August 2020

Client Alert

Private Company and Nonprofit Organization Exposures and Trends

Premium increases are making upward pricing adjustments across multiple management liability lines

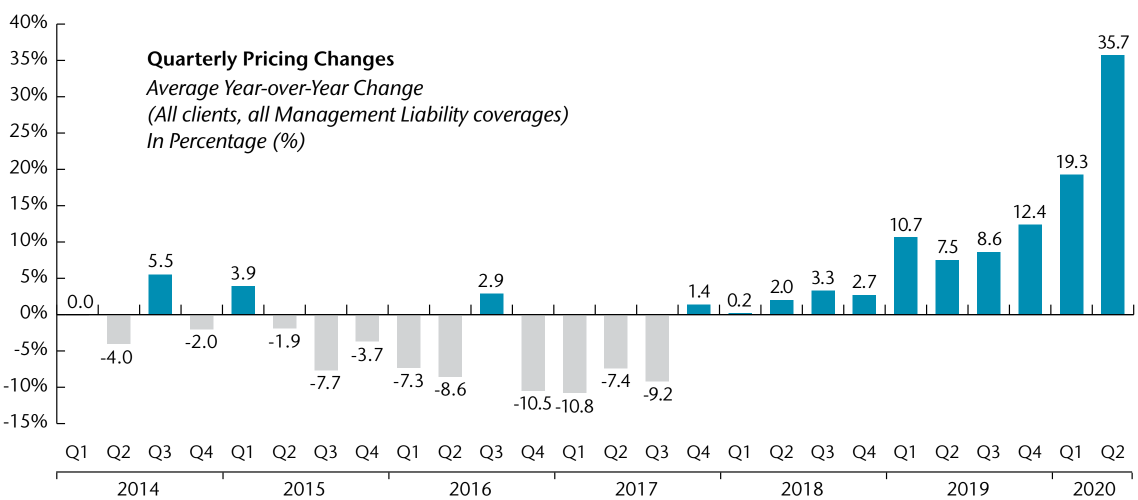
In the first half of 2020, Management Liability rates for Private and Nonprofit clients escalated across all industry sectors. Premium increases accelerated in the second quarter as insurers generally made upward pricing adjustments across multiple Management Liability lines, including Directors' & Officers' Liability ("D&O"), Employment Practices Liability ("EPL"), Fiduciary Liability, and Crime.

Quarterly pricing changes

As Aon's Private and Nonprofit Pricing Index in the chart below displays, the quarterly pricing change for the second quarter is 35.7%, largely driven by D&O, as compared to the same quarter in 2019.

When compared to the first quarter year-over-year increase of 19.3%, the pricing surge in the last quarter is even more pronounced. Additionally, the second quarter year-to-date index reflects an overall year-over-year price increase of 23.6% for all Management Liability lines combined.

Private/Nonprofit Pricing Change



Source: Aon Financial Services Group, Private and Nonprofit Pricing Index

Programs with excess towers also are subject to higher rate increases as insurers are re-evaluating cost for excess capacity and increasing their rate as a percentage of underlying premium. Clients in higher risk industries such as retail, hospitality, healthcare, energy, entertainment (including athletic organizations), media, and higher education, as well as risks with unfavorable loss history, are at the higher range or above the average reflected in the pricing index. As an example, we have seen second quarter year-over-year premium increases of 41.3% in retail and 78.1% in hospitality across all Management Liability lines. In some cases, individual accounts may experience price increases in the triple digits.

Exposures are heightened across multiple Management Liability lines

The impact of the COVID-19 pandemic has compounded insurers' concerns amid numerous exposures across several Management Liability lines of insurance. Unrelated to the pandemic, D&O insurers continue to underwrite risk as it relates to claims that

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may be brought against the organization including anti-trust, privacy, False Claims Act, breach of contract and false advertising, as well as the more traditional bankruptcy, merger and acquisition, and regulatory exposures. Additionally, due to the economic downturn stemming from COVID-19, insurers are extremely concerned with financial impairment and as such are scrutinizing liquidity & debt obligations, inquiring as to receipt of Paycheck Protection Program ("PPP") funds, and seeking to gauge the potential impact of these factors on future operations. Many insurers now require quarterly, in addition to annual, financial statements and ask detailed questions relating to COVID-19, which often are addressed in calls with the insurers.

EPL and Fiduciary Liability in a volatile market

The EPL concerns related to COVID-19, which come on the heels of #MeToo, rising claim costs and employee biometric privacy litigation, are focused in the short term on claims that may stem from workforce layoffs, furloughs and other staff reductions, and employment-related privacy claims tied to the virus. Longer term, insurers are evaluating return to work procedures, accommodation protocols, anti-retaliation policies and training, as well as the impact of the economic contraction on the workforce, as higher unemployment figures often translate to an uptick in claim frequency. Additionally, unrelated to COVID-19, the potential of an even more divisive workplace because of the recent race-related social unrest is an increasing insurer consideration. We expect to see more underwriting questions on this topic.

