2023 US MANAGEMENT AND PROFESSIONAL LIABILITY MARKET OUTLOOK

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The softening of the management liability (ML) and professional liability (PL) insurance markets that started last year looks set to continue over the second half of 2023 as new entrants and increasing capacity continue to drive up competition and drive down premiums.

That's according to Manny Cho, executive vice president, Executive Lines, at Risk Placement Services (RPS), who says that the sector as a whole is very much a buyer's market.

"This year, flat is now the worst result that many people are seeing, and you might be seeing anywhere from 10% to 20% rate reductions in a number of areas," he says.

But that doesn't necessarily make it an easy market for brokers and agents to operate in, and Cho says that with price no longer being the differentiator it used to be, agents need to look at other areas to ensure they are delivering the best for their clients, while also protecting their own books of business in a shrinking market.

"Here at RPS we are very much focused on quality of cover and financial stability," he says. "With some of the issues we've seen in the sector, there's definitely a call for financial security and stability with the carriers that we're placing business with."

The market is also seeing underwriters fighting harder to find profitability, and this is in turn increasing the workload agents are faced with.

"Underwriting is getting a little tougher, with underwriters really trying to create profitability in their books of business. This means that there is going to be more underwriting questions, creating even more work to do for brokers in terms of gathering information."

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"This then means they are working harder, and many times that is just to retain 70% of their renewal base."

And for those working in the ML and PL insurance markets, there are additional pressures coming from other lines of business that are facing their own challenges, the result of which is a reduction in the overall budget available for buying insurance cover.

"The property insurance market is one example of a line of business that is proving particularly challenging for agents and their customers and, with rates rising so much in those markets, businesses are looking for ways to reduce their overall dollar spend on insurance protection," Cho says.

D&O INSURANCE

One of the lines of business that is seeing the biggest drop in premiums is Directors & Officers (D&O) insurance, particularly when it comes to public companies.

RPS Senior Vice President Rodney Choo says that the average renewal premium is coming in at a decrease between 20% and 30% of the previous year's price, a continuation of a trend that started over the second half of 2022.

One of the lines of business that is seeing the biggest drop in premiums is Directors & Officers (D&O) insurance, particularly when it comes to public companies.

"This year has really been a continuation of the soft market that started last year, and follows the really difficult period we went through between 2019 and 2021," he says. "By the end of 2021 everyone knew that the worst was over, so 2022 saw throughout the year a real acceleration of competition, and a reduction in rates across all layers for everything except the most difficult risks."

"We are back to the old days where it is truly again a buyer's market," he adds.

Companies that recently went public are seeing the largest decreases given they faced the worst conditions of all with punishingly high minimum retentions and seven-figure premiums. It is not uncommon for companies in their second or third year being public experiencing premiums drop by as much as 50% to 60% over the last 18 months.

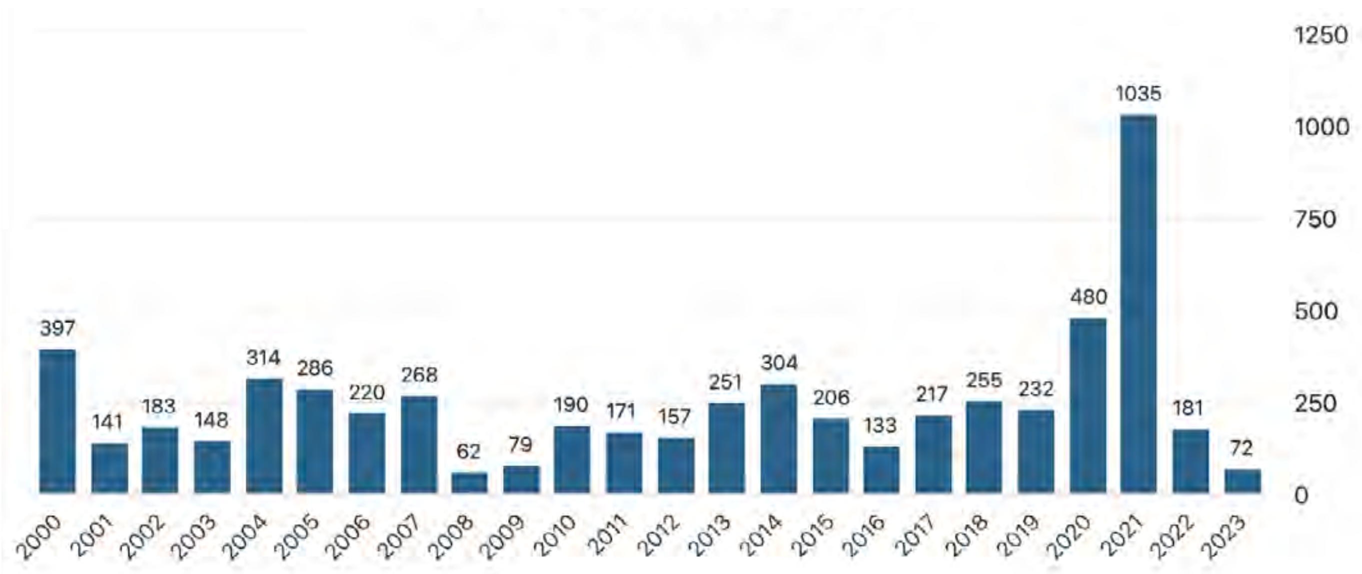
The reason for this repricing of the market has been an influx of new capacity driving competition, which has led to an increase in competition and a softening of rates for public D&O.

