



# Seminar on Loss Reserving

Online Event  
September 15-17, 2020



# Directors' & Officers' Liability The Evolving Landscape

September 15-17, 2020



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# Meet the Speakers

## Rick Ramotar, FCAS

VP, Swiss Re

Rick is a VP and Senior Actuary at Swiss Re with expertise in Professional Lines insurance pricing. He has been with Swiss Re for 5 years.

Rick has more than 20 years of actuarial experience dealing with a variety of lines of businesses. Rick has had with prior roles at Hiscox, the PMI Group, Aon, Trans Re, and Farmers.

Rick holds a BS in Statistics from UC Santa Barbara.

## Dave Moore, FCAS

President, Moore Actuarial Consulting, LLC

Moore Actuarial Consulting, LLC provides actuarial consulting and ERM services for commercial and specialty lines of insurance.

Dave has over 25 years of actuarial experience. His areas of focus include: Executive & Professional Liability, Warranty & Extended Service contracts and standard commercial lines.

He presently serves as the Chair of the CAS Risk Management Committee.



# Agenda

- Types of D&O products
- Market since the Great Financial Crisis
- 2019 market inflection pre-COVID
- COVID-19 Related Cases
- Settlement Severity
- Shareholder Derivative Lawsuits
- Reserving considerations

# Question #1

On a scale of 1-5, what is your experience level with D&O?

1 – none

2

3

4

5 – very experienced



## Question #2

Do you currently work on D&O?

No

Yes



# Directors & Officers – Key Features

- Claims-Made business
- ALAE included in the limit
- Claim must have a triggering event
  - Stock price falling is not enough to be a trigger event





# Directors & Officers Coverages

- Side A – Non-Indemnifiable Coverage
  - Provides direct coverage for D&O's in cases where company cannot indemnify
- Side B – Reimbursement Coverage
  - Covers losses where the company indemnifies the D&O's
- Side C – Entity Coverage
  - Provides Entity Coverage which protects the corporation
- Related Coverages
  - Employment Practice Liability Insurance (EPLI)
    - Provides protection against employee lawsuits including harassment
  - Crime
  - Fiduciary



# Directors & Officers Liability

- Not just one type of product
- Public D&O
  - Financial Institutions (FI) D&O
  - Non-FI D&O aka Commercial D&O
  - Side A
    - Covers D&O's for non-indemnifiable claims ie Bankruptcy or Derivative claims
- Private/Not-for-Profit D&O

Over time these segments tend to move directionally in similar ways but magnitude and timing can differ

# Historical Rate Change (Pre-2019)

- Since the Financial Crisis ('07-'09), rates have generally been falling
- Double digit decreases for non-FI D&O
- FI D&O rates have fallen but annual decrease tended to be single digits
  - Had started to flatten out
- Side A rates have fallen but product has remained profitable due to healthy stock market and lack of bankruptcies
  - but uptick in large derivative claims
- Private/PNP – mixed bag but generally down

# Rate Inflection (2019)

- Initial estimates were flat to single digit increases
- Actual Rate Movements
  - Non-FI: 20-30%
    - Much higher for Excess Layers vs Primary Layers
  - FI: 5-15%
    - FI Rates > Non-FI Rates
    - Historical decreases not as great
  - Side A: 5-10%
  - Private/PNP: 2.5%-10%
- Rates during 2019 trended upward during the year
  - Q4 >>> Q1

