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Insurance Uncovered

Directors' & Officers' (D&O) Liability Insurance

Here's a quick Q&A to introduce D&O Liability Insurance ...

What does it cover?

A Director's liability for 'wrongful acts' committed in that capacity. It's concerned with liability for the management of the business itself as opposed to the professional services that it might provide.

What are the main sources of liability?

Statute, common law, regulatory regimes and contracts are just a few examples. This means that there are lengthy lists of potential claimants, from Regulators to customers and even the company itself, in the case of derivative actions.

What's at risk for Directors?

Without wanting to sound too dramatic, everything! It's a personal liability which pierces the corporate veil and ultimately puts your own personal assets at risk. If you also face disqualification then it can affect your reputation and ultimately your livelihood. Of course, relatively few claims end up being successful, but the policy gives you the chance to defend yourself against allegations of wrongful acts.

Is D&O just about individuals?

It's primarily designed with individuals in mind (the market has traditionally described this as 'side A' cover) but policies are also structured to provide balance sheet protection for companies in the event that they're permitted to indemnify an individual ('side B'). On larger programmes there may even be an element of cover for the company itself in the event of a securities claim (you can see where this is going, 'side C'!).

Is D&O the same as Management Liability?

Yes and no. D&O is a component part of Management Liability packages which developed over the last decade to make the cover more relevant for smaller private companies. Typically such packages would also include Employment Practices Liability cover and a generic Corporate Legal Liability section providing a smaller limit, ring-fenced for the company itself.

In the event of a claim what does the policy provide?

Primarily legal defence costs but also awards of damages in the event of a successful claim and even penalties to the extent that the Insurer is legally permitted to pay them. In the 'soft' D&O market we started to see 'any one claim' indemnity limits becoming the norm for most sectors, but these are increasingly reverting to the traditional, annual aggregate basis.

Are there any common exclusions?

Aside from sector specific exclusions, D&O policies typically exclude claims that are more appropriately insured elsewhere e.g. professional services under a PI policy or bodily injury/property damage under an EL/PL policy. With the latter, however, there would often be a carve back of cover for Corporate Manslaughter claims. Beyond that, particularly in the soft

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market, there were relatively few exclusions other than 'conduct' such as fraud and those were subject to final adjudication by a Court.

What is the current state of the D&O market?

We're experiencing a hard market which means increasing premiums and narrower cover after almost two decades of the reverse. Common features of the soft market, such as additional limits for Non-Executive Directors, any one claim indemnity limits and retentions only applying to US claims, are starting to disappear. Automatic discovery periods (which allow a 'grace' period for claims to be reported after a policy expires) are also reducing, which increases the need for early reporting of any circumstances that might lead to a claim.

Does the future look brighter?

It depends on your perspective. In the face of diminishing premiums, spiralling claims and costs, a market correction was inevitable. High profile Insurer exits such as AXA XL in 2020, meant that capacity was disappearing from the market and not being replaced. For the cover to be sustainable Insurers had to take action to secure a more robust premium base. Whilst we don't anticipate that premiums will return to the lowest levels seen in the soft market, we do expect that the current increases will level off in the short to medium term as new capacity enters the market. This should make the cover sustainable in the longer term.

What should I look for in a D&O Insurer?

Experienced Underwriters, tried and tested policy wordings, a reputation for excellent claims handling and a good security rating are all key elements. An experienced Broker will also be able to direct you towards Insurers with sector-specific expertise.

If I met a D&O Underwriter at a dinner party what hot topics would impress them?

Drop 'SPAC' into the conversation and you're sure to get a reaction. They're currently a trendy alternative to traditional IPOs and primarily a US phenomenon, although starting to make their way across the pond. Like many US trends their impact is quickly felt in the UK D&O market and they're currently testing the capacity of some of the major global markets. Forbes described them as 'placing the risky chicken before the regulatory egg' and that certainly seems to be borne out in the claims experience.

As with all other aspects of our life we also can't ignore the current Pandemic as an accelerant of the hard market. Insolvency has traditionally been a source of D&O claims so anything that destabilises the economy, on a large scale, causes concern for Underwriters.

Once I renew my policy can I put it in a drawer and forget about it?

Hopefully, from a claims perspective, but not entirely. There are certain corporate events which can have a significant impact on the way the cover operates, so it's important to engage with your Broker to understand these. Mergers and acquisitions can trigger a number of different policy conditions which will determine how past, present and future claims will be handled. You need to take advice as early as possible in the deal timeline to achieve the best outcome.

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And finally, what about Elon Musk?

You didn't misread that. Ever the innovator, reports suggest that he may have replaced Tesla's D&O coverage with some form of personal undertaking to indemnify in a bid to reduce costs. For a number of reasons we think that this is likely to create as many problems as it solves and it's therefore unlikely to take off as a meaningful alternative to D&O insurance. Companies aren't always legally permitted to indemnify their Directors and, where corporate relationships break down, interests can diverge leading to 'Insured v Insured' claims. A tried and tested policy wording with an experienced, regulated, and security rated Insurer is likely to be more attractive to the majority of Directors.

To find out more about the cover you purchase, or to arrange an audit of your existing policies, please get in touch.