# State of the Directors and Officers Insurance Market

AM Best Associate Director David Blades joins industry experts to discuss emerging trends in the segment, as well as innovations and shifting dynamics.

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## PANELISTS:

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View the complete webinar at: https://www.ambest.com/video/Video.aspx?vid=6327627984112

**JOHN WEBER:** Welcome to our webcast, "State of the Directors and Officers Insurance Market." I'm John Weber with AM Best. Over the next hour, our panel of experts will discuss the challenges and opportunities facing the directors and officers insurance market. We're going to meet our panel in just a moment.

Let's meet our panel. First, we welcome in Uri Dallal. Uri is Managing Director, US Regional Leader for Aon. Next we say hello to Daniel Hojnowski. Danny is Senior Vice President, Head of US D&O/E&O/Cyber at TransRe.

**JOHN:** Last but not least, we have David Blades, Associate Director, AM Best. David, take us through the details in the highlights of AM Best's most recent D&O report.

**DAVID:** As you mentioned, John, yes, we did just complete our report on the D&O market. First thing I'll say is that I definitely look forward to this discussion and learning a lot in terms of engaging thoughts with Uri, and Danny.

Just looking at this marketplace, these last several years has been very dynamic from the perspective of somebody looking at it from a research perspective. It's been very interesting getting involved, going to conferences, hearing more and more about the marketplace and what's going on.

Like I said, hopefully, for the viewers of this webcast, they'll get a good feeling and get good insights from our discussion today. I do have a few slides that I can go through to give the highlights of our report. Again, it was just published earlier today.

In general, just looking at things initially, current global economic challenges have created considerable uncertainty in the business world. Corporate directors and officers have to navigate those challenges in terms of running their corporations, generating favorable results, and putting the corporations in the best competitive positions.

One of the key themes in the report, 2022 was a year of transition in terms of the pricing in the public and D&O Market.

Coming into the year, renewal pricing had been on a dramatic upswing. Beginning in 2019, that pricing reached a peak midway through 2020. Those significant quarter to quarter increases continuing through 2021.

By 2022, we saw things start to moderate and a definite deceleration in those rate increases. As the months war in, you got closer to the year, and we saw more and more rules. We heard about more and more renewals even getting close to the flat renewal, very small increases in comparison to what you saw 24 months earlier.

Part of the reason for that is additional capacity from new market entrants and established market competitors who are looking to grow their book. That led to heightened competition and that, obviously, then put downward pressure on pricing to somewhat less restrictive policy, terms and conditions.

All those factors went into what we saw on the marketplace in 2022. Ultimately, from our perspective we think that the jury is probably still out on the ultimate profitability of the business that's mid written recent years, especially when we're trying to see the maturity of the 2019 through 2021 excellent year.

We'll continue looking, continue monitoring what we see but we think the jury still out in terms of whether rates got to a point where they aren't really going to make a sustained difference in terms of the profitability that D&O underwriters fine.

The next slide shows what I referenced in terms of what we saw on the pricing. If you go back to 2014, 2015, 2016, where rates are generally flat, small increases or decreases. Those were in use, what we saw the loss ratios ticking upward a little bit, so the reaction from the company's more or less started to manifest in 2019 and you can see rate started to go up a little bit there.

Then, in 2020, a full market change, market hardening hit. It was at a peak in 2020 and then regulate a little bit, stabilize a little bit, but it's still sore. Sizable increase, a double digit increase in 2021.

Then, 2022 is when we start to see more stabilization and deceleration in what we saw in terms of the quarter to quarter rate increase. Again, a dramatic change in 2020 and 2021 and the deceleration by the end of 2022 got where we are now, where it's softer market conditions heading into the start of this year.

What this exhibit shows, we utilize the information that we get in the annual statements that are filed by rated insurance companies that we follow. In those statements, there's a D&O liability supplement that provides direct top line premiums written and loss information, so we can follow that information and look at the premiums and also look at the loss ratios over time.

This shows 2011 to 2022 information. You can see the 2014, 2015, 2016, very stable premiums, but you saw the direct loss ratio start to tick upward. You only saw the manifestation of the concerted actions by the D&O underwriter to start to manifest themselves in 2019.

In 2020, obviously, the rate increases that were being applied then leading to higher overall premium volume and reaching a crescendo, at least, for the most recent market in 2021. Premiums went down a little bit in 2022. You can see the actual direct loss ratio did take upward a little bit in 2022.

