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Management Liability Insurance: Privately held businesses fare well despite hard market



by George Williams, CPCU

Agents and brokers might be surprised at how eager carriers and intermediaries are to write management liability insurance for their closely held clients.

WHEN it comes to account-selling for privately held businesses, agents and brokers should not overlook the opportunity to offer their clients management liability insurance. By doing so, they can arrange more comprehensive coverage for their clients while also boosting their own bottom line.

Management liability insurance is a relatively new product. Typically, it offers a combination of D&O and EPLI insurance with full entity thrown in as well. Sometimes such other coverages as fiduciary liability and crime insurance are included, too.

Despite the hard market, agents and brokers might be surprised at how eager carriers and intermediaries are to write management liability insurance for their closely held clients. Capacity for such business appears to be plentiful and, compared with coverage for publicly traded businesses these days, a lot safer to write. Following are some comments from markets we checked with, including their observations about the state of the market and suggestions for agents and brokers interested in writing more of this coverage.

E-Risk Services

According to Paul Tomasi, president of E-Risk Services, a managing general underwriter for Ace USA, management liability insurance capacity for privately held businesses is actually on the increase. "I think there are more and more markets trying to get into this niche," he said.

One reason capacity is growing, he said, is because reinsurers are discouraging carriers from writing publicly owned businesses by limiting

the amount of D&O insurance carriers can cede to them under their quota-share treaties. Consequently, carriers are diverting more of their surplus to the writing of privately owned business.

Furthermore, Tomasi said, "capital is a function of market potential," and with some five million privately held businesses in the U.S., versus roughly 15,000 to 20,000 publicly owned corporations, insurers know that the real opportunity for management liability insurance lies with the smaller players. If one assumes that privately held business pay \$10,000 on average for management liability insurance, Tomasi said, carriers could be looking at a \$50 billion market, which would dwarf the market for publicly owned business.

Like capacity, coverage for privately held businesses is going the opposite way that it is for publicly owned businesses, according to Tomasi. For companies traded on the nation's stock exchanges, insurers are moving away from entity coverage for securities claims and back to an allocation approach. Meanwhile, full entity coverage is still readily available for the privately held market, he said. "You're not seeing any coverage restrictions," he said, "other than a normal IPO exclusion," which gets a carrier off a closely held risk if it moves into the public sector.

Management liability products, which often add such coverages as fiduciary liability insurance and kidnap and ransom to the core D&O and EPLI coverages, continue to get broader, Tomasi said. Cyber liability insurance is the latest addition to his own product, he said. Management liability rates are not moving much, Tomasi said, with the exception of the EPLI component in some litigation-prone states, where rates are increasing 20% to 50%.

In today's hard market, underwriters are in the driver's seat for most risks, but Tomasi said that in the management liability market, agents still have considerable power. Carriers are competing for their business by trying to make their underwriting operations as "user-friendly" as possible. Tomasi said a number of markets, including his, allow agents to transact business with them online. Knowing that agents can't afford to spend a lot of time and money for risks that produce average commissions of perhaps \$1,000, most underwriters also confine their requests to information that is "need to know versus nice to know," Tomasi said.

Hartford Financial Products

For the typical privately held company, which purchases limits of no more than \$10 million, there really is no shortage of capacity for management liability insurance, according to Michael Price, vice president of Hartford Financial Products, a unit of The Hartford. "While there is an extreme tightening in the management liability marketplace for large and publicly traded companies," Price said, "at this point the privately held company still enjoys more options." Prospects also are being offered what amount to bargain-basement rates in today's hard market. "While publicly traded companies are seeing increases north of 100% and sometimes 200%," Price said, "the well-managed privately held firm is seeing rate increases in the 10% to 20% range."

The industry is, however, asking insureds to retain more of the risk, Price said. For companies with fewer than 100 employees, "we're seeing the average SIR for a small, privately held company moving from the lows of the soft market, where it was \$5,000 to \$10,000, to an average of \$25,000-and that would increase dramatically as the number of employees within the firm grew."

The scope of coverage is "relatively stable," Price said, with individual insurers combining various coverages in the management liability

package. For instance, HFP's product includes D&O, EPL, fiduciary liability and E&O insurance.

"The small employer tends to wear more than one hat," Price said. "For instance, if I'm a small consulting operation, I govern the financial affairs of the company, so I have D&O exposure. I probably do a majority of the hiring and firing, so I have employment practices exposure. I'm probably the trustee of the 401(k) plan, so I have fiduciary liability exposure. Finally, I'm probably the head consultant, so I have E&O exposure.

