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D&O Insurance for Non-U.S. Domiciled/ U.S. Traded Companies in 2021

A Year at a Glance

February 2022

1 A Year at a Glance

U.S.-listed companies domiciled outside the U.S. are subject to a higher litigation risk than their non-U.S. listed peers. Such a notion has been particularly tangible in recent years, as these companies have attracted an unprecedented number of claims and have caught the D&O underwriter community's attention.

In 2020, the rapidly deteriorating claims environment, compounded with the increased volatility created by the coronavirus (COVID-19) pandemic, translated into a striking capacity shortage and massive premium corrections for this class of insureds, leading to significant concerns and challenges for their directors and officers.

While fully engaged in supporting our clients in complex D&O transactions during this testing time, Aon FSG Teams in the U.S. and the U.K. have been dedicating energy and resources to collect and analyze D&O placement parameters.

Not only do data and analytics enable us to hone our capabilities and obtain the best for our clients in challenging times, but they also cater to the needs of increasingly sophisticated and data-hungry insureds.

The D&O Commercial Team with the Global Broking Centre placed some 46 and 35 D&O programs in 2020 and 2021, respectively. While the statistical value of this data pool can be limited, it is possible to draw several meaningful insights, which we share in this brief.

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Evolution in the Litigation Landscape

As reported in "Cornerstone Research I Securities Class Action Filings - Year in Review", the year 2021 has seen a relative decrease of securities class actions (SCAs) filed against non-U.S. issuers.

The number of core federal filings against non-U.S. issuers fell to 41, significantly down from its record high of 74 in 2020. As a percentage of total core federal filings, filings against non-U.S. issuers decreased from 34 percent in 2020 to 21 percent in 2021. This represents a reversion back to the average value of 2012-2019.

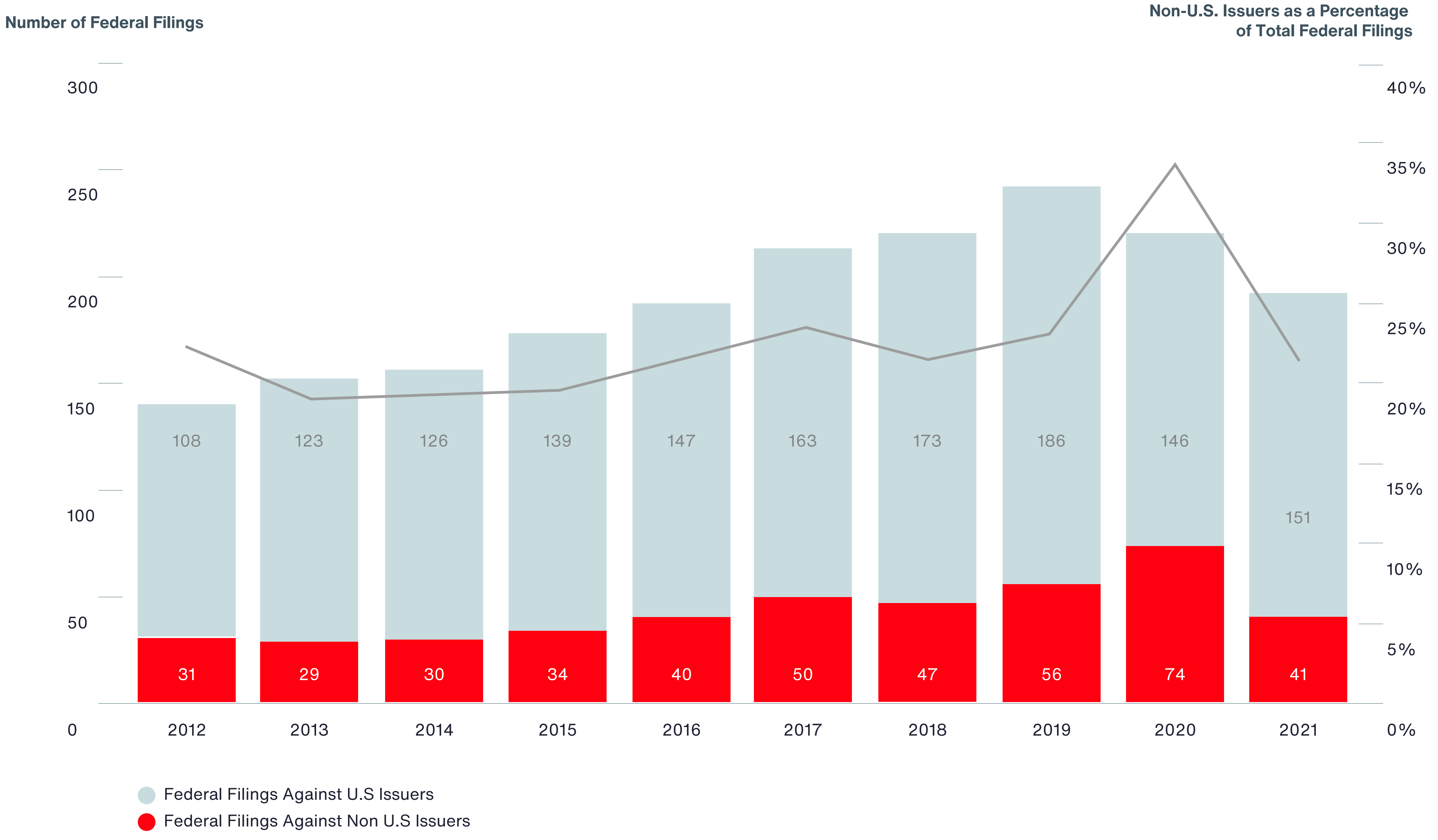
However, those numbers should be considered in the context of the broader upwards trend of filings over the last 10 years.

U.S. securities litigation risk remains a key threat to which no type of business is immune – SCAs touch a wide range of industries and geographies. Furthermore, while SCA filings may be down, settlement amounts continue to climb, evidenced recently by Luckin Coffee Inc.'s settlement of $175m. As such, directors and officers must take proactive measures to mitigate risks.

In addition to SCAs, U.S derivative claims against non-U.S. companies and SCAs have been a central topic in recent years. Recent developments for non-U.S. companies with U.S. shareholders, comprehensively covered in Ed Smerdon's article: "U.S. D&O Claims Against Non-U.S. Companies, a Happier New Year?", hint to a less dangerous future in U.S. courts of law for companies, at least as far as they do not actively cater to U.S. investors.