We're going to continue looking at the results to see what the current pricing environment does from a profitability standpoint. I do want to make point out that, AM Best sees, it wasn't all accounts that needed to have the rate increases and the considerable increases, but it was those accounts that were lost leaders.

For some of these companies that were producing multiple losses and multiple claims, those are the ones that were getting focused on by the underwriters out there in the marketplace, and those are the ones that needed the attention.

What we look at here is the red line tracks number of federal securities class action litigation filings. You can follow what's going on in the D&O marketplace by what's going on with the security class action filings.

Generally, when the SCAs increase in volume and in severity, rates tend to increase. You can see as federal securities class action litigation filings increased, 2017, 2018 2019, they reached record levels in those years.

In those years, you were still seeing the direct loss ratio again, on a direct basis on an aggregate basis for the PC industry at gotten to its highest point, at least, in the 2011 to 2022 period. You see the big thing on here is that you can see in 2020, 2021, and 2022, you see security class action filings trending downward.

To some extent, that's a favorable position for D&O underwriters. That's also supportive of the mindset of those who were looking to decelerate the rates or that were looking to get lower rate increases or more moderate rate increases because in part the impact of the lower security class action filings.

What we saw in 2017 to 2019, we didn't see the impact from a rate perspective hit until, like I said, 2019. It was still a couple of years that it took time for the rates to catch up with the higher security class action litigation filings in those years. Those filings were generally up largely due to merger objection lawsuits.

Like I said, in general, the way AM Best has looked at it, we believe the overall softer market position for D&O market and underwriting conditions. It's questionable whether that will be sustainable for the overall health of the marketplace.

Like I said, as accident years 2019, 2020, 2021 mature, and we see how the reserving process, whether the reserves that were initially put up for those claims end up being enough, or whether there needs to be more padding to those reserves, and therefore, that will tell whether the business was actually profitable or not.

We'll continue to look at that and see how that manifests itself over time.

**JOHN:** David, who are the top writers for D&O in 2022, and is it shifting in any way?

**DAVID:** Actually, I have another slide here, where we can look at the top. This is the top 15, based on 2022 direct D&O liability premium, again, taken from the annual supplement in the annual statements.

In general, in any market, any line of business, we generally see the top 25 or so organizations. Again, this is not individual companies, this is the organizations. This is Chubb or XL America, as you can see at the top, and the various companies that fall under that umbrella. You'll generally see in the top 20 or 25, them writing a majority, or 70, maybe 75% of the overall line of business.

In this case we see a lot of concentration at the top level. What's interesting in this slide is that the percentage change from in 2021 to 2022, you see 9 of the top 10 companies there, or top groups, all posting a negative premium change.

That again is part and parcel to what we saw in the marketplace two of the companies, XL being the top group and AIG generating double digit declines in premium. Again, that's largely due to market conditions and maybe some other factors in there for them as well.

Going through this listing and looking at the overall direct loss and defense and cost containment expense ratios, you see even for some of the better companies, some of the ones that are writing more of the business, that they have had higher loss ratios and have struggled a little bit from that perspective.

We've seen generally that the concentration, in terms of the premium, has relatively stayed in with these companies, although in the marketplace some of the competition has been brought in by new market entrants. Some of those have been surplus lines companies but some of them, there haven't been any big enough, obviously, to crack the top 15.

We've seen new market entrants making a difference in the marketplace, in terms of the competitiveness and the overall pressure on rates.

**JOHN:** You mentioned the surplus lines companies. We want to address that a little bit later. In the meantime, I want to bring Uri on into the conversation. Ari, first quarter D&O prices have plummeted. What's driving that?

**ARI:** David had a chart up where he was showing the overall premium volume across the industry and you could see that that was down, year over year, from 2021 to 2022. Correspondingly, as noted, the capacity in the market increased. New markets coming in, markets evolving their appetites.

The broad stroke response is that you have a larger selection of markets and capital chasing a shrinking pool of D&O premiums and that persisted in the first quarter of 2023. Aon puts out a quarterly pricing index. Our first quarter numbers came out a week or so ago. The headline number was 25% and change, 24.9%.

