

William H. Connolly & Co.

Insurance & Risk Management

Retrenchment in Directors and Officers Liability Insurance Marketplace

Carmel Loughman, Senior Account Executive

Enron, Tyco, WorldCom, Arthur Anderson, Global Crossings are infamous names now, known to even casual readers of the business press. Headlines describe enormous shareholder losses, massive employee layoffs, and the extreme loss of value of pension and 401(k) plans.

Mismanagement by executives, poor counsel from outside lawyers and investment advisors, misunderstandings of board members and sheer personal greed of certain executives led to the well-known decline of these once heralded companies. What remains in our minds are news images of accountants, chief financial officers and even board chairmen trying to explain the Byzantine structure of questionable deals in which they participated and/or of which they approved.

These issues of corporate governance malfeasance have led to a rise in the number of lawsuits against corporate directors and officers. Shareholders have turned to lawsuits as a means of recouping some of their losses. The average size of settlements in securities lawsuits has increased dramatically from \$6.9 million in 1996 to \$16 million in 2001 and \$20 million in 2002.

Directors and Officers Liability insurance is designed to protect the personal assets of persons who serve in these corporate positions. However, as a result of the dramatic rise in the number and cost of claims, insurers are scaling back on the coverage provided under Directors and Officers Liability insurance policies. Insurers are reducing policy limits, requiring higher deductibles or self-insured retentions, and increasing the premium charged for this coverage. Insurers are also declining to insure or renew companies in undesirable classes of business.

WHAT THIS MEANS TO YOU

As a financial manager of an insured corporation you should be prepared for dramatic price increases for Directors and Officers Liability coverage. You should consider your company's ability to absorb higher deductible levels and recognize that coverage terms may be more restrictive. You may have more difficulty finding outside directors to serve on your board unless they are satisfied that their personal assets are fully protected.

Personal D&O Coverage for Independent Directors

The major insurers of corporate directors and officers are now offering a new insurance policy to protect the personal assets of independent directors serving on corporate boards in the event they are sued by shareholders or other third-parties.

Coverage is provided under a stand-alone policy specifically written for an individual director who serves on one or several boards. Coverage is designed to respond to a loss where the director is not otherwise covered by the corporate indemnification or insurance policy of the board on which he serves. There are various prerequisites to be eligible for this coverage that vary by carrier.

This personal coverage is intended to address the independent board member's or potential board member's concerns over D&O exposures and coverage issues that might lead to such a person's reluctance to serve on a board in the current environment.



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Would Your Insurance Pay for Rebuilding Your Home?

Elaine Kane, Director
Personal Insurance

The *New York Times* ran a story last March that could send chills down the spine of any homeowner.

Reporter Susan Garland wrote about a California couple who lost their 2,250 square foot home to a wildfire. When they filed their insurance claim, they found out that their homeowners insurance did not cover the full cost of rebuilding their home.

The *Times* article noted that many homeowners think their insurance will pay the full cost of replacement if their homes are severely damaged by fire or other disasters. But according to a recent study by Marshall & Swift/Boeckh, a firm that provides building cost data to the insurance and other industries, three-quarters of all homes nationwide are undervalued for insurance purposes by an average of 35%.

The cost of replacing a home has risen substantially in recent years due to increases in property values and construction costs. The cost of building a home in the northeast rose 28% from 1996 to 2002, according to the *New York Times*.

Most homeowners get their insurance policies when they buy their homes and do not consider that the cost to replace them can increase substantially



over time. Homeowners should not confuse property values with replacement costs. The cost to rebuild a home in a neighborhood where houses are selling for \$500,000 could be more or less than that amount depending on construction costs in the area. And if the house has custom features — solid wood floors, period details, tiling — the value is of course affected. Also, homeowners should make sure they are not insuring the value of the land their house is on. The land usually runs about 25% of the home price. But the cost of debris removal and landscaping should be factored into the replacement cost.

According to Marshall & Swift/Boeckh, insurance companies have traditionally used a square-foot measurement to determine home value. But this method fails to account for cost differences in construction materials and custom amenities. Now more insurance companies are turning to “total component estimating” which analyzes all features of a house, from the roof to the bathroom tiles.

Unlike many other insurance companies, Chubb and

Fireman’s Fund offer guaranteed full-replacement policies. Such coverage from Chubb may cost about 15% more than standard policies. Chubb has its own appraisers who inspect each house they insure, determine construction costs by various methods including talking to local builders, and set the coverage accordingly.

A Household Inventory— Worth the Time

A household inventory could prove invaluable if you lose some or all of your household belongings in a fire, burglary or natural disaster. It can assist you in recalling and reporting to your insurance company exactly what you have lost. A personal household inventory can provide you with a record of your household furnishings and belongings, when you purchased them and their original cost. For an investment of just a few hours, you can survey your belongings and be prepared in the event of a loss.

