D&O Liability:
A Start-up's Perspective

Athula Alwis

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Agenda

- **Introduction**

- **Trends**

- **Data**

- **Modeling**

- **Start-up Company View**

- **Reinsurer View**

- **Q & A**

Introduction

- *Excellent opportunity to enter a large market at a point of significant change*

- *A very strong parent with a solid capital base*

- *A+ paper*

- *A very experienced team*

Introduction

- ***Philosophy of writing high excess and A – side business***

- ***Management of limits***

- ***High quality accounts***

- ***Industry diversification***

- ***Good opportunities in a stressed market***

Trends

- *A wave of SCA law suits due to financial crisis*

- *Recent settlements*

- *Overall frequencies up again to historical averages*

- *2006 seems like an anomaly*

Trends

- *D&O is a cyclical financial product*

- *It is difficult to apply traditional actuarial methods based on past history*

- *Start-up companies do not own historical data any way*

Trends

- *Change in market cap (stock price) as a proxy*

- *Credit ratings*

- *Institutional investors, liquidity, M&A and IPO activity*

Data

Three key elements to consider when reserving D&O losses

- **Data**

- **Contagion Risk**

- **Systemic Risk**

Data

Data

- **Historical data for traditional SCAs (Securities Class Actions) available through commercial vendors**

- **Requires scrubbing and cleansing**

- **Manual work**

Data

Data

- **Use more than one vendor**

- **Regular updates**

- *Differentiate data based on appetite (ex. ADRs)*

Modeling

Contagion Risk

- **Institutions connected through one or more parameters deteriorating at the same time**

- **Mutual fund cases**

- **Analysts cases**

- **Asian debt crisis**

Source: Reuters

Modeling

Systemic Risk

- **The movement of the entire market in a downward cycle**

- **Current financial crisis**

- **Interest rates**

- **Unemployment**

- **National home prices**

Source: Wikimedia Commons

Modeling

Exposure Based Modeling

- **Market Cap**

- **Change in market Cap**

- **Assets**

- **Revenue**

Source: GETTY

Modeling

Parameters for reserving

- **Market Cap loss during class period**
  - **Plaintiff friendly**
  - **Carrier friendly**

- **Maximum dollar loss**

- **Bounce back effect**

- **Stock price movement compared to sector movement**

Modeling

Predictive Modeling

- **Stock price movement**

- **Option pricing**
  - *D&O contract as a put option protecting shareholder value*

- *Debt markets*

Start-up View

- **Pick a loss ratio based on UW experience, judgment ,and intuition**

- **Historical loss ratios of similar companies**

- **Adjustments for market trends, contagion risk and systemic risk**

- **Risk appetite (primary vs. excess, ABC vs. A-side, …)**

- **Loss ratio indication based on a holistic view**

Reinsurer View

- **Pick a loss ratio based on UW experience, judgment and intuition**

- **Portfolio assessment (including contagion risk and systemic risk)**

- **Market indicators**

- **Expected loss ratio based on market cycle (as opposed to 3 to 5 previous years)**

- **Loss ratio indication based on a holistic view**

Questions

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