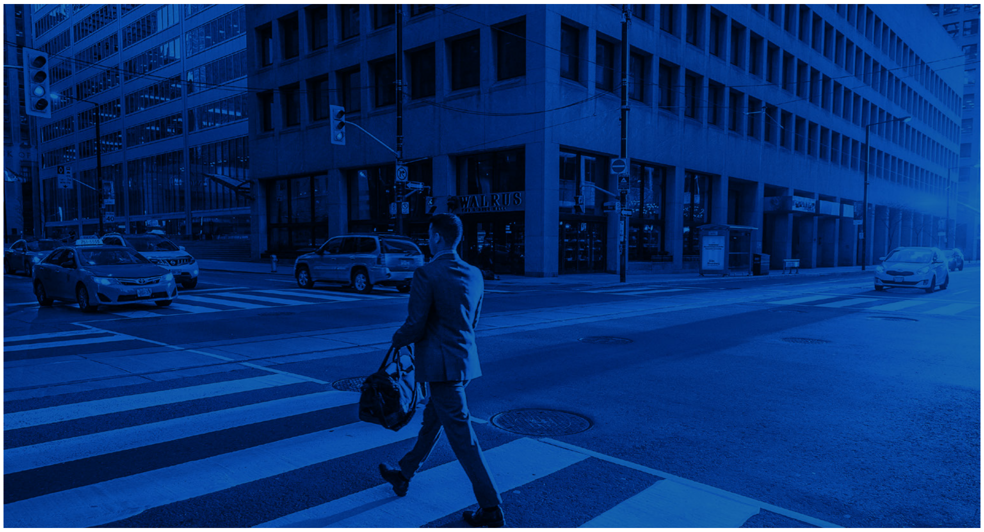

Private Company & Not-for-Profit Organization Management Liability Insurance

In the first quarter of 2019, private company management liability insurance carriers were generally seeking premium increases of 5% to 10% (absent any material exposure changes). Since mid-year, many of the same carriers have gravitated toward double-digit premium increases based on actual rate need as well as updated market based underwriting strategies. In addition, a number of established carriers are approaching particular industry classes with significant shifts in underwriting appetite. Of particular note is the healthcare industry. Several D&O insurers with large books of healthcare business are seeking 20% to 30% premium increases at renewal, as well as increasing (often doubling) retentions, and reducing both limits and coverage. Antitrust and unfair business practices coverage has been a hot button issue for healthcare D&O insurers in recent years, as M&A activity has led to increased enforcement action - and thus the potential for significant losses. As a result, healthcare insureds are seeing this coverage removed or sub-limited at renewal, as well as subjected to a higher retention and/or coinsurance.

D&O pricing for "unicorns" (private companies with a valuation of $1 billion or more), has skyrocketed as of late, to near public company premium levels. The marketplace for such risks is also shrinking as D&O underwriting appetites have become more conservative. Of the carriers that are still willing to write D&O coverage for unicorns, some are seeking to convert coverage to public company policy forms, which results in less coverage than privately held companies are accustomed to receiving.

While not the sole driver, Securities and Exchange Commission (SEC) enforcement actions in recent years against privately held companies and their executives have contributed to the hardening private company D&O market (most notably, but not only, for unicorns). The 2018 SEC "massive fraud" complaint against Theranos, Inc., a consumer healthcare technology startup once valued at $10 billion, but now operationally defunct, provided a stark reminder for many in the D&O insurance industry that privately held companies are not exempt from federal securities law enforcement actions.

The Lucent Polymers matter emphasizes that a privately held company does not have to be highly visible or have a high valuation to be in the crosshairs of the SEC. In February 2019, the SEC brought an enforcement action against two former executives of Lucent Polymers, a shuttered Indiana-based plastics and polymers manufacturing company. The two executives allegedly concealed the company's fraudulent financial reporting practices and made misrepresentations in connection with the sale of Lucent to Citadel Plastics Holdings, later profiting substantially from the sale. These executives were separately indicted by a federal grand jury in connection with the same incidents.

The DOJ's press release about the indictments quotes an agency official as saying "Corporate officials who put deviousness over good faith degrade the integrity of our markets and impugn the reputation of American industry. This office will continue to prioritize the investigation and prosecution of corrupt corporate executives who enrich themselves through fraud and deception." The DOJ statement says nothing about the fact that Lucent was a private company.

As the Fenwick & West law firm noted in its February 2019 memo about the SEC's and the DOJ's actions, "The government's aggressive action here is a reminder that securities regulators and law enforcement agencies are increasingly scrutinizing statements

made by private companies, especially statements that create investor fervor and lead to inflated share valuations.”

With mounting evidence that the SEC will pursue private company executives for securities law violations, some underwriters are beginning to price in this potential risk.

Employment Practices Liability is an integral coverage part of a well negotiated Private Management Liability Policy. While the changes in the EPL environment have not been nearly as pronounced as those in the D&O space, there are a number of recent legislative changes which warrant discussion.

Statutory developments will continue to drive changes in Employment Practices Liability Insurance (EPLI) pricing, retentions and coverage. #MeToo laws in California, Illinois, New York and other states that mandate sexual harassment training and/or require businesses to take other steps designed to address workplace misconduct may affect EPLI carriers’ underwriting appetites.

Also, a recent development in California could set the stage for a national shift in the way independent contractors are treated as well as impact EPLI coverage. California lawmakers recently approved Assembly Bill 5, which codified the state supreme court’s 2018 decision in Dynamex Operations West, Inc. v. Superior Court[4], that companies must treat certain independent contractors as employees. The bill provides eligible “gig economy” workers with the right to minimum wage, workers’ compensation and other benefits, which, in aggregate, represent a 30% employment cost increase for the affected companies. For EPLI insurers, laws like Assembly Bill 5 could significantly impact ratable exposures (e.g., headcount), leading to higher retentions and pricing for these insureds.

Further, in September 2019, the U.S.

“

The government’s aggressive action here is a reminder that securities regulators and law enforcement agencies are increasingly scrutinizing statements made by private companies, especially statements that create investor fervor and lead to inflated share valuations."

House of Representatives passed the Forced Arbitration Injustice Repeal Act (FAIR Act), which aims to invalidate mandatory arbitration agreements and class-action waivers for employment, consumer protection, antitrust, and civil rights matters by amending the Federal Arbitration Act. Among other things, the bill prohibits companies from requiring workers and consumers to resolve legal disputes in private arbitration, a common practice that has often made it difficult for employees to pursue action against colleagues and superiors for workplace harassment. Passage of the FAIR Act would undoubtedly impact the EPLI marketplace, as workers tend to be less successful in private arbitration than in the courts. Restoring court access to millions of workers who have signed away their right to sue would likely lead to higher defense and settlement costs for companies and their EPLI carriers. As of this writing, support for the FAIR Act in the Senate and by the White House is far from certain. However, its passage in the House is a significant development, and we will be following its progression in order to assess how it may affect EPLI insureds in the future.

Although to a lesser degree than public and private company placements, we are starting to see premium increases in the not-for-profit (NFP) executive liability segment. At least one established D&O carrier is re-underwriting its entire NFP book of business, and exiting certain classes altogether. It appears that as carriers seek to address poor underwriting results - and the broader executive liability insurance marketplace hardens, no stone is being left unturned. That said, while NFP D&O business has received significantly less attention than public or private D&O business with regard to rising rates, a major industry survey reports that 63% of NFP insureds have reported a D&O claim. As such, further changes in the NFP D&O space may be on the horizon.