But Choo says there has been much more at play as well.

"What really supercharged things in 2022 was that the go-public market effectively shut down," he says. "I think most markets you're anticipating a reduction—or at least a softening—on their renewal book, but the expectation or hope is that you're going to offset that with new business from new companies going public."

"That didn't happen, and so now you have markets that are finding themselves, for the first time in recent memory in a bit of a hole, and that led to a little bit of angst when it comes to pricing and retaining their renewal books."

ANNUAL IPOs, 2000–2023



Source: https://stockanalysis.com/ipos/statistics/#

Indeed, in 2022 there were only 181 IPOs, down from a record 1,035 in 2021, and the second lowest of the last decade, with the 133 IPOs completed in 2016 the only lower annual figure over that period.

Interestingly, however, there has been little change to the coverages available, largely because the hard market between 2019 to 2021 led to steeper price hikes rather than a reduction of the terms available.

"Coverage always matters, but we didn't see wholesale changes to coverage this hard market cycle," Choo adds.

The changes seen in the public D&O market also have little to do with a changing claims environment, with Choo saying that much of the talk around the volume of claims in the sector is overhyped.

"A lot of the rhetoric around securities litigations year by year tends to be a little bit overblown," he says. "If you look at numbers between 2017 and 2019, all you heard was that it was the worst time to be a public company director, because we were having record high filings.

"While that was true—we were getting more than 400 a year—the reality is more nuanced. A high majority of those cases were merger objection M&A cases, and there was a specific reason why we saw that big jump."

A lot of this was due to a decision by the Delaware Supreme Court that made such cases more difficult to settle in state court, thus pushing them into the federal system. Recently, we've seen the reverse—with a significant drop in overall filings due in large part to a material drop in these merger objection cases, meaning that the wider claims environment for public D&O insurance has not really changed that much over that period.

"If you look at the core cases we deal with, there has not been as much fluctuation in activity as the conversations may suggest," Choo says.

For agents, all this means that winning new business is becoming harder, as everyone is able to offer a big reduction in the cost of a premium. To combat this, Choo says brokers need to concentrate on providing core value to clients that is tailored to their particular business.

"Those agents that focus primarily on price are going to struggle. Our job at RPS is to help our partners develop a more sophisticated approach to these areas where best price and quality of coverage is the baseline. It's the bare minimum. We need to bring value by helping our mutual clients understand the proper context of D&O insurance by focusing on broader issues, such as corporate indemnification, practical litigation risk and what concerns are driving them to buy the insurance in the first place," he says. "Our approach at RPS is to make sure that the coverage on offer is a rational solution to the risk that is being presented."

Meanwhile, conditions are similar in the private company D&O market, just on a more muted level, with a softer market ranging from flat premiums to a 5% to 10% reduction at renewal.

RPS Area Senior Vice President Bryan Dobes says this has a lot to do with the easing of market conditions following the spike during the COVID-19 pandemic.

"There was a stretch during the COVID-19 pandemic where we saw a sharp tightening of underwriting guidelines and rate increases that we had not seen since 2008," he says. "A lot of hardening and tightening of the market during that time was due to the financial and economic uncertainty, but over the last 12 to 18 months those concerns have largely faded. Thanks to more than a dozen new entrants, additional capacity has helped drive competition up and rates down."

Many of these new entrants have followed the cyber insurtech model with wholesale heavy distribution, and Dobes says this has brought additional speed for brokers operating in the private company D&O market.

"These new entrants often have the capability to quote and bind online in a matter of hours or minutes, and this gives brokers many avenues to garner competitive quotes without the need for a traditional submission to an underwriter," he says.

