricing** – not as ‘hard’ as in the public D&O sector
  - Most of our renewals fall in the **+1% to +10% range**
  - Still **plenty of competition**
  - Not experiencing the ‘inversion’ between primary and excess layers
  - Other lines – stable, but underwriters paying more attention to underwriting factors, such as headcount, AUM, GWP, jurisdictions, insurance lines, etc.
- **Retentions** – very few adjustments
  - Most taking place in lines such as **ICPL**
  - 2 or 3 carriers pushing more aggressively
- **Capacity** – **plentiful**
  - But carriers are getting more picky
  - For accounts with claims, other issues, carriers reacting more violently
- **Terms & Conditions** – **stable**
  - Not seeing a contraction
  - Some adjustments on the ICPL side when needed

## Generally speaking...

- **Pricing** – *can be more flexible* than some US carriers
  - Mostly excess placements
  - Some asking for 'rate adequacy adjustments', but mostly following
- **Capacity** – *plentiful*
  - New entrant – Everest Bda – Kyle Adams and Mike Dickinson – no writings up-to-this point
- **Terms & Conditions** – *innovation*
  - State-of-the-art DIC products
  - Wage & Hour
  - CAT5
  - CISO
  - Etc.

- **General – *hard market conditions***

- Isolated pockets of hardening in specific classes, geographies and industries has developed into more general hard market conditions
- Rate increases, constriction of capacity, resistance to broadening of coverage

- **Attachment points – *more focus on 'real rate' than 'ILF'***

- Some primaries have exited specific classes, focus on premium
- Some excess not following what primaries or lower layers are doing
- Focus on capacity management, managing cat exposure per risk

- **Problem areas**

- Australia
- US - ~9% probability of SCA
- IPOs
- Toshiba ruling – do US securities laws apply to unsponsored ADRs?