Fiduciary Liability is not immune to additional COVID-19 exposure, as insurers have expressed concerns regarding CARES Act mandates, staffing to meet administrative burdens, and the potential for employee layoffs to trigger partial plan terminations. Insurers consequently are seeking more underwriting information. With the emergence of these exposures stemming from the COVID-19 pandemic, on top of existing challenges in connection with the expansion of excessive fee litigation, Fiduciary Liability insurance placements will garner more attention among the suite of Management Liability insurance policies than in prior years.

Insurance marketplace update

The marketplace, not surprisingly, is dynamic as the COVID-19 pandemic trends fluctuate, and ambiguity is constant. In addition to pricing changes, insurers are continuing to appraise capacity, retentions and coverage across all Management Liability lines. Access to the Management Liability suite of products remains relatively stable, however, insurers are reducing primary and excess limits in some cases as they seek to contain aggregate loss potential over multiple policies and total exposure to financial impairment claims. Total capacity is generally available, but expect to see compression of limits (to accompany the rising premium rates), requiring an introduction to new markets and likely resulting in more participants on a program.

As clients review the adequacy of Management Liability insurance limits, peer group purchasing data is just one determinant of adequacy. Consideration of external factors including industry risk factors, legislative and regulatory environment, jurisdictional trends, and the insurance market cycle (coupled with internal issues such as financial condition, merger & acquisition activity, governance, ownership and company risk retention appetite) are essential to assess. Despite rising premiums and constrained insurance budgets, in the current economic environment and amidst escalating litigation trends, it is even more important than ever to closely evaluate limit adequacy. Private and Nonprofit clients are increasingly considering the benefits of additional Side-A D&O limits to help protect their individual directors and officers from non-indemnifiable claims.

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About Aon's Financial Services Group

Aon's Financial Services Group (FSG) is the premier team of executive liability brokerage professionals, with extensive experience in representing buyers of complex insurance products including Directors' and Officers' Liability, Employment Practices Liability, Fiduciary Liability, Fidelity and Professional Liability insurance. FSG's global platform assists clients in addressing their executive liability exposures across their worldwide operations. Aon's Financial Services Group manages approximately $2.9 billion in annual premiums, assists with average annual claim settlements of approximately $700 million, and uses its unmatched data to support the diverse business goals of its clients.

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Retention and coverage trends

Retentions have been increasing over the past year in pockets and are expected to continue. We expect that D&O retentions for securities claims, Fiduciary Liability excessive fee retentions, and California EPL retentions will all experience upward pressure from insurers. Clients with changes in exposure or unfavorable loss history may see continued retention increases and companies with significant reductions in workforce are likely to be subject to higher EPL retentions.

Broad coverage remains available for many clients though Aon's Private & Nonprofit Insurer Panel, however, insurers are increasingly adding specific exclusions relative to the entity coverage provided. For larger clients with over $1 billion in revenue, a few insurers are removing non-securities claim D&O entity coverage as they view them akin to public accounts and insist the premiums are not keeping pace with entity losses. Entity coverage, however, still remains generally available and is a critical component of Private and Nonprofit programs. Management Liability areas garnering attention of insurers and resulting in some narrowing of coverage include but are not limited to: Anti-trust (coinsurance or exclusion), Governmental Funding (sublimit, co-insurance or exclusion), as well as potential exclusions for Bankruptcy/Creditors, Intellectual Property, Employee Biometric Data, Network/Cyber Security (specific exclusions on non-cyber policies), Products Liability, Professional Services, Regulatory and Sexual Misconduct. Automatic extensions for extended reporting periods and pre-determined run-off may also be restricted.

Aon's dedicated team can assist in navigating the changing marketplace

As insurers introduce coverage limitations or programs move to new insurers, inspection of the policy wording and impact of the changes relative to each clients' risk profile is key. While insurers may be increasingly excluding biometric privacy claims from EPL, if clients do not collect or plan to collect such information, the impact is negligible. However, how carriers address financial impairment under the D&O policy universally requires close examination. Clients should work closely with their broker to identify how coverage changes specifically impact their organizations' exposure.

Leading Private and Nonprofit insurers, including Aon's Private & Nonprofit Insurer Panel, remain open for new business; however, submission requirements are more robust. Be prepared to discuss Management Liability insurance objectives and set renewal strategies early, provide as much up-to-date financial information as possible, and expect additional questionnaires to supplement the renewal application. Anticipate additional questions specific to COVID-19 and discuss with your broker whether a call is appropriate with insurers to relay your organizations' story. As the Management Liability marketplace continues to transform rapidly, Aon is uniquely positioned with our Private and Nonprofit team with dedicated brokerage experience and market knowledge to assist clients in navigating the marketplace.