# What Happened in 2019

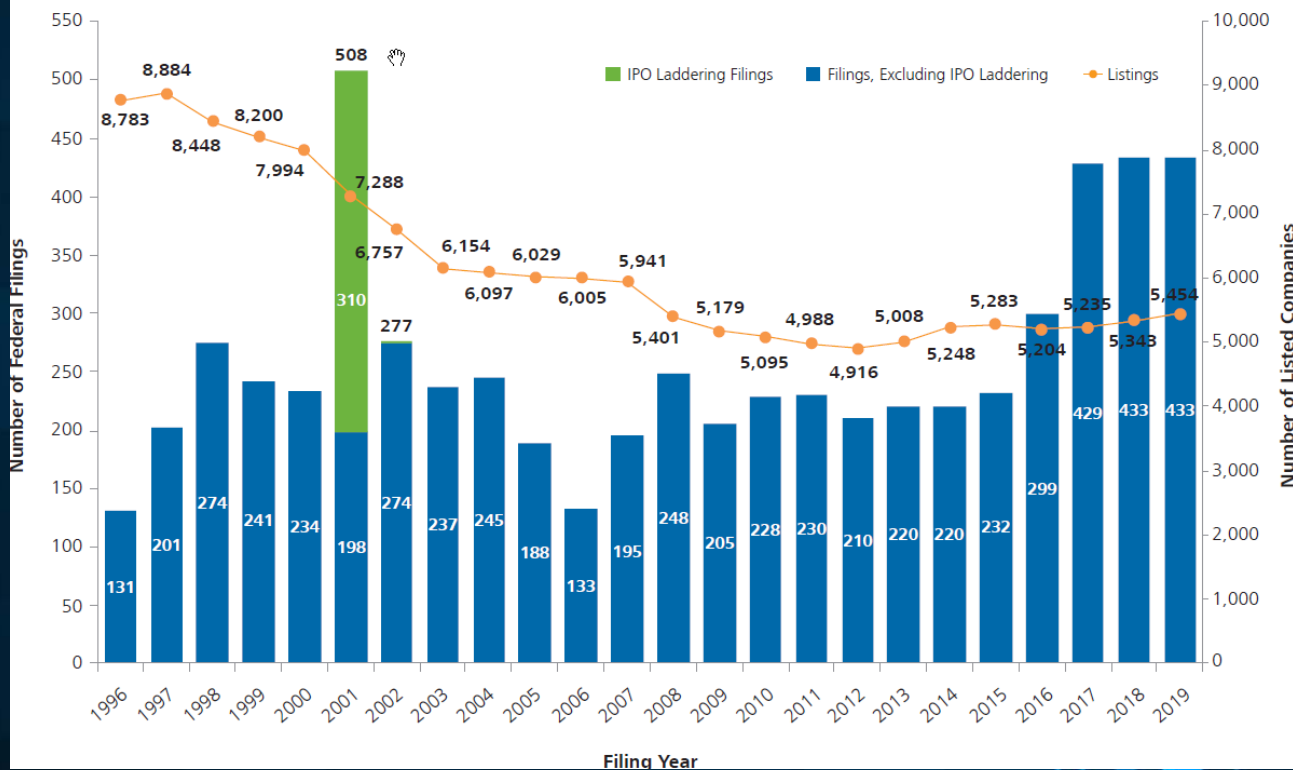
- Concerns about Profitability
- Concerns about trend and emerging risk
  - Increase in Security Class Actions
  - D&O is claims-made business with expenses within the limit so can react to concerns before seeing emerging losses
- Limit retraction
  - Large towers are placed in D&O
  - Insurers pulled back from offering layers of 15m and above on excess layers
    - Typical excess Layers max Limits offered in 2019 in 5-10m range
- Increasing Retentions

# Limit Retraction

- D&O has large with many insurers taking different tranches throughout the tower
  - Some of these tranches can be 20m or even 50m
- As insurers pulled back on the limit they were putting out, layers had to be broken in smaller tranches and  $1 + 1 \neq 2$ 
  - In other words, the cost of a 20m layer tranche broken into four 5m limit pieces can be much greater than the original single layer
  - In other to place towers with layers cut into smaller piece, ILF curves flattened and increased on some segments
- For now, there is still ample capacity in the market