The same store sales number of quarter to quarter, same limit, same companies, was 22.3. There's obviously a lot of nuance in those numbers. Greater decreases for folks that are coming off a year following an IPO or a de SPAC, and the more stable changes for other, so let's say, Fortune 250, in the marketplace, but certainly, that downward trend persists.

It's generally not perceived to be because of a decline in risk. It is generally a function of competition in the market and a larger pool of insurers chasing a smaller pool of deals, be that on the basis of a dearth of IPOs, a lack of the expectations coming out of the SPAC/de SPAC marketplace. Really, that is the driving function of the market.

There's some interesting nuance in our charts that came out, where we've now shown, at least on the basis of our data for public D&O, the price index lines up about equivalent to 2004. We see that as a baseline for how the market is behaving and where it's acting.

You saw dramatic decreases in that time frame as well, coming off of big increases in 2003 and some of the prior years. The market took a downward trend for a long time. Whether that persists is a bit difficult to predict. We have shown price decreases each of the last four quarters. It'd be curious to see, as you get into Q2 2023, if there's rate on rate that comes out of the market.

My anecdotal experience in the last couple of months suggests that that is the case. I do think there's obviously risk based factors that are impacting where pricing will go in the market, certainly in corners of the marketplace, like the banking area, where the regional banking crisis is unfolding.

We expect there to be pressure on rates, certainly in firms that are treading water, having difficulties with liquidity. The credit out there and available is difficult. That is likely to be a function of some pressure on rates there. The broader world of public company D&O is that there is competition chasing every deal. Folks are, at this point, for the most part, unwilling to shed market share.

You can see, David had up the chart of the leading market share insurers out there, and they all shrunk in 2022, but that chart didn't change much, year over year, those rankings. The expectation, my expectation, would be that that persists. Firms don't want to shed market share. They still, in a whole, feel pretty good about rates are, compared.

Certainly, if you look at where the baseline is now, compared to 2018 or 2017, it's well above. That continues to be a function of putting pressure downward on rates.

**JOHN:** Danny, what's going on on the reinsurance side?

**DANNY:** When you look at the professional liability reinsurance size and D&O and E&O here, we've been in a soft market since 2013 when you think about it. You had a fair amount of third party capital come into the property market. That took some traditional reinsurers who played heavily in the property space, and they started pushing into the longer tail lines of business, around 2013, 2014.

Similar to what Uri said, supply and demand's a big factor at play here. More reinsurers wanted the business, so ceding commissions went up. When you saw us get to the lows of where we were on the underlying business rate laws, especially in public D&O around 2018, a function of that was that reinsurers were willing to pay higher seating commissions.

If you're an underwriter sitting at your desk, you could probably give 10 points off if you know now you're getting an extra 10 points worth of override your reinsurance.

When the underlying market started to correct in '19 and '20, the reinsurance market remains soft. In fact, we started paying even higher seating commissions, we were relying on underlying rate to solve our problems essentially. Since everything's done on a quota share basis, all that rate was flowing right to us.

What we're seeing now is a bit of a shift in that. One's a very heavy time for us on our renewal cycle. Everything we were seeing, whatever your rate projection was for 2022, you missed it. You missed it by a wide margin because the rates turn so quickly negative, especially in public company D&O.

Then, on top of that, I'm adding another negative projection for 2023, anywhere from 7.5 to 15 points running through. Next thing you know, my loss pick is going up. Typically, we're up double digits on anything that's a heavy public company D&O.

Seeds have started to come down. They're not coming down as much as, in my opinion, they should come down. The funny thing that we're seeing, and it's counterintuitive, a lot of the people are keeping more net.

I think there are a few factors at play on that. One, everyone's property reinsurance costs a boatload more. If you're looking to keep your spend constant, maybe you keep a bit more net on the professional liability side.

The other thing at play here as well, a lot of people are missing their budgets. We saw just about everyone was shrinking as far as premium goes.

Everyone wants to focus on the bottom line, but the top line for a lot of these carriers does matter as well. You cut back on the reinsurance purchase a little bit, that stays right there on your top line for you.

**JOHN:** David, the report mentions IPOs. Is the IPO market cyclical, or are we seeing some sort of trend here?

**DAVID:** I think from an IPO market perspective, and Uri touched on a little bit how IPOs had been down, a large reason why they've been down is the economic conditions that have been really tough. It'd been limiting the number of companies that were trying to use IPOs to go public. Again, given the troubles in the marketplace.