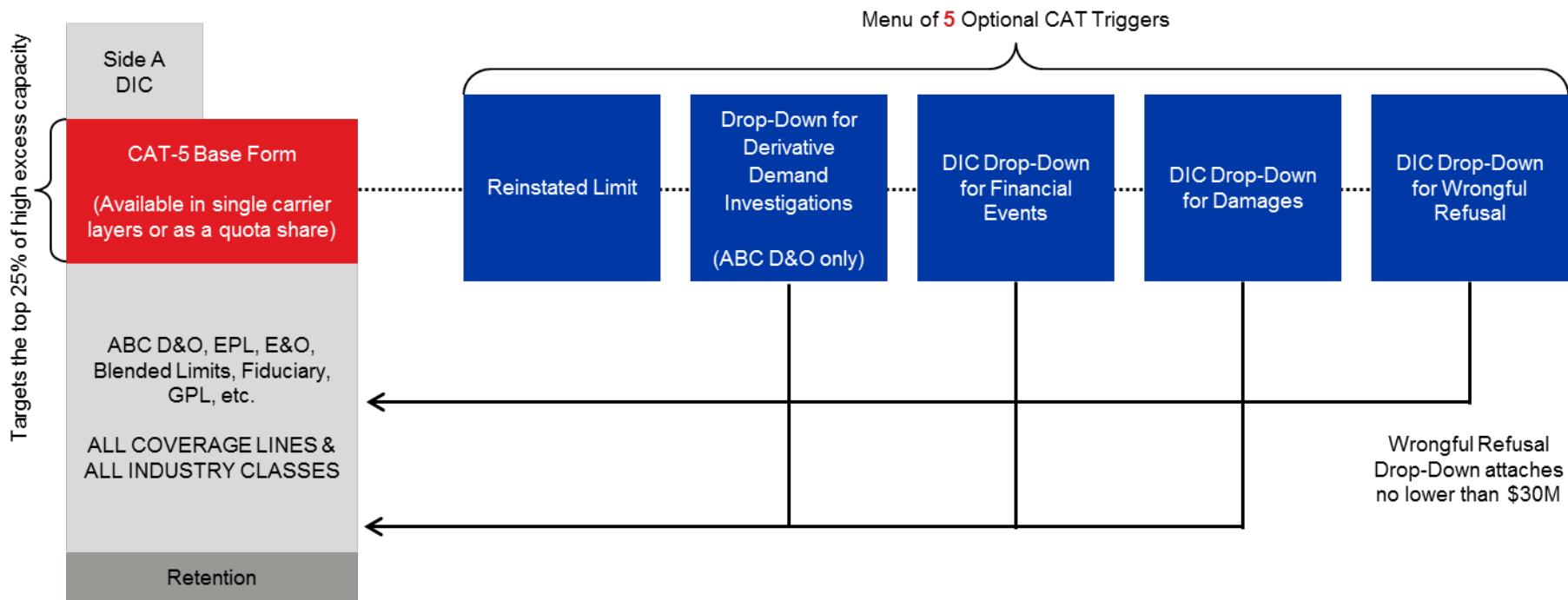
# London

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| Client | 2018 Primary limit | 2018 retention | 2018 pricing |  | 2019 Primary limit | 2019 retention | 2019 pricing | Change Rate/MM |
|--------|--------------------|----------------|--------------|--|--------------------|----------------|--------------|----------------|
| 1.     | \$15M              | \$5M           | \$370,000    |  | \$10M              | \$10M          | \$525,000    | 113%           |
| 2.     | \$10M              | \$1M           | \$199,500    |  | \$10M              | \$5M           | \$425,500    | 113%           |
| 3.     | \$10M              | \$5M           | \$495,000    |  | \$10M              | \$5M           | \$544,500    | 10%            |
| 4.     | \$10M              | \$1M           | \$85,000     |  | \$5M               | \$1M           | \$76,680     | 80%            |
| 5.     | \$15M              | \$5M           | \$410,000    |  | \$10M              | \$5M           | \$325,000    | 19%            |
| 6.     | \$10M              | \$1.75M        | \$420,000    |  | \$10M              | \$5M           | \$1,150,000  | 174%           |
| 7.     | \$20M              | \$7.5M         | \$847,676    |  | \$20M              | \$7.5M         | \$911,252    | 8%             |
| 8.     | \$10M              | \$750K         | \$129,000    |  | \$10M              | \$1.5M         | \$150,000    | 16%            |
| 9.     | \$10M              | \$1M           | \$180,000    |  | \$10M              | \$2.5M         | \$262,500    | 46%            |
| 10.    | \$15M              | \$1M           | \$235,400    |  | \$10M              | \$2.5M         | \$425,000    | 171%           |

- **CAT-5**
- **Chief Information Security Officer**
- **London Aon A+ Protect**
- **Wage & Hour**

# D&O Product Innovation – CAT5



# D&O Product Innovation – Chief Information Security Officer

- 3/1/17 - NY State Department of Financial Services (DFS) - rigorous cybersecurity regulation intended to protect clients, consumers and financial entities
- Could expose financial institutions and their executives to liability from regulatory actions or plaintiff's.
- Small to midsize entities, in particular, may struggle to implement the required cyber security plans, risk assessments and response plans.
- Not limited to NY based entities, nor is it limited to financial institutions
- The Superintendent can bring enforcement actions and seek fines for violations
- Executives will have accountability: they will need to certify compliance with these new regulations annually
- Quick notification requirements: 72 hours