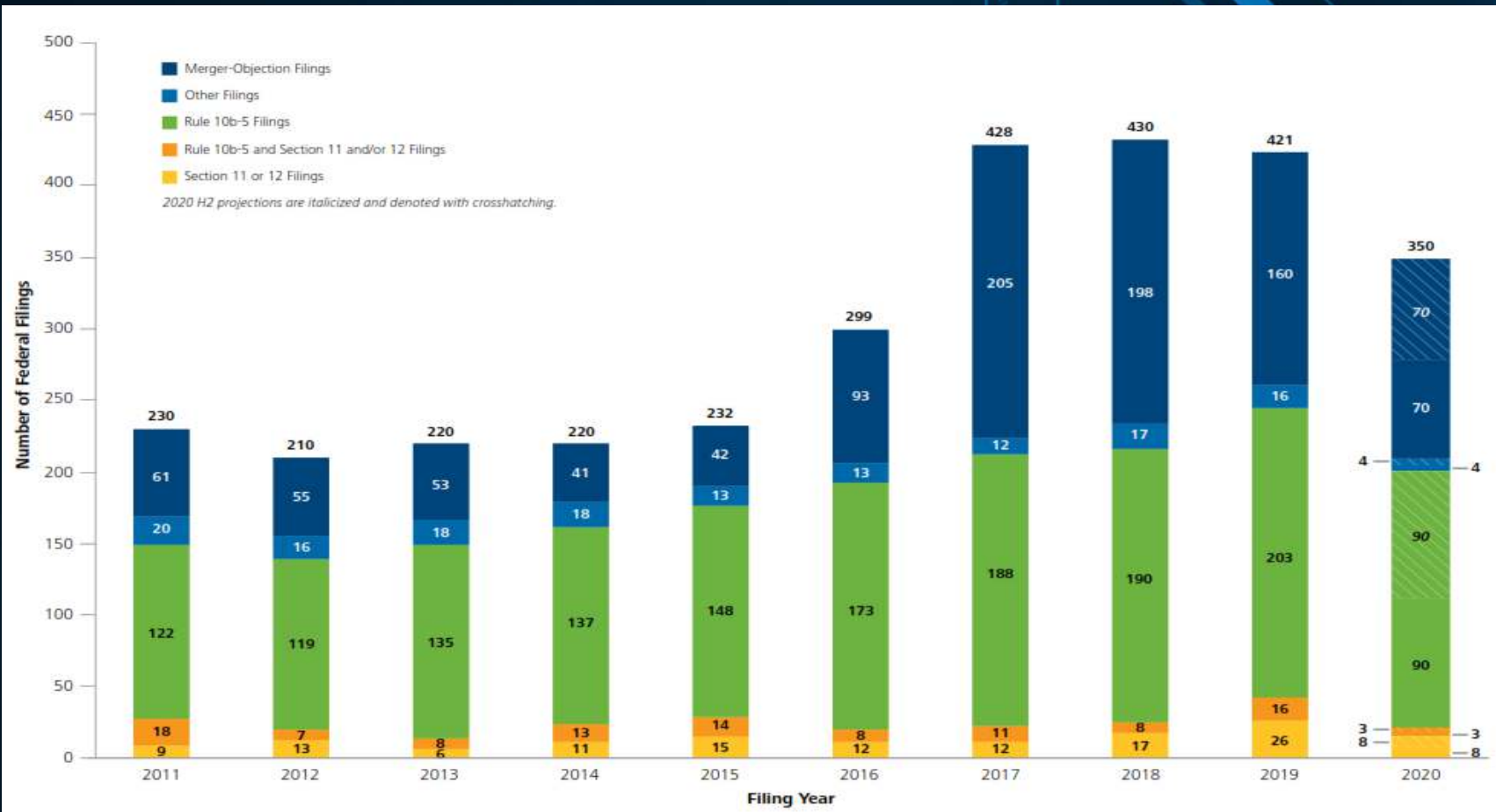
# Security Class Actions Claims

Figure 1. Federal Filings and Number of Companies Listed in the United States  
January 1996–December 2019



\*NERA Recent Trends in Securities Class Action Litigation: 2019  
Full-Year Review