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WHAT THIS MEANS TO YOU

If you have renovated recently and have not informed your account representative, you should do so right away. Over time, making improvements of even several thousand dollars can quickly bring you over the limit on your policy.

If you do not have guaranteed replacement coverage now, you should talk to your representative about it. And if premium costs are rising too high (and they are expected to rise again) consider increasing your deductible.

Long Term Care Coverage: Asset Protection

Gary Donadio, Employee Benefit Products

Think about the very first things you did this morning — you got out of bed, walked to the bathroom, brushed your teeth, took a bath or shower, got dressed, made coffee. No doubt you do these activities without even thinking about them. But should you or a loved one be stricken with a stroke, develop Alzheimer's disease or another degenerative illness, these normal "activities of daily living" can become difficult or impossible without assistance. And such assistance does not come cheaply.

The assistance required when someone develops one of these conditions is called long term care. This "custodial" care involves providing an individual with assistance with the activities of daily living or supervising a person who is cognitively

impaired. Long Term Care can be provided in a person's home, in a nursing home, in an assisted living facility or in an adult day care facility.

How do families pay for this help?

The very wealthy can pay cash; the very poor have Welfare. The rest need to consider buying



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Wall Street Journal

Long Term Care is expensive

According to the *Wall Street Journal* in 1999, a year in a nursing home averaged more than \$40,000 annually and could exceed \$100,000 in some parts of the country. On the other hand, bringing a home health aide into your home every other day for just 4 hours can cost at least \$1800 a month.

Long Term Care insurance.

Long Term Care insurance has been around since the early days of Medicare but the coverage has evolved so that now policies cover a broad range of services including assistance in your own home, nursing home care, assisted living facilities and adult day care.

Medicaid will eventually pay for Long Term Care but only after a person's assets have been eliminated. Therefore, Long Term Care insurance is a kind of asset protection. If you can pay Long Term Care insurance premiums without diminishing your lifestyle, you should transfer that risk to an insurance company. Your state of health is a factor in your ability to get Long Term Care protection.

Too often people wait to consider Long Term Care insurance until their own health or their loved one's health has been compromised.

WHAT THIS MEANS TO YOU

Planning for long term care for yourself or for a loved one is not something to be left until you are elderly. If you are in good health and in middle age, you should look into it now. Some employers offer access to Long Term Care coverage to their employees. If yours does not, you might approach your Human Resources office about this.

Because Long Term Care insurance is for the "long term" it is important to know the financial strength of your carrier. Often, policyholders do not receive benefits until 10 or 20 years after policy issuance.

Be sure to ask your Long Term Care representative about these important but often ignored questions:

- What is the carrier's claims process?
- What percentage of claims filed are paid?

Gary Donadio at William H. Connolly & Co., can review all aspects of Long Term Care insurance with you.



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Employee Benefit
Programs

Risk Management
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Rebuilding, *continued*

How do I take my own inventory?

There are three basic steps. First, list all of your major belongings and furnishings, room by room. Record a brief description, any serial numbers, purchase prices and dates, and current value. Attach any receipts and appraisals.

The second step is to back up your inventory list with photographs or video. Take photos or a video of every room, with closet or cabinet doors open. Note the date, contents shown and location.

Third, store the inventory and photographs/videotape in a safe place away from your home, such as in a safe deposit box in a bank. Keeping a copy of the list or tape at home is fine, but it is wise to keep the original inventory and receipts in a secure location in case a fire or natural disaster destroys your home. Of course, you should likewise protect certain valuables and hard-to-replace documents such as deeds, bonds, stocks and insurance policies by storing them in a safe deposit box.

You should also be aware that homeowners policies generally limit the amount of coverage on fine art, jewelry, furs, silver and other possessions of high value, and you may want to purchase additional coverage for these items in the form of Personal Article Floater policies.

Vacation Planning Strategies

How can I secure my house or apartment while I am away?

Create a lived-in look to deter burglars. Stop newspaper and mail deliveries; ask a neighbor to park a car in your driveway occasionally; put the lights on a timer or ask a neighbor to turn them on in the evening. Use a telephone answering machine or call-forwarding to quiet ringing phones. Make sure that all the windows and doors are locked .

What do I do if the items I take with me on vacation are stolen?

Your belongings are generally covered by your homeowners or renters policy anywhere in the world. This includes items in storage facilities, suitcase contents and items borrowed by friends.

I plan to rent a car. Do I need to buy the insurance the rental agency sells?

Not necessarily. Prior to leaving on vacation, check with us to determine if your personal auto insurance policy covers damage to a rented vehicle, as many policies do. You may want to contact your major credit card company to ask if a rental car charged to that account is covered for damage. If you don't have one of these pre-existing coverages, it may be wise to purchase insurance from the rental agency.

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