What we did see is that in 2019, 2020 and 2021, we saw, and I'll put up a slide that shows it, special purpose acquisition company.

IPOs that were utilizing the special purpose acquisition company or SPACs, SPAC IPOs, they trended upward or they jumped upward in 2020 and 2021. Fell considerably in 2022.

When you're looking at things from a cyclical perspective, in 2020 when equity markets really bounced back initially after the initial onset of the pandemic, that's when we saw increase in the number of SPAC IPOs and continued through 2021.

Essentially, once they form, they have two years after formation to find a target company to merge with. We're still seeing that play out even as we're in the beginnings here of 2023, but from a cyclicality perspective, yes, it seems tied to economic market conditions.

We've seen the IPO market show cyclicality or exhibit that cyclicality is a definite part of it. Like I said, the SPACs and them coming to the forefront as a vehicle that were being used for the IPOs, they were a big part of what we were seeing.

There are risks associated that the directors and officers of these SPAC organizations and the sponsors obviously had to deal with.

One of the reasons why we saw the drop off in 2022, is because of regulatory pressures that were put on them from a disclosure standpoint, much more regulatory scrutiny on the sponsors than those involved in forming the SPAC company.

That also played a part in the lower numbers in 2022 and continuing what we're seeing from an economic standpoint. I do think it's cyclical. We'll see as we're still dealing with high interest rates, we're still dealing with equity market, bond market volatility.

As we see some of those conditions moving hopefully for all of us closer in the rearview mirror, we might see some pickup on the IPO side.

**JOHN:** Uri, what are some of the risk trends that you're noticing?

**URI:** Like I said, it's in the first round of commentary. We don't see risk as good being reduced in the current market.

Securities class actions are about at their baseline. The uptick, in some prior years, may have been a little bit misleading around the distinction between M&A claims and whether they fall locally or federally. We see a persistence of, let's say, 200 to 230 securities class actions on a regular year.

Defense costs continue to increase. Often, the plaintiffs' are the villains in the room in a D&O context, but the increasing defense costs erode, exhaust pretensions, and make up a significant component of insurers' loss.

Big settlements persist. Just in the last week, there's a massive securities class action settlement, and in the last couple of weeks, a massive derivative settlement also.

That's become an important component of the overall market and how we think about it and how our clients think about it. If those derivative settlements are a side losses a portion of the program that was historically relegated to bankruptcy laws and sleep at night, insurance is more actively a working component of the programs.

Bankruptcy has become something that is on a lot of people's desks on a regular basis here and increasing.

Not just a function of whether someone can't make an interest payment or whether they're breaching a covenant on a term loan, but we are increasingly seeing different components of a debt stack pushing for restructuring in order to get ahead of an eventual risk down the line. That perpetuates and increases that risk in the market.

I do think, sometimes, the D&O loss around a bankruptcy is overstated. Sometimes, insurers get a little bit over concerned about that and push that risk in a way that maybe is less aggressive or less toothsome than one might think.

Regional banking crisis, obviously, has some time to work out. Certainly hearing a lot of questions in the space about valuations of commercial real estate on people's books, how that and valuations there might filter through as a loss issue.

Then, certainly, ESG is a hot topic that we're persistently talking about, questions about how much that ends up codified in law. I think the political nature of it, a little bit of the damned if you do damned if you don't component of that.

Our clients, large public companies and other companies, getting swept up in the polarized nature of the political environment and that turning into D&O's style litigation is something that people are actively concerned about, thinking about, and we find underwriters asking a lot of questions about.

**JOHN:** You mentioned ESG, Uri. How much is ESG impacting the D&O market?

**URI:** It's hard to pin down how much insurers are pricing for ESG risks. For the most part, the risks associated with failures in those components of running your business are issues that have long been part of the D&O marketplace.

They're go board level governance style issues. How do you manage your company for long term exposures to things like climate change and other environmental pressures? How do you hire and retain talent that is most beneficial to the success of your business? What is governance and how much diligence do you pay towards it?

Those aren't new tasks for boards, but there is this highlighted and valuable new onus on it.

At the very least, we're discussing it consistently with clients. It's coming up at underwriter meetings. It's coming up at one on ones. How are you addressing it? It may be in the vein of whether you're net zero or not. It may be in the vein of diversity and inclusion as it corresponds to pricing. It may be more in the context of our these board level committees.