Annual Number of Class Action Filings by Location of Headquarter

Core Federal Filing 2012-2021



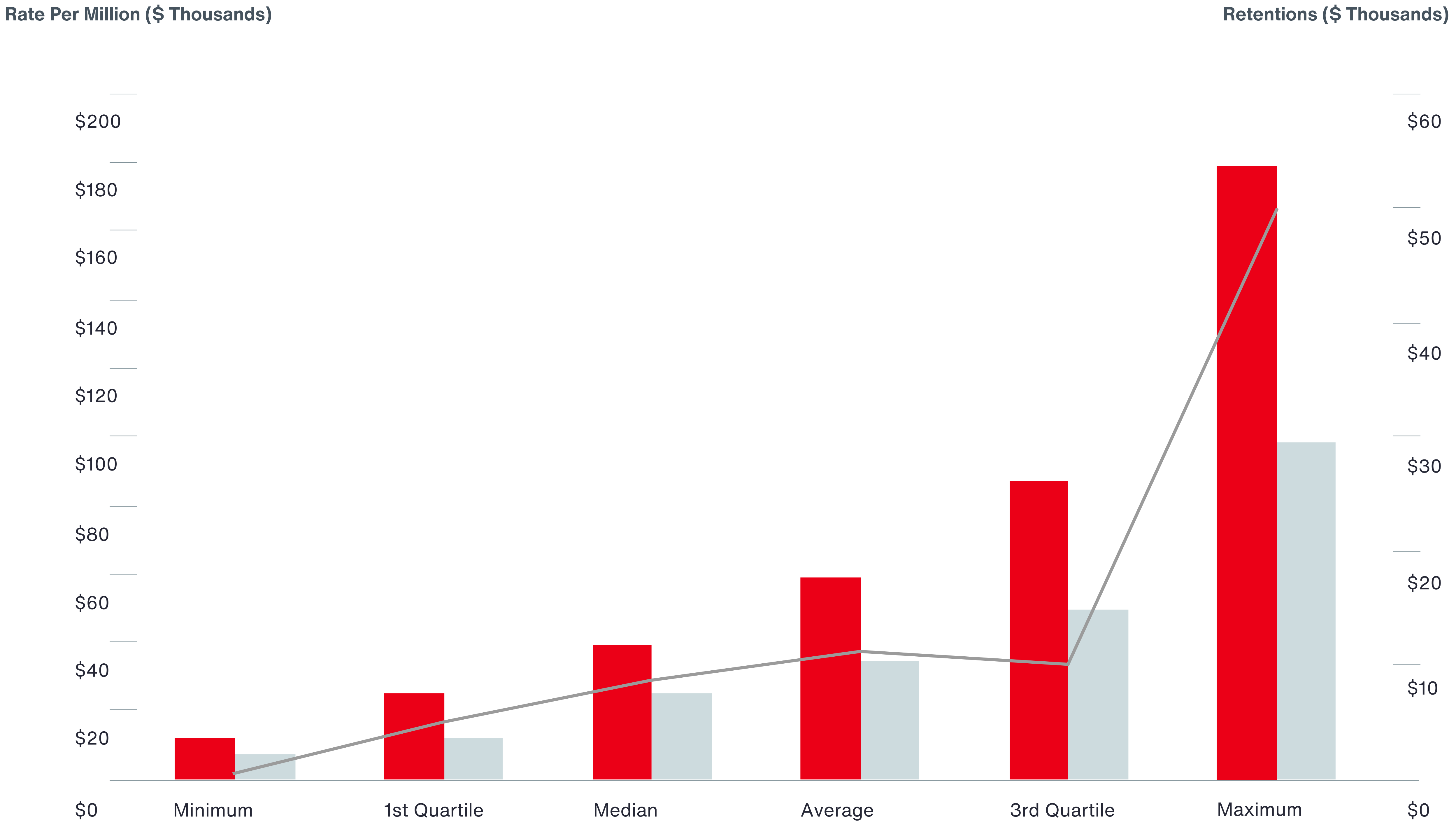
Source: Cornerstone Research. Securities Class Action Filings 2021- Year in Review

D&O Insurance

3 Rate Evolution

Directors & Officers Liability

Total Pricing and Retentions (inc Side-A)



	Minimum	1st Quartile	Median	Average	3rd Quartile	Maximum
Total PPM	$12,039	$25,467	$39,300	$58,554	$87,117	$179,167
Side- A PPM	$7,070	$12,158	$24,884	$34,773	$49,549	$98,000
Retentions	$500,000	$5,000,000	$8,750,000	$11,118,421	$10,000,000	$50,000,000

Total Sample: 42 Percent Purchasing Side-A: 95% Side-A Sample: 40

Source: Aon FSG 2021 and 2020 Foreign Domiciled - US Traded Pricing Benchmarking

The starting point of our analysis was a detailed snapshot of the rates observed in 2021.

The statistical analysis showed that the median total programme cost, expressed as rate-per-million, was 4 percent, whereas the median Side A coverage cost was 2.5 percent.