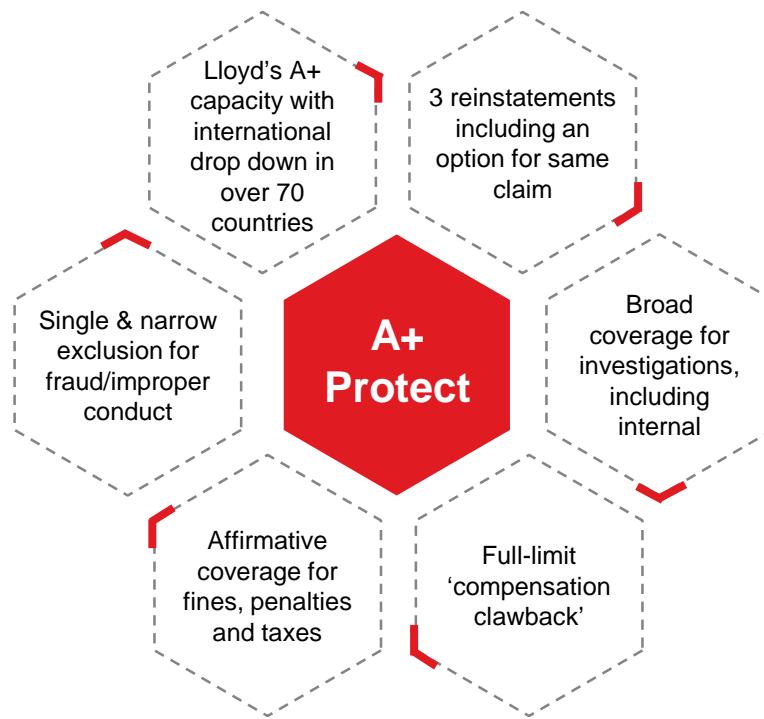
## Aon's Solution for CIOs

Via a lead Side A D&O policy as follows:

- Coverage for fines, penalties and monetary assessments imposed upon cybersecurity officers pursuant to any local, state, federal or foreign computer, technology, information assets, data or network system related contract, tort, law, rule, regulation, ordinance or legal requirement
  - Including New York State DFS
- Broad insurability provision. Insurers may not challenge an insurability opinion presented by insured's counsel.
- Responds in the event the officer is not indemnified by the company
- Includes the advancement of defense costs
- Nil deductible

# D&O Product Innovation – A+ Protect

| \$200M                                      |
|---|
| Participating Lloyd's of London syndicates: |
| Beazley                                     |
| Hiscox                                      |
| Barbican                                    |
| Brit  |
| Chubb                                       |
| CV Starr                                    |
| Navigators                                  |
| W. R. Berkley                               |
| Aon Client Treaty                           |



**W&H is designed to provide employers with insurance protection for claims by:**

- Employees
- Leased Employees, Independent Contractors
- Department of Labor

**Covered claims include the following:**

- Misclassification:
  - *Employee v. Independent Contractor*
  - *Exempt v. Nonexempt*
- Meal and rest break violations
- Regular rate claims
- Failure to timely pay wages upon termination
- Failure to pay wages for off-the-clock work
- Donning and doffing claims
- Compliance with pay stubs
- Tip credit issues

## WHAT CONSTITUTES A CLAIM – REVIEW YOUR POLICY LANGUAGE

- Generally – “Receipt by the Insured of a written demand naming the Insured seeking Damages, Professional Services, or equitable relief arising out of a Wrongful Act by the Insured or any Entity for whom the Insured is legally liable”
- Is your definition too broad? Too narrow? How do you want your policy to be triggered
- Do you have a mechanism in place to capture these incidents?
- Once you capture them, how do you report them?
- Late reporting is our biggest concern

## WHEN SHOULD NOTICE BE GIVEN – REVIEW YOUR POLICY LANGUAGE

- Wording usually does not match internal escalation/notice process
- Post-policy reporting period (60 to 90 days)
- Control Group language
- Threshold amounts
- Bordereau reporting
- Non-prejudice language