I'm yet to see clients be uninsurable or take on higher premiums as a result of not being prepared in that regard. I think, to some extent, the nature of the clients that we work with in the public company space have been savvy to that, have good answers, and are addressing it.

For the most part, right now are able to give insurers the comfort that they want that the firms are addressing it. We do expect as time develops, there would be an increasing amount of litigation with and each of those silos climate litigation, this woke anti woke style issues persist. It's something that we're closely watching and thoughtful about.

**JOHN:** Danny, what are you seeing from Schedule P data?

**DANNY:** Schedule P data center we look at every year when it comes out here at TransRe. We look at the results from other liabilities claims made. For us, that's the best proxy for the professional liability market, includes D&O, all the various E&O lines, reps and warranties, cyber.

What we always look at is where people are booking themselves now versus where they had originally booked themselves and even where they were booking themselves maybe two years ago.

Some stats, if you look at where as an industry we were booking professional liability in 2020 versus where we're booking it now, we've added about one and a half billion dollars worth of adverse development onto the books.

2018 alone contributed four billion over the past two years. I believe it's roughly 2 billion in total adverse development since that was originally booked. What we see is we're looking at that 16 to 19 block. It seems to be extremely problematic, the social inflation, higher security class actions.

There were a number of things that ran into there as well as you are at the point. You were at the low point of the soft market. 2018 is probably one rates bottomed out for a lot of these lines of business.

Then, we look at it from a reinsurance perspective. I have a real math problem here. Most of those years are running high 60s, low 70s, the years I mentioned at 16 to 19 block.

Let's say someone was running to a 65 loss ratio, which would be generous given where the schedule P data is, and a 30% ceding commission, which where the market was back then, 30 would have been on the low end. I got to pay two and a half points of [indecipherable]. 65 plus 30 plus two and a half, that's a 97 and a half before we pay salaries, before we pay our rent.

Keep in mind we had no investment income in that block years. From the reinsurance side, it was a very tough go. You couldn't make that math work, which is why now you're seeing reinsurers pushing to drive some ceding commissions down.

I know this is about D&O, this particular webinar. Other liabilities claims may touches on all professional lines. When you think about what goes in there, what I just talked about, you had some E&O lines, you had reps and warranties, you had cyber.

Within that 16 to 19 block, for the most part, those lines actually did run fairly well. If we're looking at loss ratios in the upper 60s lower 70s, you had some lines that were running probably somewhere in the 50s. Things had to be running well above those numbers as well.

The biggest one of that was D&O, particularly public company D&O that drove those loss ratios up considerably.

**JOHN:** Uri, in your role engaging with clients, what are some of the uncovered risks they might not be aware of?

**URI:** For the most part, D&O policies, both in the public and private space, do a good job of providing robust coverage. We talked earlier about pricing changes historically. I don't think during the more challenging years of price increases, we didn't see a ton of slippage in terms and conditions.

Now, in a moment where there's more pricing pressure, I don't think we're seeing the opposite, where all of a sudden, the insurers are willing to blow open the door on the terms and conditions that they're willing to offer.

I do think historically, where D&O policies struggle is with the blurrier lines around money spent, particularly around defense expenses and legal fees for items where allegations of wrongful acts maybe murky.

On the regulatory side, where's the line on regulatory investigations, when the SEC or another regulator comes and starts poking around, there are often not entirely clear or forthright about what their intentions are, what exactly they're looking for, trying to uncover.

Understandably, D&O insurers have a hard time parsing out where to start that line on covering legal expenses when some of the questioning may not necessarily directly be leading to what you view as a more formal litigation expense.

Internal investigations fall into a similar bucket. If all of a sudden you have a activist shareholder and there's maybe proxy issues looming, and the board wants to go out and retain counsel to evaluate considerations, though that is not clear cut litigation but defense expenses are being spent.

It has a lot of the look and feel of what D&O losses look like.

There can be confusion on the client side. There can be frictional between clients and insurers around where that line is, where coverage can trigger, and whether there are direct or implied allegations of wrongful acts.

You see that happen in the world of 220 demands, also as they've become an increasingly an entry point for the potential derivative or shareholder litigation. Sometimes, those demands aren't particularly clear. Language may require it to relate to a securities claim or not. Those can become trapdoors in coverage.