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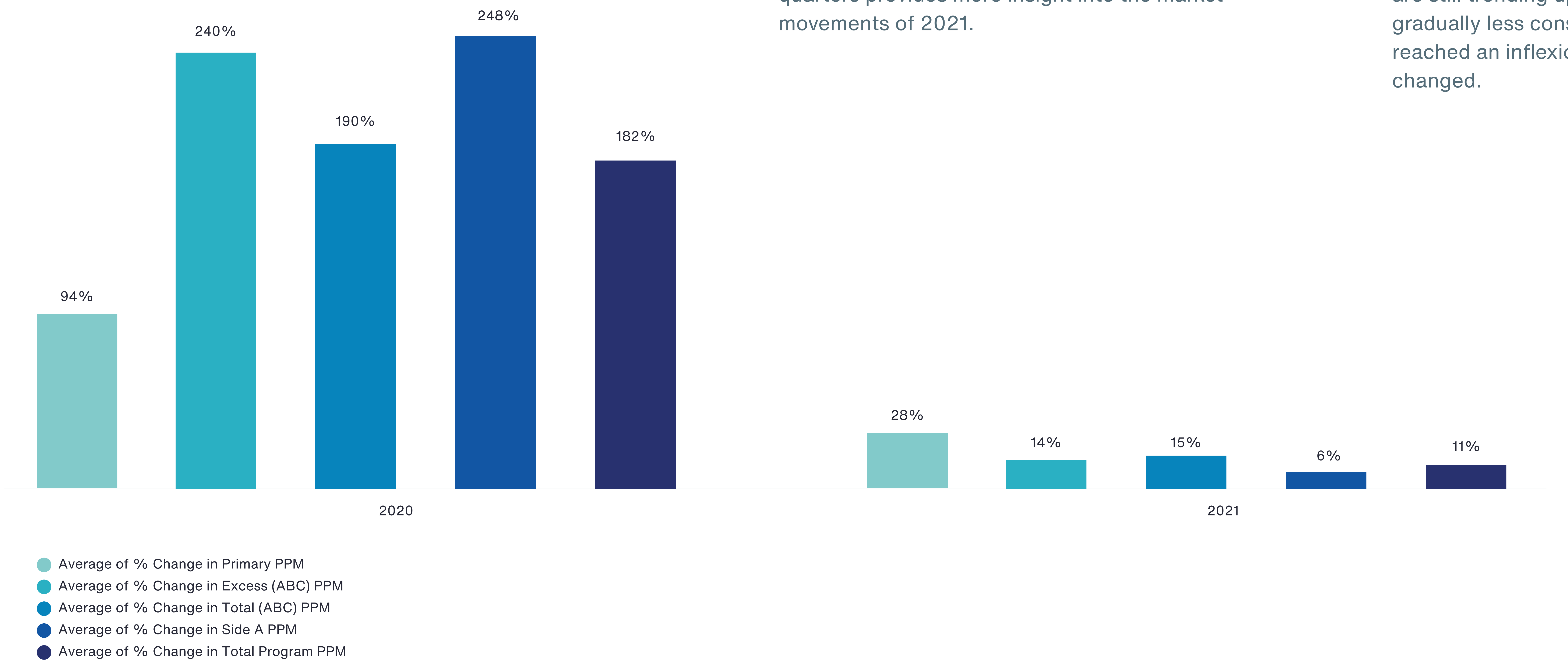
2020 vs. 2021 Average PPM % Change



PPM = Price Per Million

Source: Aon FSG 2021 and 2020 Foreign Domiciled - US Traded Pricing Benchmarking

The main focus of our work was the kinetic analysis, or how rates evolved throughout 2021, compared to the previous year.

In general, the rate corrections observed in 2021, with overall averages in the low single-digits, appear to be a far cry from the unprecedented triple-digit rate increases that occurred in 2020.

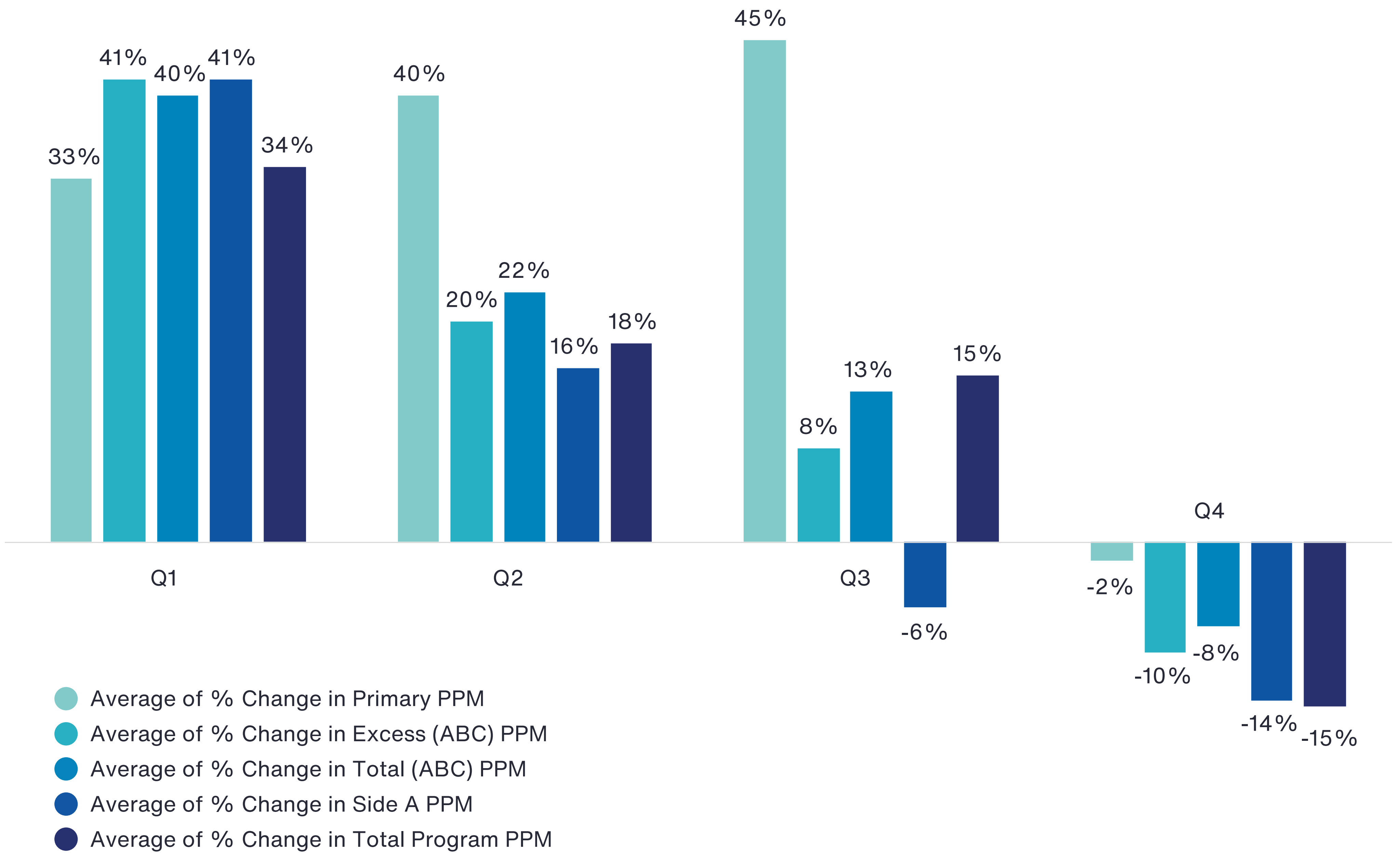
However, breaking down the rate variations across quarters provides more insight into the market movements of 2021.

In fact, during the first three quarters of the year, the rate trend is still upwards, albeit with meaningful differences between the behaviour of primary and excess layers.