# Federal Filings By Type – January 2011 – June 2020\*



\*NERA Recent Trends in Securities Class Action Litigation  
2020 H1 Update



# COVID-19 Lawsuit Filings

Company	Security Class Action Filing Date	Shareholder Derivative Filing Date
Norwegian Cruise Lines Holdings Ltd	3/12/2020	
Inovio Pharmaceuticals, Inc.	3/12/2020	4/20/2020
Zoom Video Communication, Inc.	4/7/2020	6/11/2020
iAnthus Capital Holdings Inc	4/20/2020	
Phoenix Tree Holdings Ltd	4/24/2020	
SCWorx Corp.	4/29/2020	6/15/2020
Elanco Animal Health Incorporated	5/20/2020	
Sorrento Therapeutics, Inc.	5/26/2020	
Carnival Corporation & Plc	5/27/2020	
Wells Fargo & Co	6/4/2020	
Forescout Technologies, Inc.	6/10/2020	
Co-Diagnostics Inc.	6/15/2020	
Chembio Diagnostics, Inc.	6/18/2020	
United States Oil Fund, LP	6/19/2020	
The GEO Group, Inc.	7/7/2020	
ProShares Ultra Bloomberg Crude Oil	7/28/2020	
Velocity Financial	7/29/2020	
Eastman Kodak Company	8/13/2020	
Vaxart	8/24/2020	

Sources: Advisen, The D&O Diary

Filing Counts in 2020 by Month

	SCAs	Derivatives
March	2	1
April	4	2
May	3	0
June	5	0
July	3	0
August	2	0
<b>Total</b>	<b>19</b>	<b>3</b>



# What is a Shareholder Derivative Lawsuit?

- A lawsuit brought by a shareholder on behalf of a company
- Often brought against a director or officer of the company
- If lawsuit is successful, proceeds go to the company
- According to Advisen, there are typically over 200 Shareholder Derivative suits against publicly traded companies per year

# Shareholder Derivative Lawsuit Allegations

- Self-dealing by corporate executives
- Mismanagement or waste of corporate assets
- Objections to certain transactions or governance practices
- Options backdating (~2006; numerous companies)
- Board racial diversity (e.g. Qualcomm, Facebook, Oracle, Lifelock, The Gap)
- Data breach (e.g. LabCorp, Yahoo, Wendy's, Home Depot)
- Opioid Crisis (e.g. McKesson)
- “Me too” (e.g. Google, Nike, 21<sup>st</sup> Century Fox)
- COVID-19