But with claims frequency and traditional underwriting standards still at historically elevated levels, Dobes warns that agents need to be wary of policies that don't have sufficient levels of cover or with embedded restrictions—and that expert or specialist advice is crucial.

In the closely connected employment practices liability (EPL) sector, rates have steadied after a turbulent period that tailed off during 2022.

"Some of the traditional players have serious deficiencies when it comes to some of the more nuanced coverages," Dobes says. "Most carriers are not offering the broadest suite of coverage that they can and, despite many broker-specific endorsements, carriers are still limiting the coverage in a number of ways, whether that be embedded exclusions for anti-trust or explicit industry-specific exclusions to limit key exposures."

"It is here that companies like RPS can help, by providing specialty knowledge to help with negotiations and ensure that adequate levels of protection are being secured under the terms of the policy."

EMPLOYMENT PRACTICES LIABILITY

In the closely connected employment practices liability (EPL) sector, rates have steadied after a turbulent period that tailed off during 2022.

RPS Area Senior Vice President Dave Tardif says that while EPL rates had been decreasing over the course of 2022, premiums have since stabilized, and most renewals without a difficult claims history are now seeing flat rates at renewal.

There are, however, still some challenging areas of the market, with businesses in areas like New York and Florida—as well as those operating in the healthcare sector—still facing tough market conditions and rising renewal rates.

"We are still seeing different levels of retention in certain geographies," Tardif adds, "and if you're an entity with high wage earners, you are going to see that there would be a separate retention for those high earners."

"So there is a little bit of volatility in the market still, depending on those particular characteristics, but overall the EPL market has stabilized from the hard market cycle from 2019 through 2021."

But while the market continues to struggle with claims inflation and a difficult economic landscape that is creating challenging trading conditions for clients, Tardif says that insurers are once again fighting for growth after tightening their risk appetite in the immediate aftermath of the pandemic.

"COVID-19 created a lot of unknowns from a risk perspective, and insurers were wary of that," he says. "This means that many insurers reduced their risk appetite drastically, so whereas you might've had 10 capacity providers quoting for a risk in a particular industry, such as hospitality, that dropped to just one or two—and those were left to do what they wanted with price because there was no competition."

"This led to the rise in rates that were felt across the market, but insurers got used to the increased levels of premiums they were bringing in. Now, they are all facing the usual growth targets, so they are all actively going after this business—and the effect of that is it is driving down costs."

And Tardif says agents also need to be aware of the impact a changing headcount has on the cost of a policy, particularly in the current economy where layoffs are becoming more frequent.

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"While the exposure from an employee count perspective may be reduced following a layoff, the claims potential is still there," he says. "So even if your customer had 1,000 employees and it goes down to 750, the reasonable exposures are 750, but the 250 employees who were let go are the ones who are most likely to file suit."

"So that factors into the pricing, and you'll see that insurance companies are going to underwrite more stringently to a company that has either laid off employees recently or plans to do so in the future."

Everyone saw a significant drop in ransomware attacks last year, but it has started to pick up again.

CYBER INSURANCE

Cyber insurance is another line of business that is entering into a softer market, with premiums falling as a result of a more benign claims environment.

"Last year most carriers reported very positive loss ratios that have demonstrated great improvements compared to previous years, so that has made the market very competitive," Cho says. "For small to middle-market accounts, we are seeing premium reductions of up to 15%, and a lot of this softening of rates is down to a fall in ransomware claims."

Some in the market say that this drop in claims from ransomware attacks is attributable to the conflict in Ukraine, with a lot of the bad actors occupied elsewhere and not focusing their efforts on ransomware attacks against businesses.

Cho, however, is wary that the impact of this could be short lived.

"Everyone saw a significant drop in ransomware attacks last year, but it has started to pick up again," he says. "We are keeping an eye on this—and so are the carriers—and any increase in attacks could start to impact the market later this year."

The market is also struggling to come to terms with changes in coverage that have led to new definitions of what war means—and how that affects any limits or exclusions.

Cho says that the important thing is for agents to seek advice should they find a new wording they are not 100% comfortable with.

"There's been a number of carriers, starting in Lloyd's, that have developed new exclusions that we are reviewing, and some US carriers are also looking to amend their existing exclusions following that move," he says. "Part of our job at RPS is to make sure that we have proven they are not taking away from cover for typical ransomware attacks and that carriers are not trying to hide these claims under exclusions for war or silent war events that aren't typically covered under a policy."