At primary level, the average rate increase seems to be quite stable in the first nine months of the year, with values close to 40%.

The excess Side ABC and the Side A rate variations are still trending upwards. Yet the increases become gradually less conspicuous – as if the rate curve has reached an inflexion point, and its convexity has changed.

2021 Quarterly YoY Average PPM % Change



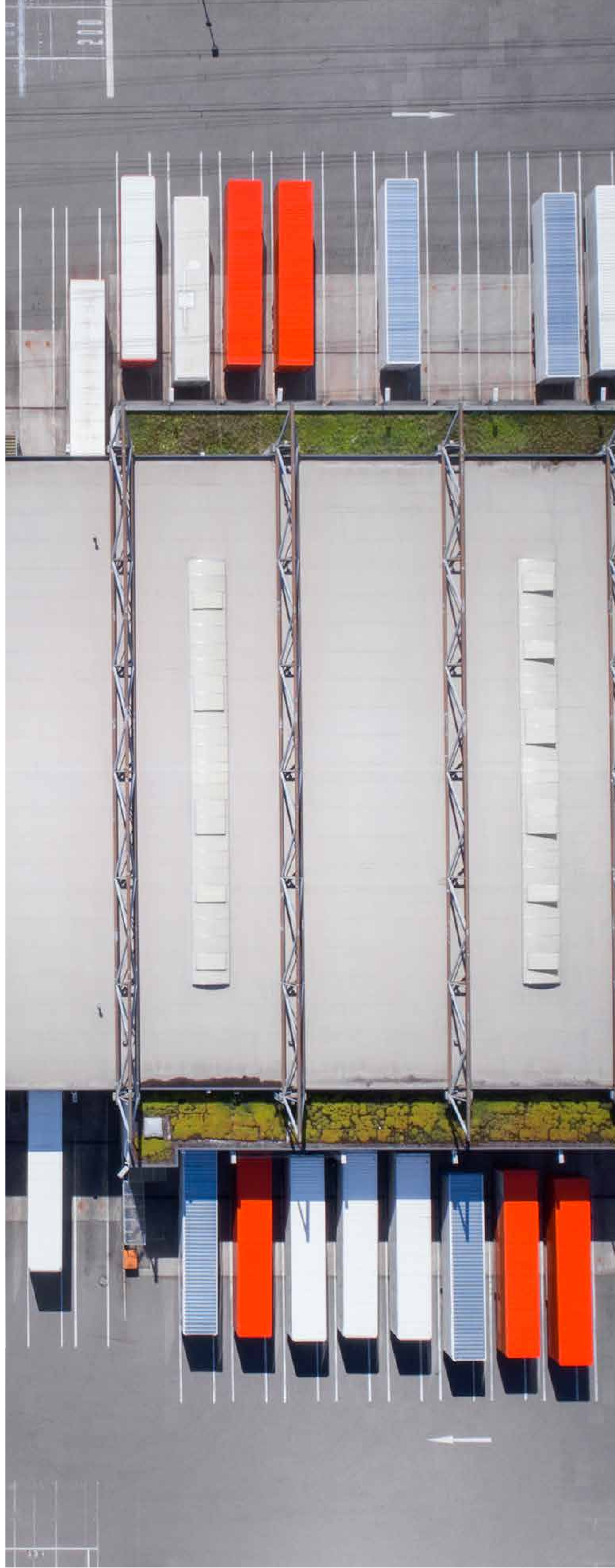
Source: Aon FSG 2021 and 2020 Foreign Domiciled - US Traded Pricing Benchmarking

Q4 seems to bring a more decisive change of pace. At primary level there is an evident stabilization of the rates, meaning that, on average, the primary renewed flat.

A low double-digit average decrease is observable at excess level, both for excess ABC and Side A, meaning discounts in the 10-15 percent region. Once again, the rate movement of excess layers is magnified at the market turning points.

By comparison, in 2020 the excess layer rates were increasing on average by triple digits (+250 percent), considerably faster than the average 94% of the primary. The excess rates were catching up with primaries, leading to higher and sometimes inverted increased limit factors (ILF) after a year of depressed ILFs.

One possible explanation for the excess layer rates' distinct evolution in 2021 is the influx of new capacity that first became available during Q2 and came to fruition towards the back end of the year – carriers such as Tegron, IQUW, Inigo, SCOR and others. The net effect has been to bring "liquidity" to the excess layer marketplace, conducive of competitive pressure to both the excess ABC and Side A.



At primary level the number of the key players, net of substitutions, remains stable overall, as outlined below.

We also investigated the parameters influencing the rate change impact upon companies. Insureds with lower primary (or total programme) rates (expressed in premium per million – PPM) tended to be subject to higher-than-average increases and more outcome variability than companies with an already high PPM.

	Average	Standard Deviation
% Change in Total Programme PPM (Expiring <50,000PPM)	19%	31%
% Change in Total Programme PPM (Expiring >50,000PPM)	3.5%	20.6%
% Change in Primary PPM (Expiring <50,000PPM)	76.3%	82.6%
% Change in Primary PPM (Expiring >50,000PPM)	11.1%	15%