While as a whole we feel like coverages robust, insurers do a good job of putting their arms around the risks inside of policy. At the margins, they continue to be items to keep an eye out and costs that are maybe not well covered in the traditional or typical D&O policy.

**JOHN:** Danny. what kinds of conversations are you having with your clients?

**DANNY:** It depends on the particular client. I always say I have three different types of clients that make up our portfolio. One, you have the partner who buys reinsurance for the long term. They value our feedback. They value the partnership. It's a long term give and take with them.

There are other new markets that quite frankly have to buy reinsurance that they don't have a choice. Then, there are others who buy on an opportunistic basis that you get a certain override, they'll buy it and if they're not, they're not getting it.

A lot of the conversations we're having now, first off, centers around renewal retention ratios. Obviously, we're concerned about the price decreases we're seeing. We want to see, "Are you willing to walk away from business that is under too much pressure? Or are you staying with business?"

What I find amazing is the delta in the responses I get from people we talked to be a client's new prospects or just people out in the market. I've heard, "We know retention of ratios for DNO as well as mid 60s." I've heard as high as the mid 90s, I don't ever recall seeing that big of a spread amongst people.

Some of the other things that we talk about is rate change. We talk a lot about rate change because I have people missing their 2022 rate and projecting negative alpha 23. What makes that up? Were you writing a fair amount of opportunistic deals?

Uri alluded to this earlier, talking about what's getting what type of rate decreases? Were you writing an IPO that two, three years ago was in an ultra hard market and you were able to charge a 30 plus% rate online, or are you giving back a similar amount on a more typical manufacturing company, where the rates shouldn't be fluctuating as much?

Also having a lot of conversations about the data that they could provide to us. The more granular you can give us information… We have some benchmarking tools that we use. We're always happy to give feedback to our clients.

The more granular you can get with even your policy level data, that allows us to do some things, to look at yield and actually differentiate yourself as opposed to just broad brush every one of our clients with, "The whole market's going this way. We're going to do this."

If you could give me data that shows me that you are in fact outperforming the market, we are happy to reward you with a higher seeding commission for that.

**JOHN:** Thanks, Danny. David, a viewer asks can you talk pricing differentials between excess D&O and primary D&O?

**DAVID:** That's an interesting question. It's funny, I went to a conference early this year, and they batted around that concept. I can talk about it a little bit from what we hear from our analysts.

It seemed like we focus a lot, and I know even in our report we focused a lot, on what we saw on the primary side in terms of the rate increases that, again, companies really needed to address what they saw coming through their book as they look at those reserves, as Danny pointed out, as they start seeing some adverse development in some of their prior years and looking at the risks that are out there, that are inherent in the marketplace.

Now again, social inflation, litigation funding, all these different things, they really focused on hitting on the primary side.

It seemed like for the companies that do right, both primary next…As it seemed like the rate need might have been bigger on the excess side because of how some of that business was getting written whereas, on some of the excess coverage, even when companies were pushing for increases and to improve their pricing on the primary side.

They weren't pushing as much on the excess side so it seemed like they might have made some strides from a primary perspective but the strength of the excess book from a pricing adequacy perspective was trailing that on the primary side. That's a compilation of some of the things that I've heard. I'm interested to hear the other gentleman have perspective on that.

**URI:** In the pricing index that I was referring to earlier, we break out primary versus excess or at least primary versus the overall number.

In Q1, the primary decrease was  7.9% and recall that the overall number was 24.9 percent. This primary number doesn't clarify for same store sales thing which that numbers a little bit lower, but you can see the trend there where the excess are far higher than they are on primary.

I think for the most part, that speaks more to, I would say, the greater commoditization of excess markets and a greater willingness on the part of a lot of buyers to build and nurture relationships with primary and low layer insurers and be willing to negotiate with them a little bit more.

A little bit of give and take, and really, a more aggressive approach both on the excess part from insurance companies, willing to be more aggressive about pricing that they can give on an excess layer because maybe they feel like they're a little bit more comfortable in the risk.

Also, probably a greater willingness on the buy side from our clients to reshuffle excess insurers and be more aggressive with price savings there, and the expectation that primary insurers are going to drive the boss on to claims adjusting front.