FIDUCIARY LINES

The fiduciary lines sector has traditionally been a relatively forgotten part of the management liability market, with big limits given for very little premium. But RPS Area Vice President Jack Rosen says that has definitely changed on the back of a changing claims landscape.

"Fiduciary lines used to be a commonly overlooked coverage, with large limits and first-dollar coverage for relatively low premium amounts," he says. "But that has now changed as we've seen some large plans hit very hard by excessive fee litigation—last year alone there were 88 excessive fee claims filed—and we've seen a substantial trend in litigation against these large plans, but there are only so many large plans out there."

"This means that plaintiff attorneys are looking downstream for smaller plans, and we are now seeing plans over $100 million and even below that figure being targeted by these class-action lawsuits, which are very costly to defend."

This in turn means that insurers had to push up rates and tighten coverage.

"A coverage that used to be a throw-in is now facing substantial litigation and, as claims frequency goes up, so do rates," Rosen says. "Insurers are now rating for this increased exposure, and they are also introducing special retentions for class-action suits or specifically for excessive fee litigation."

"These could range anywhere from $50,000 for smaller plans to as high as $10 million for very large plans that have not been de-risked," he adds.

The market has started to soften as we move through 2023, however, with Rosen citing new entrants and increased competition as one of the drivers.

"I am seeing certain new entrants who are lowering retention for large plans," he says. "They are still seven-figure sums—but instead of, say, a $2.5 million retention, it is coming in at $1 million or $1.5 million."

"They are also offering a slightly reduced premium as well," he adds.

And Rosen says the secret to success in such a market is educating the customer, in a similar way to how cyber insurance has had to use education in order to secure better coverages.

"You need to educate these plans that they need to be proactive and they need to document everything," he says. "They can't just move along on autopilot as scenarios change or fund sizes grow; they need to be proactive and make sure that any decisions that are made are explained and recorded appropriately.

"A lot of claims we are seeing today are from actions that have happened in the past, and we need to make sure that today's actions don't result in similar claims in the future."

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ARCHITECTS AND ENGINEERS

The architects and engineers (A&E) sector has followed a similar path to the wider ML and PL market, having settled down following a period of market hardening.

And while rates may not be falling—with most renewals coming in at a flat rate compared to the previous year—RPS Senior Vice President Ron Kiefer describes the sector as robust with carriers eager to write business.

"I am seeing underwriters being more aggressive on opportunities in the market," he says. "Rates are becoming much more stable—I'm certainly not seeing any rate increases at the moment—and there are good terms available without any issues around coverage restrictions that would be outside of the norm."

But Kiefer says that, while he believes we are very much in a buyer's market at the moment, agents are still facing challenges and won't be able to get everything they want when negotiating terms.

"The majority of carriers are still limiting the amount of capacity that they will put up for any one firm," he says. "Whereas in the past you might have readily been able to get $5 million and $10 million limits, now that is more like $3 million to $5 million with most carriers, and you are having to build excess layers on top of that to get appropriate levels of cover."

A lot of this is down to the rising cost of claims, with social inflation having increased some large claims by as much as three to five times the levels seen a decade ago.

Agents can't be complacent given the current state of the A&E market, and they can't rely on the market to provide the solution.

"The claim settlements seen today are at multiples of the levels that would have been expected even accounting for inflation," Kiefer says. "So while underwriters are happy to offer favorable terms, they still want to cap that top level of risk."

For agents, Kiefer says this means they have to be much more proactive in the market, and they can't solely rely on the traditional relationships that have worked for them in the past.

"Agents can't be complacent given the current state of the A&E market, and they can't rely on the market to provide the solution," he says. "Put simply, they can't rely on the handful of markets that they've traditionally done business with, because that isn't enough anymore."

"That is why as a wholesaler we love working with agents because we have access to a broader market and a greater number of markets that can be drawn on to get the right level of cover, under the right terms and at the right price."

PARTNERSHIPS ARE KEY

Ultimately, Cho says that the ML and PL market as a whole is still a challenging sector for agents to operate in, even if affordable cover is not hard to come by and customers are happy with the rates they are being presented with.

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"Almost every market we operate in is in a very competitive market situation, with high levels of capacity, and good rates and good terms and conditions available," he says. "This is good for financial stability and good for the customer, but it does mean that renewals are being kept at 80 cents for every dollar made the previous year."

"This makes it a difficult market for brokers, and it is in times like these that partnerships come into their own. We want to work with our agents to help them set the right expectations for the customer and get the information we need so that we can get them covered under the best terms available."

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