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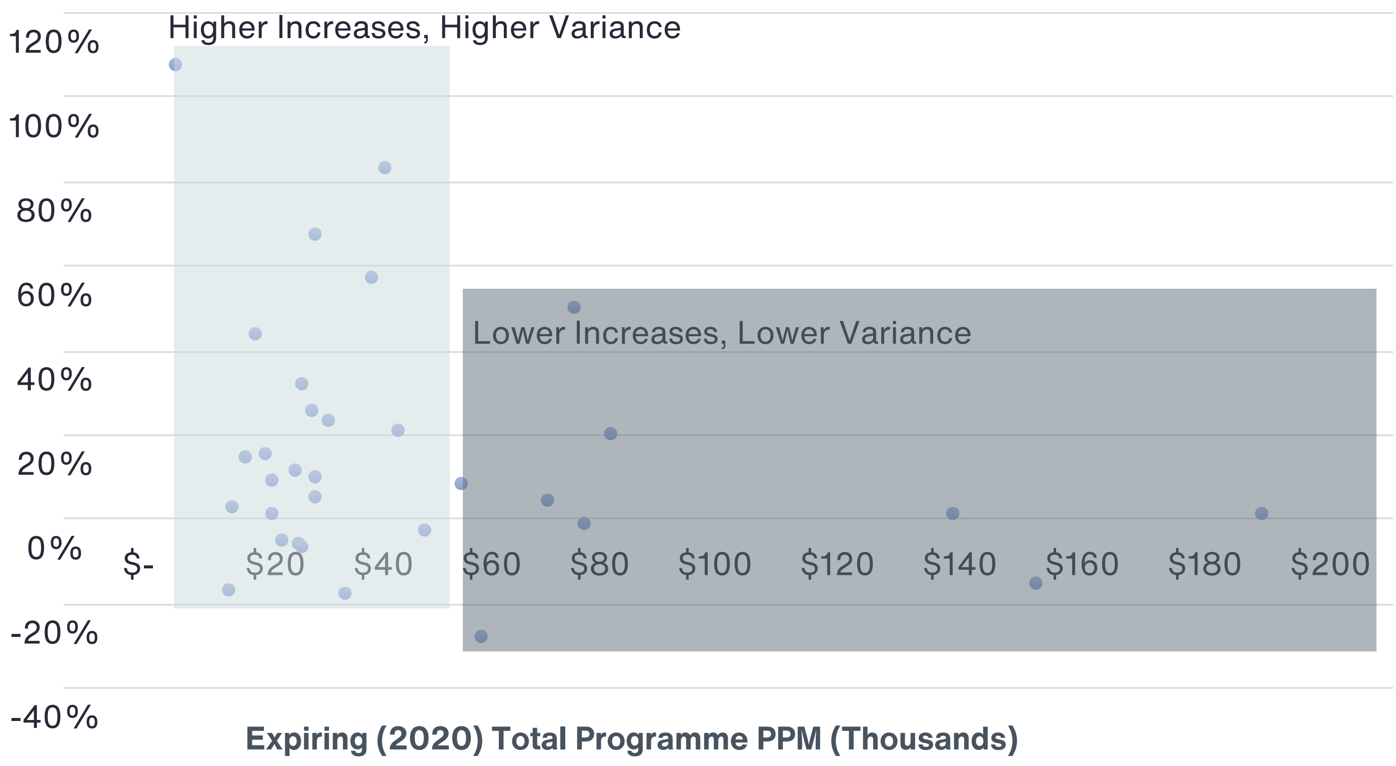
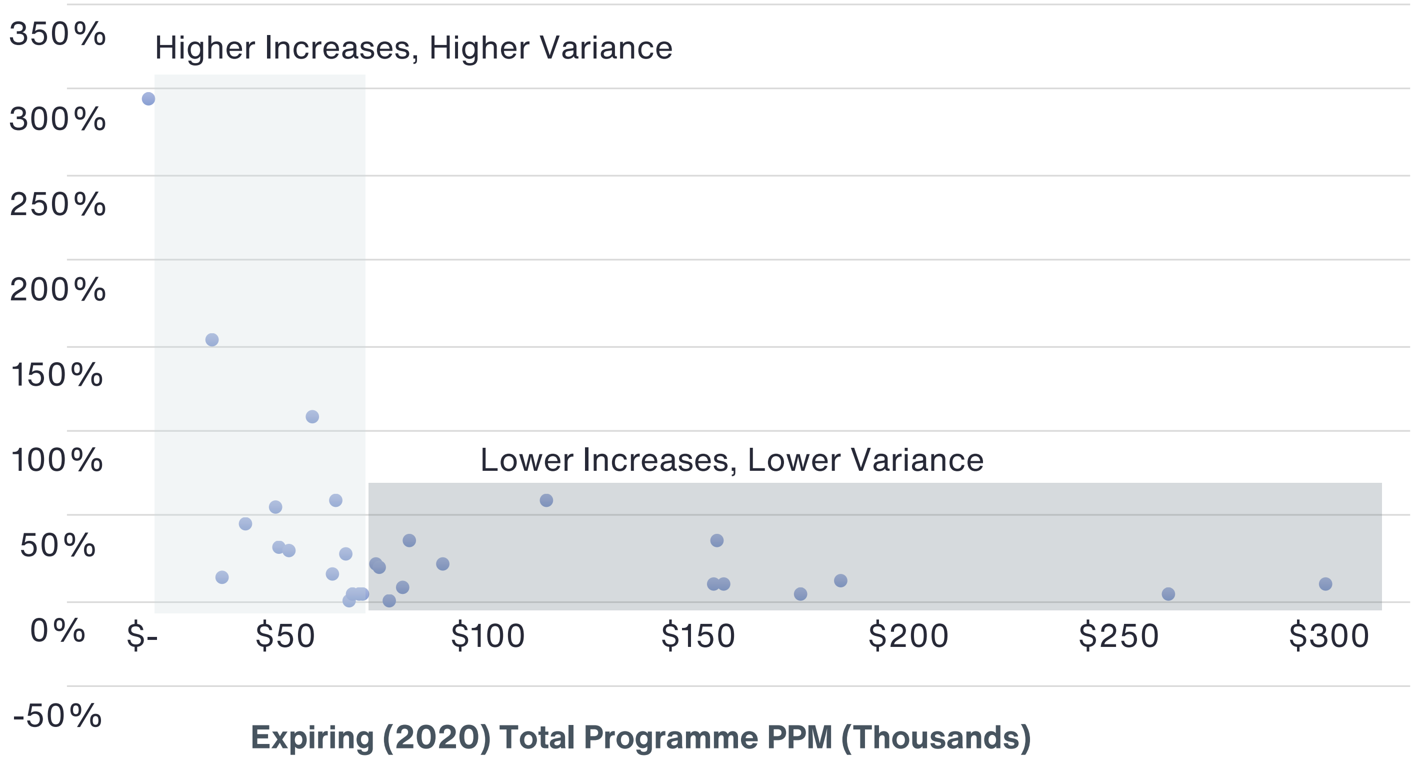
% Change in Total Programme PPM in 2021