Many States Prohibit Punitive Damage Insurance Coverage by Statute or Common Law

## PUNITIVE DAMAGES EXPOSURES

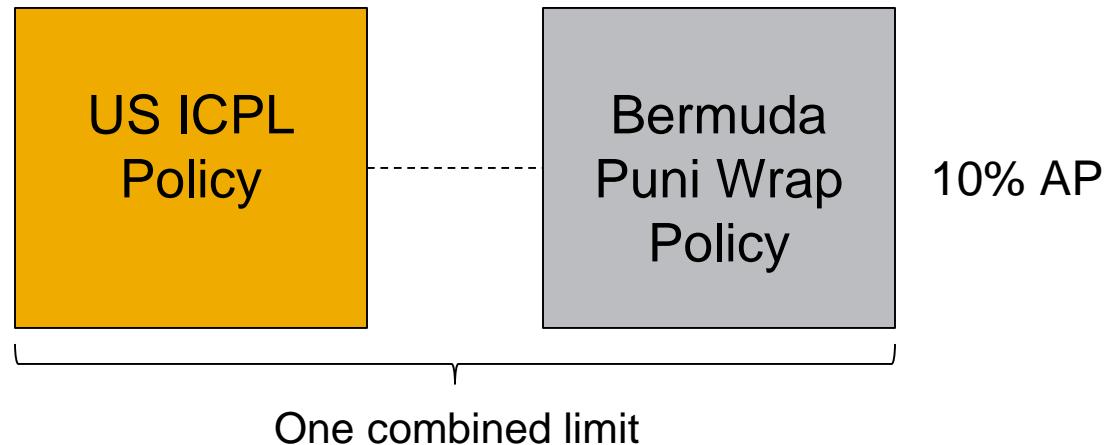
- *Lanwood Medical Center, Inc., v. Sadow, M.D.*, 43 So.3d 710 (Fla. 4<sup>th</sup> DCA 2010)(Punitive damages award of \$5 million)
- *Young v. Becker & Poliakoff*, 88 So.3d 1002 (Fla. 4<sup>th</sup> DCA 2012) (\$2 million punitive damages award)
- *James v. Horace Mann, Ins. Co.*, 638 S.E.2d 667 (SC 2006) –(\$1 million dollar punitive damages award)



**Punitive Damages Wraps could provide a solution for coverage**

## ○ Punitive Damages Awards

- ✓ Not insurable in many states – for example: ***Florida***
- ✓ Potential Solutions:
  - ❖ *Punitive Wrap*



# E&O Issues and Concerns

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| Insurer      | Punitive Wrap | Intentional Act | Company             |
|--------------|---------------|-----------------|---------------------|
| AXIS         | Yes           | Yes             | AXIS Specialty LTD. |
| Arch         | Yes           | Yes             | Arch Bermuda        |
| Beazley UK   | Yes           | Yes             | Aria London         |
| Beazley U.S. | Yes           | Yes             | Aria London         |
| AIG          | Yes           | Yes             | AIG Excess LTD      |
| Chubb        | Yes           | Yes             | Chubb Atlantic      |
| CNA          | Yes           | Yes             | CNA Bermuda         |
| Lexington    | Yes           | Yes             | AIG Excess LTD      |
| Zurich       | Yes           | Yes             | Hanseatic           |
| Berkshire    | Yes           | Yes             | Bunker Hill         |

# E&O Issues and Concerns

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## 1. ICPL Primary to Reinsurance



- Typical arrangement, ICPL responds primary over deductible
- Insulates reinsurance treaty from full effect of shock loss
- ECO/XPL can infill ICPL deductible

## 2. ICPL Excess of Reinsurance



- Reinsurance responds to primary – Exposed to shock loss
- Reduces ICPL costs as much as 50%
- ICPL can DIC non claims handling exposures

## 3. Reinsurance – NO ICPL



- Reinsurance responds primary – No ICPL
- 90/10 ECO/XPL quota share more common
- Coverage tied to claims handling only

# Key Renewal Considerations

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- **Start your renewals early**
- **Meet/talk to your underwriters – tell your story – don't just rely on applications**
- **Client/broker planning**
  - Discuss latest coverage developments
  - Make sure your coverage matches your internal mechanisms
  - Even in a hard market, an 'as expiring' renewal is not a good renewal
- **Understand/explore your options, but understand that this is a small market and relationships matter**
- **Understand that the market for insurance companies is not the same as the market for other industries. Specialization is important**