Danny: I think Uri summed it up well with the difference between primary and excess. Most of the time, especially for a large public company D&O, you're going to have a few main carriers, who are your primary, and low excess people who come in and write primary should anything happen.

The excess, to some extent, has gotten a bit more commoditized. Where I sit, we're looking at results of the entire industry. We have people who write mainly primary. We have people who write mainly excess. We're seeing a big change. Primary is giving back a lot less rate. If we look over a 10 year block, they're up for debate.

What I could tell you is we see a lot more volatility in people who write excess because you're going to have fewer claims, but you're getting much less premium versus the primary. The primary is a bit more steady, more predictable, whereas the excess is just fraught with volatility.

**JOHN:** David, surplus lines has been gaining traction, gaining market share when it comes to D&O. That's another sector that I know you follow very closely. Should we be surprised by how much market share surplus lines is gaining in the D&O market?

**DAVID:** No, given the noise that we saw on the D&O market. We're talking about in the 2019, 2020, 2021, where we saw rates increasing dramatically or at least in 2020 and 2021.

Where the surplus lines market comes into play is when clients are...When their agents or brokers are having a hard time placing their coverage, that's when a lot of time the surplus lines market will have to come in and provide coverage.

They have the freedom of written form to be able to put together coverage product and charge the rates that they feel truly assess the risk to be able to come to the marketplace with that.

I think for those where a lot of the brokers might have been having a lot of trouble finding a home or finding options for some of their clients, the fact that surplus lines companies came to market and filled some of that need is not surprising in terms of their function in the overall market place.

I will say that from a D&O perspective, while the surplus lines numbers that we saw, it wasn't a dramatic increase, but it is a discernible increase in terms of how much more premium they wrote. I also think when you look at what's happening at late last year and where the market is now, these brokers are going to be able to find coverage for their companies in the admitted market more or less.

You have to bifurcate when you're talking about those risks that have been lost leaders that have had multiple claims and have some issues that need to be dealt with. Those are the ones that are still maybe have some trouble and might need surplus line coverage, whereas the ones that may have had a loss or two here or might be lost free should be able to find admitted coverage, I would think.

**JOHN:** Uri, W.R. Berkley Corporation President/CEO Robert Berkley was quoted just last week as saying, "The company is not going to chase cyber down the drain." What do you make of a statement like that?

**URI:** I think that's a fair statement and probably one that a lot of senior leadership at underwriting firms would make. Not just about cyber, but about other lines. Cyber is unique, and that folks have long feared the systemic risk associated with it. That you could have a mass event that impacted thousands of companies on a short basis.

The world of financial institutions, D&O and E&O, has looked a little bit like that and probably kept some of the volatility out of it. What's going on in the cyber market is not that dissimilar from where we started this conversation.

People are still fearful of risk in the space, but at the same time, capital chases rate. You had an environment where rate increased dramatically, particularly last year and maybe the latter half of 2021. That meant that new markets flooded in. They saw opportunity, but eventually that opportunity levels out and you end up with markets that have capital. They've been capitalized. The reality is, is that money gets spent. Insurance companies don't get capitalized and then not write risk.

At some point you end up cannibalizing a marketplace and driving rate down. That's what we're seeing in D&O. Over time, absent that systemic claim environment that people worry about, that systemic risk environment in cyber, you see the same thing happen there, but time will tell.

**JOHN:** Uri, are you seeing clients buy more limit?

**ARI:** We're seeing clients consider what to do with D&O savings. Danny made a comment about how the property market and the treaty renewals on the property side impacted what was going on on the financial line side.

I certainly have clients who have said, I got murdered on my property renewal and now I need to be thoughtful about how I allocate dollars to D&O and other professional lines and what I can do with savings here. We also have clients that look at settlement trends and look at defense cost trends, and when they can get savings out of their D&O programs, they take that as an opportunity to buy increased limits. Or there's that nuance within D&O programs between ABC or entity cover programs and Side A only. We see clients be thoughtful about those ratios if they feel like there's cost savings to be had.

Then maybe in the more challenging market, they took down entity cover in favor of A Side, they may be reorienting those ratios back to a higher percentage of entity cover and not necessarily increasing limits in the aggregate, but taking on a higher amount of limits that have a broader amount of risk that they cover.