Source: Aon FSG 2021 and 2020 Foreign Domiciled - US Traded Pricing Benchmarking

% Change in Primary PPM in 2021



Source: Aon FSG 2021 and 2020 Foreign Domiciled - US Traded Pricing Benchmarking

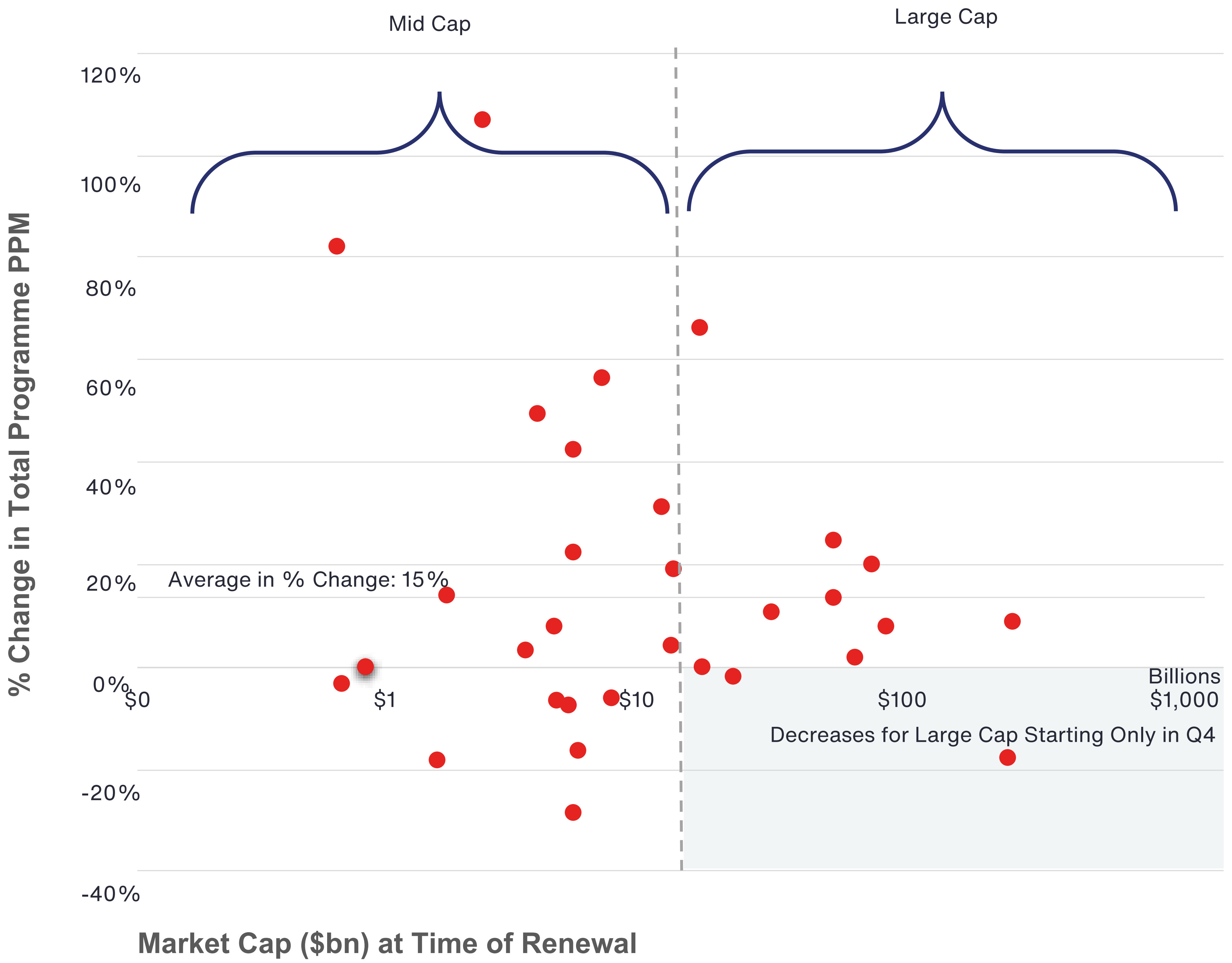
We observed similar behaviour when mapping the rate changes versus the company market cap. This is understandable as large-cap, i.e., companies with market capitalization above $10 billion, tend to command higher PPM.

In short, smaller companies suffered more violent correction with wider outcome variance in 2021. On the other hand, large-cap companies already paying substantial premiums faced more rate stability at renewals.

As such, the rate changes of large-cap tended to be slower. While 66 percent of mid-cap suffered rates increases in 2021, we also noticed that most of the 34 percent rate reductions occurred in the second half of the year. Furthermore, the first-rate decrease for large-cap did not occur before Q4.

U.S. traded / non-U.S. Companies 2021

% change in total programme PPM 2021



Source: Aon FSG 2021 and 2020 Foreign Domiciled - US Traded Pricing Benchmarking

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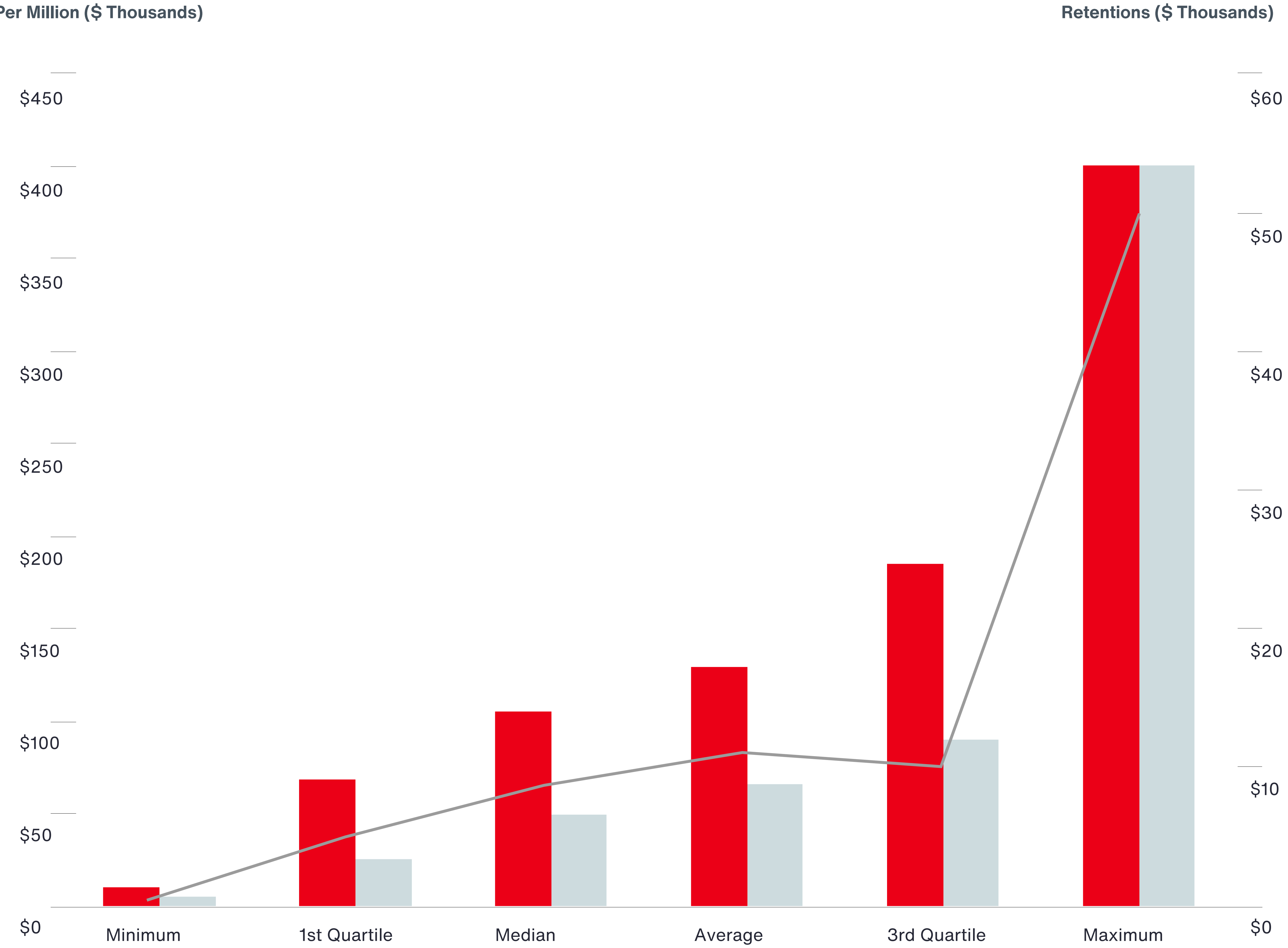
Programme Limits and Market Capacity