Sources: Advisen, The D&O Diary

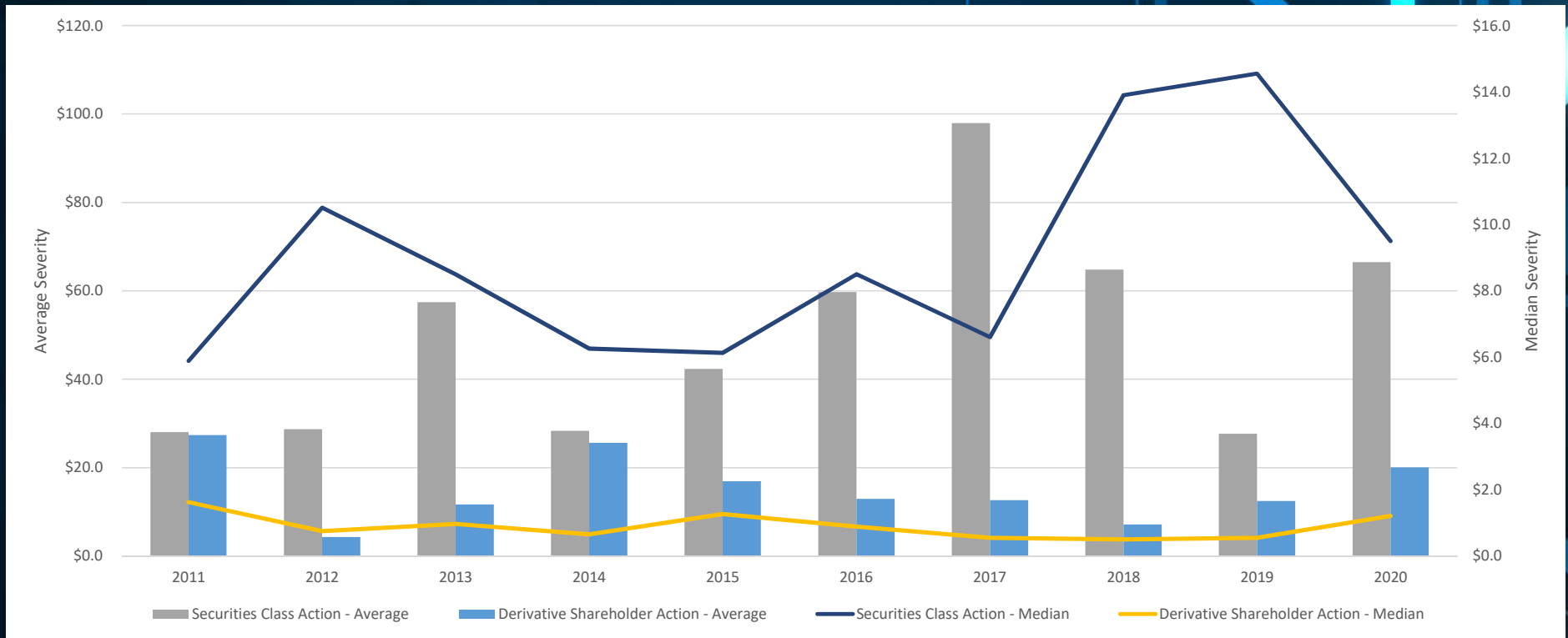


# Shareholder Derivative Awards

- Historically, these were generally low severity
- Awards included attorneys' fees and non-monetary relief
- However, seeing large settlements occur more frequently now
- Some attribute this increase to the options backdating scandal
- In many cases, Shareholder Derivative Awards are not indemnifiable
- This increases exposure to Side A

# Settlement Amounts by Settlement Year

## In Millions



Source: Advisen



# Shareholder Derivative Lawsuits

## Sample of Large Settlements in last decade

Company	Settlement Year	Settlement Amount in Millions
Wells Fargo	2019	\$320
Vereit/American Realty	2020	\$286
Activision Blizzard, Inc	2015	\$275
Google Inc	2015	\$250
Washington Mutual, Inc.	2011	\$209
Clear Channel Outdoor Holdings, Inc.	2013	\$200
McKesson	2020	\$175
El Paso Pipeline Partners LP	2016	\$171
American International Group, Inc	2011	\$150
Acciona SA	2017	\$140
News Corporation	2013	\$139
Arizona Beverages USA LLC	2015	\$125

Sources: Advisen, The D&O Diary

# Wells Fargo \$320 million Shareholder Derivative Lawsuit Settlement

- Filed in 2016, tentatively settled in 2019, final approval in 2020
- Related to the alleged creation of over 2 million unauthorized accounts
- Plaintiffs sued directors and officers derivatively on behalf of Wells Fargo
- Allegations included breach of fiduciary duty, unjust enrichment
- Derivative settlement included \$240M paid by insurers, corporate governance reforms and clawbacks valued at \$80M
- Defendants continue to deny allegations of wrongdoing or liability
- Also resulted in an SCA (\$480M) and fines and penalties(\$185M)

Sources: Advisen, The D&O Diary



# Considerations for Reserving

- Traditional loss development methods might not be effective for low frequency, high severity exposures
- Systemic events can have a significant impact on a book of business
- Close collaboration with claim and underwriting partners is important
- Need to be aware of limit and retention profile of book of business and severity potential



# Questions?