**JOHN:** Thanks, Uri. Danny, will the recent banking failures have an impact on D&O?

**DANNY:** Yes, it's to be determined. Where you might start to see it is amongst the regional banks in that space, and Uri talked about this earlier. There's a lot of concern about commercial real estate now. Are they matching up assets and liabilities correctly?

I'm sure there are a lot more questions being asked. If you look back to the financial crisis that we had in 2008, the brokers did a very good job of differentiating commercial D&O versus FI. When I first started in this business it was right after the IPO laddering issues. Everything price wise went through the roof. After the financial crisis, it wasn't that way.

FI saw rate increases, but the commercial market for the most part stayed pretty steady. If you're going to see anything, maybe you'll see a little uptick in FI rates. Maybe Fi rates won't be dipping down as they would have been absent something like this.

I also think there's still a long way to go in this. Is it going to turn into a full fledged crisis? Is this contained in? I don't think anyone knows the answer to that right now, but I would be very surprised if it bled over into commercial D&O, maybe you might see an uptick in FI rates, though.

**JOHN:** This certainly has been a very informative discussion today. I'd like to get our panelists closing thoughts on what they think the big takeaway is here today and what they would like everyone to remember from this presentation. Uri Dallal, why don't we start with you? What's the big takeaway here today?

**ARI:** Big takeaway is there's pressure on pricing consistent throughout the D&O marketplace that is largely on the basis of competitiveness among capacity, not on the basis of there being a decline in risk in the marketplace.

The closing thought I would leave with is most of the buyers that we interact with, they don't want dramatic volatility in their insurance premiums over time. They want healthy insurers that pay claims and that can provide a consistent level of service at consistent premiums.

Some of the whipsaw in the market has the tendency of turning off some of the buyers out there. While certainly everyone appreciates declining rates, I would encourage markets to be thoughtful about that and thoughtful about trying to not have volatility in pricing over time.

**JOHN:** Danny Hojnowski, what are your closing thoughts today? What's the big takeaway?

**DANNY:** Sure, I hit on this, Uri hit on this. I feel like we say this a lot here at TransRe especially, but if you want to teach a high school economic class, look at the D&O industry, it's supply and demand.

We had rates go up, more supply came in. At the same time, you had fewer IPOs, fewer companies, more supply, less demand, pricing goes down. I would caution people out there. What I hear a lot is, rates are still well above where they were in 2018. That's a fair point.

Rates are well above where they were in 2018, but we talked about Schedule P data. We looked at all the numbers. 2018 is not going to be a good year for D&O.

If we want to make this sustainable, rates need to consistently stay above where they were in 2018. People have taught themselves, some people have taught themselves into using 2018 as that benchmark, but look at where that loss ratio is probably going to be for 2018.

People are also getting comfortable with security class actions being down, and while they are down, they're basically a baseline like Uri had mentioned before, and there's still a huge backlog.

I'm concerned over somewhere in the next 12 to 24 months, we're going to see that increase come back up and we're going to be back up to where we were in the 2019, 2018 time frame. I don't think that's going to end well again for insurers or reinsurers.

**JOHN:** David Blades, you get the last word today.

**DAVID:** These gentlemen brought forth a lot of good thoughts in terms of what's happening in the marketplace. The question that we got in terms of looking at the primary versus the excess market, there's a lot there in terms of telling what's being done to address rate needs and seeing how it's going to play out from that perspective.

I do think as a rating analyst, I am going to go back and do some more digging as Danny mentioned in terms of looking into some of the Schedule P data for other liability claims makes. That's where you can obviously see some of the results from a D&O perspective, although there's obviously E&O and as you said, reps and warranties, there's other business in there.

This is a dynamic marketplace, has had a lot going on. There are still a lot of challenges and although we've seen the rates softening, I hold out. As Danny said, 2018 is not going to turn out to end up being a good year once everything plays out, and still remains to be seen how 2019 and 2020 are going to play out.

We are where we are in the marketplace as they said, because the supplies out there, but it'll be interesting to really hone in on what we're seeing this year. Like I said in some of the more recent accident years how they developed to get a feel for what we're going to see over the near term going forward.

**JOHN:** Thank you, David. Thank you, panelists, one and all. I'd like to let our viewers know that our D&O report is posted online at ambest.com. We will have a full replay of this webcast posted within the next day or so. A full transcript will be out within the next week or so. For AM Best, I'm John Weber.