Directors & Officers Liability

Total Limits and Retentions (inc Side-A)



	Minimum	1st Quartile	Median	Average	3rd Quartile	Maximum
Total PPM	$10,000,000	$68,750,000	$105,000,000	$129,761,905	$185,000,000	$400,000,000
Side- A PPM	$5,000,000	$25,000,000	$50,000,000	$65,875,000	$90,000,000	$400,000,000
Retentions	$500,000	$5,000,000	$8,750,000	$11,118,421	$10,000,000	$50,000,000

Total Sample: 42 Percent Purchasing Side-A: 95% Side-A Sample: 40

Source: Aon FSG 2021 and 2020 Foreign Domiciled - US Traded Pricing Benchmarking

We have investigated the programme limits extensively, as almost all (95%) of our client population purchase Side A DIC in addition to ABC coverage.

Total Limit YoY Variations

	Minimum	1st Quartile	Median	Average	3rd Quartile	Maximum
Series 1	-50%	0	0%	-1.8%	0	66.7%

Source: Aon FSG 2021 and 2020 Foreign Domiciled - US Traded Pricing Benchmarking

In 2021 we placed $4.38 billion in capacity at renewal for clients, down from $4.5 billion placed in 2020.

Some 75 percent of clients monitored have renewed the expiring limit, whereas only five (15 percent) renewed a smaller limit. For those, the average limit reduction was 30.7 percent.

Three clients (9 percent) renewed a limit higher than expiring, on average increasing it by 31.5 percent.

On the left suggests that the capacity crunch, observed for a few months in 2020, vanished in 2021.

In summary, the market was, in general, perfectly capable of providing capacity in 2021. While rates increased, the decisions on program size were mainly driven by insured demand and budget, not by supply.

Finally, although the average total limit of indemnity remained unchanged, the ABC coverage limit was reduced by 10.75 percent, increasing the Side A portion of the towers. The most probable cause for this was clients attempting to make some marginal savings on the program's overall cost.

The observed 7 percent increase in retention for clients who purchased ABC coverage in 2020 & 2021 probably has a similar motivation behind it.

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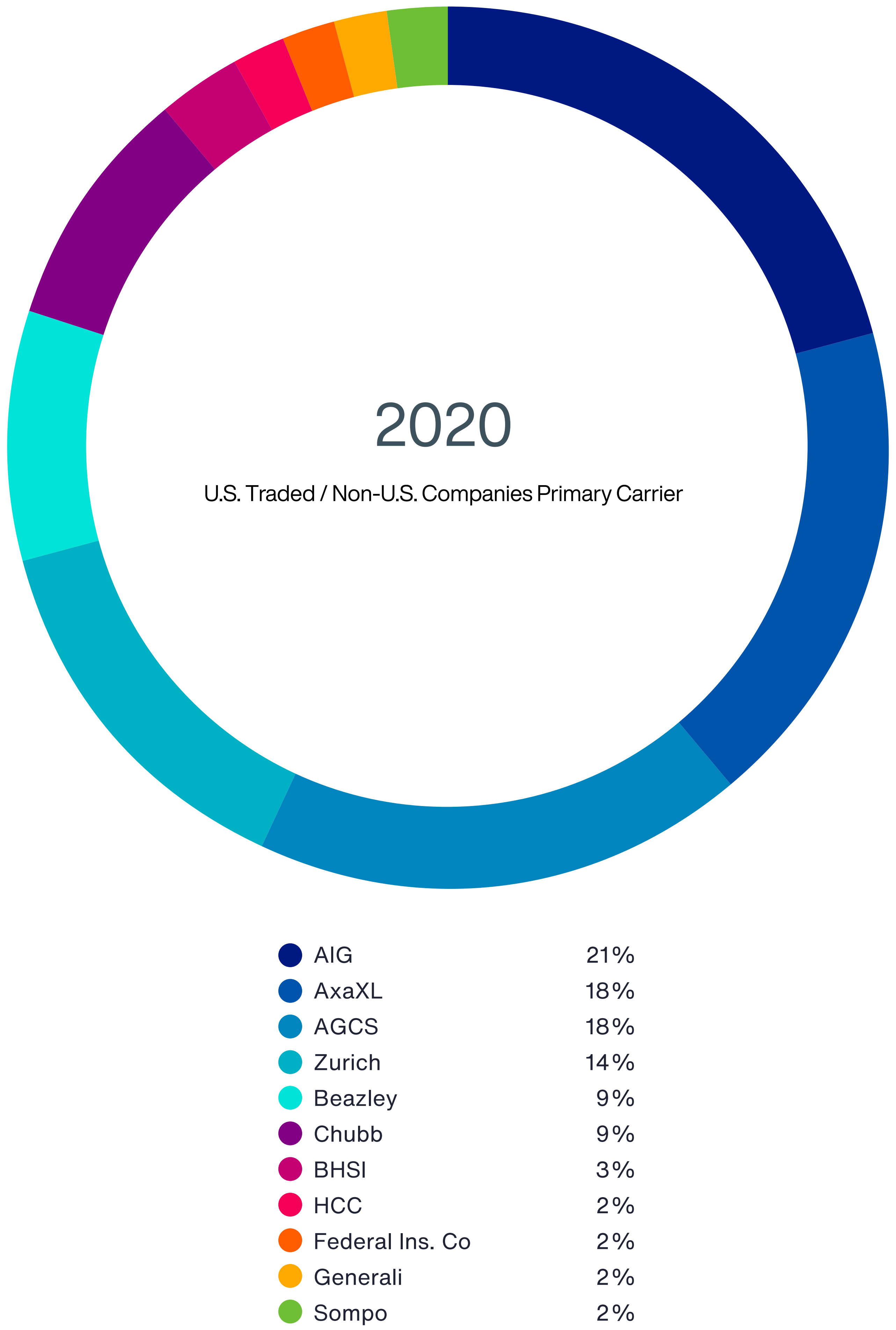
Who are the Primary Carriers?