"We believe for the small customer, its more efficient, both from a price standpoint and from a claims-management standpoint, to bucket all four of these exposures in what we call management liability." From an underwriting standpoint, all four lines of coverage closely correlate with the financial performance of a company, Price said, so providing financial statements with submissions is a must-and very much in the interest of better-run businesses.

"In my mind, showing financial statements can only help your premium go down," he said. Without them, he said, a prospective insured will have no chance to differentiate its financial condition from that of the economy as a whole. The prospect's position will be all the better, he added, if the financial statements are audited.

In today's tough economy, many businesses look on D&O, EPLI, fiduciary and E&O insurance as discretionary coverages, but Price said agents should stress to their clients that they are essential. Practically all businesses are susceptible to EPL claims, he said, which, like workers compensation and disability claims, tend to increase when times are tough. "You may be more susceptible to suits just because your employees can't find jobs when they are laid off," he said. "Even if you've done everything right, you're still going to have to face the allegations."

In regard to the need for D&O coverage, Price pointed out that customers, creditors and vendors all can sue a privately held business for financial damages. General liability policies don't respond to such claims, he noted, because GL coverage is triggered only by claims for bodily injury or property damage.

Rockwood Programs

According to Glenn W. Clark, CPCU, president of Rockwood Programs, capacity for management liability insurance for privately held companies is stable, except in California. Primarily because of adverse experience with employment practices liability insurance in that state, Clark said, "short-term players have left, and the folks who have been in it awhile are hardening the rates" by as much as 50%.

Clark, who is a program manager for Gulf and Monitor Liability Managers and brokers management liability insurance to Lloyd's and other markets, said rates in some other parts of the country also are up 30% to 50%, again because of EPL losses. Deductibles are higher too. Whereas they once were as low as \$1,000 or \$2,500, he said, most markets now set them at \$5,000 or \$10,000.

Management liability insurance continues to be a challenge to sell to private companies, Clark said. "It's a discretionary purchase, and a lot of private companies just don't perceive a need," he said, primarily because they don't feel vulnerable to D&O stockholder claims-although agents should point out that private stockholders and third parties still can bring suit against closely held corporations.

Clark said agents should methodically offer management liability coverage at renewal to every GL client they have. Today, those clients probably are more aware of and concerned about EPL exposure than they are D&O risks, Clark said, so agents probably should take their cue

from that fact.

"Rather than try to convince somebody that they need D&O insurance for their small group of shareholders," he said, "you have a better chance of convincing them, that, 'Hey, you need EPLI—and by the way, let's get you D&O while we're at it.' It's kind of reversing how it was originally sold."

On submissions, agents sometimes make the mistake of giving underwriters dated financial information (or even no data at all). Those agents who can obtain interim financial statements to update the last annual statements will get the best look from underwriters, Clark said. In the interest of their own efficiency, Clark advised agents to seek a relationship with the market that gives them the fastest turnaround for quotes and indications. The price it offers, he said, will indicate of what is available from other sources. Then, after obtaining a quote for a client, the agent can tell him or her, "If you're interested, we'll go to the market and get a firm price for you." Only at this point might the agent approach multiple markets (up to three, Clark suggests), to keep the initially quoting carrier honest.

Zurich North America

According to Keith Thomas, vice president of Zurich North America's commercial group, privately held businesses are seeing nowhere near the tightening of capacity for management liability products or increases in rates that publicly owned businesses are. He said premium increases are averaging 15% to 30% on D&O insurance for privately held middle-market companies. These increases partly reflect the fact that a number of clients are coming off multiyear programs or are having financial difficulty because of the tepid state of the economy.

"There are some segments that are experiencing a tightening," Thomas said. These include privately owned nursing homes, physician practices and other businesses in the health-care arena. Claims arising from Medicare and Medicaid fraud are among underwriters' concerns, he said.

Thomas said management liability offerings are broad for privately held businesses, but some carriers are enhancing their programs by adding services. For instance, Zurich, to help clients manage their employment-practices exposures, offers them an online service called H.R. Care, where clients can access information about current laws pertaining to anti-harassment and anti-discrimination laws, the Americans With Disabilities Act, etc. They also can obtain information about employment-application questions that might not be allowed, trends in litigation, etc. All the information "potentially could cost a fair amount of money" for businesses to obtain on their own.

Thomas said the quality of an agent's submission still makes a difference—especially if the client has not had a portfolio of management liability offerings before. He advised agents to provide three years of full financial statements and comprehensive background information about directors, officers and managers. For those clients with more than 14 or 15 employees who are considering employment practices coverage, a copy of the EEO-1 report—a census required by the Equal Employment Opportunity Commission that breaks down employees by age, race, gender, etc.—should be included.