# Aon Cyber Risk Report – Predictions and Outcomes



## 1 Technology

Embracing Digital Transformation Creates New and Unanticipated Risks



## 2 Supply Chain

Supply chain security wake-up calls grow more insistent



## 3 IoT

IoT is everywhere, and it is creating more risks than companies realize



## 4 Business Operations

Technology for operational efficiencies can lead to security deficiencies that disrupt organizations



## 5 Employees

Excess privileges and shadow IT increase employee risk



## 6 Mergers & Acquisitions

Vulnerabilities from deal targets increases as dramatically as M&A value



## 7 Regulatory

Managing the intersection of cyber security policy and enforcement



## 8 Board of Directors

Directors and Officers face growing personal liability relative to cyber security oversight

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# Regulatory Scrutiny is Heating Up

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16

Material loss disclosures from public companies as a result of a cyber event

10

Derivative or securities claims brought as a result of a cyber loss

\$140M+

Losses to date resulting from those suits

These numbers are constantly changing

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## Significant Events

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SME /  
Middle Market

Enterprise /  
Large Cap

**Competitive pricing.  
Broadening Coverage.  
Losses Accruing.**

- Profitable space for most Insurers with robust Cyber Insurance Offerings
- Market competition causes insurers to chase new coverage offerings – i.e. theft of funds / social engineering, broad business interruption / extra expense, etc.
- Losses, due to ransomware activity, will mount throughout 2019

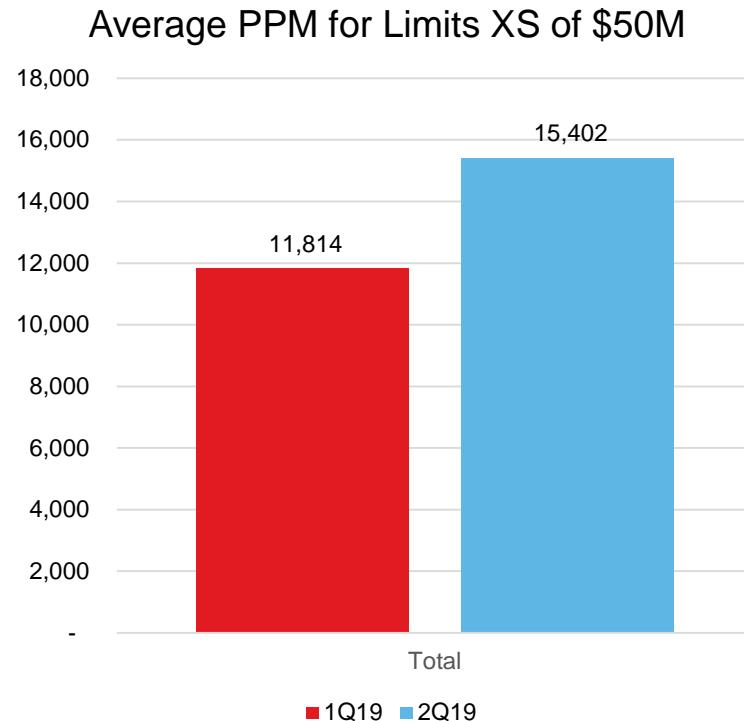
**Firming pricing.  
Broadening Coverage.  
Loss Trends Changing.**

- Pricing is starting to firm, particularly in the large market cap segment
- Coverage continues to be stretched, the market is offering a more holistic enterprise risk solution than a data breach solution
- Losses are viewed more often as binary by insurers – expect firming price environment in excess market

***Insurance Companies tend to face less scrutiny than other Industry Segments***

# Excess Pricing

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- Large Data Breaches trigger “Binary Losses”
- Minimum Excess Price Points (\$5,000 per million are not sustainable)
- Two Potential Scenarios:
  1. Market Correction
  2. Lost Capacity

## 2020 Cyber Predictions

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- Pricing will firm, quickly, in the excess marketplace
- Key coverage “Grey Areas” will gain clarity
- Losses will continue to mount
- Tackling cyber risk will continue to be everlasting