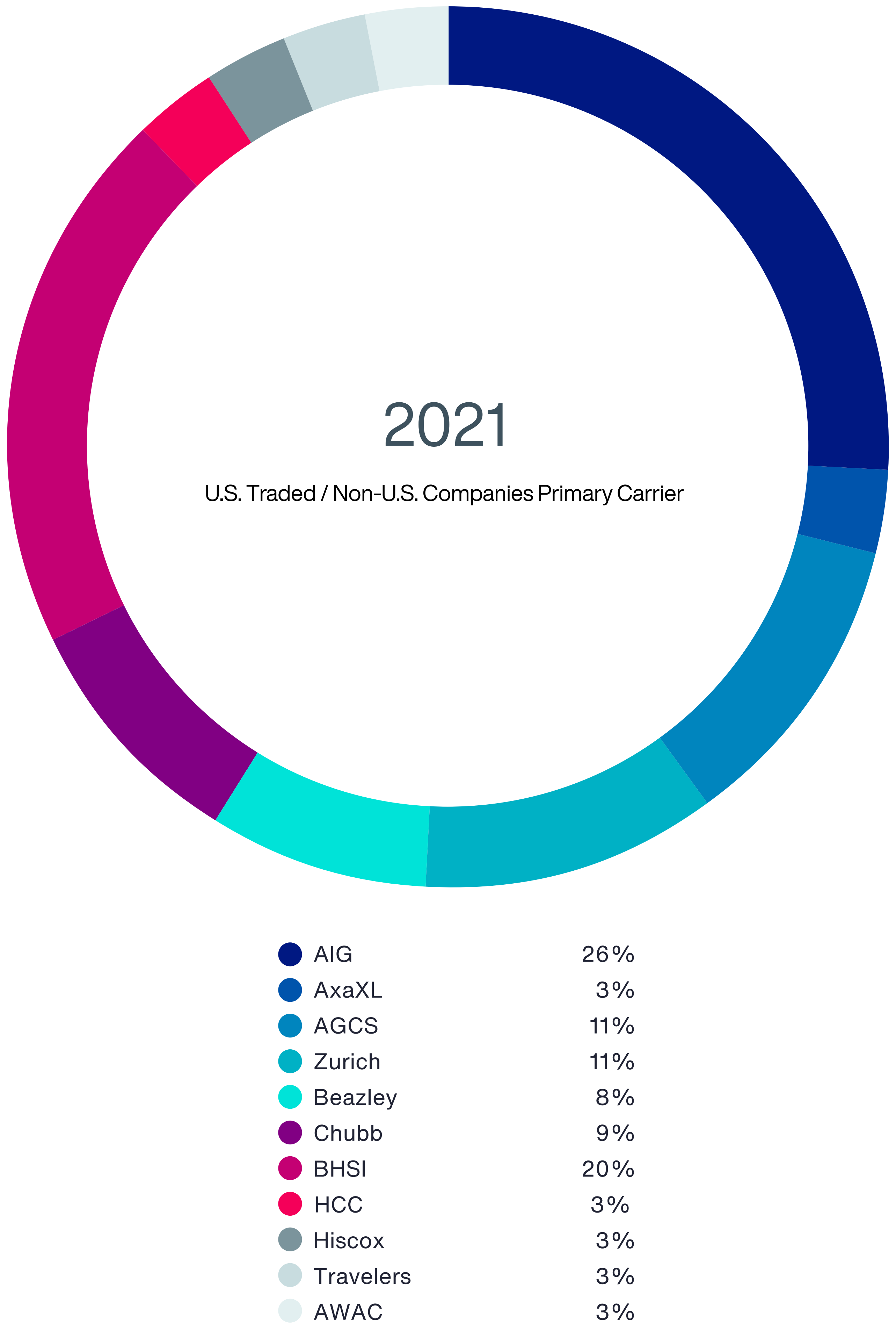
The effect of the hardened market and concern for the increased number of claims (and future claims) has made the challenge of engaging and retaining new primary players very difficult.

All insurers are managing their exposure carefully, some have exited the market altogether. In 2020 AIG, AGCS and Zurich, in this order, were the top three primary carriers for U.S.-traded non-U.S. companies. Those carriers appear to have broadly maintained their respective market shares in 2021, whilst AXA XL completed its withdrawal from the primary market.

Berkshire Hathaway Specialty stepped up considerably from its position in 2020, capitalizing on the opportunities to become a primary player second only to AIG in our sample.

Beazley and Chubb persist in the top six, just shy of 10 percent market share, confirming a consistent, disciplined underwriting approach.





Source: Aon FSG 2021 and 2020 Foreign Domiciled - US Traded Pricing Benchmarking

6 Conclusions

While there are signals that the litigation landscape is becoming less hostile for U.S.-listed non-U.S. companies, directors and officers should keep monitoring carefully and take proactive measures to mitigate risks.

Rates seem to have stabilized starting from Q4 2021; competitive pressure brought by fresh capacity mean premium reductions are still possible, at least at excess level.

It is reasonable to expect the inversion to continue in the first months of 2022, if not at primary, then at excess level.

The overall available capacity seems sufficient to cater to client demand regarding their programme total limits.

The pool of primary insurers for this class remains limited and generally stable, but with the notable substitution of AXA XL with Berkshire Hathaway Specialty.

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About

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