

FINANCIAL LINES CLAIMS TRENDS

Financial claims notifications continue to rise globally, while claims are increasingly larger, more complex and international in scope.

1 REGULATORY ACTIVITY AND LITIGATION RISING

The continuing trend of rising notifications for financial lines, namely directors' and officers' (D&O) and professional indemnity, reflects increasing regulatory activity and litigation across many key jurisdictions.

While the US continues to see large D&O claims, other regions are also seeing an increase in the frequency and/or severity of claims. Australia, for example, has experienced a sharp rise in D&O activity in recent years, caused by more litigation. Class action lawsuits and more litigation funders have made Australia one of the most litigious countries outside the US from a business perspective. It is now relatively easy to build and fund a class action in the country, where consumer-friendly laws have supported an increase in class actions and larger settlements.

The UK is another country that has seen elevated claims notifications and increased settlements for D&O, mostly resulting from regulatory actions and insolvencies. There have also been some notable large professional indemnity claims for law firms and accountants, which have seen increases in exposures in recent years.

2 BOARD VS. BOARD MEMBERS

Germany has also seen the continuation of the trend for increased notifications for D&O insurance, in particular for the compliance failings of boards of German companies.

A characteristic of the German D&O market is the tendency for the board of a company to sue former directors for damages related to compliance failings. Claims are typically triggered by regulatory investigations and criminal prosecutions, which have previously included areas such as allegations of bribery and corruption or cartel activities.

"In Germany we have seen a continuing trend of internal D&O liability claims, where companies face more – and more expensive – lawsuits," says **Stephan Kammertoens, Financial Lines Claims Specialist at AGCS**. "Higher values also mean that suing former board members for damages has become an increasing option for German supervisory boards. We continue to see increased activity from prosecutors and regulators and growing public interest and media coverage of corporate wrongdoing."

3 EXPOSURES INCREASING AROUND THE WORLD

Financial lines claims have also been increasing in frequency and severity outside the US, Australia and Europe. Companies operating in markets in Asia and Latin America are more likely to face regulatory actions and litigation, either domestically or abroad.

For example, insurers handled one large D&O claim from a UK company related to a regulatory investigation at the group's subsidiary in Columbia. Brazilian companies have also faced class action litigation in the US related to corruption and environmental damage. Such claims are likely to become more



TOP CAUSES OF LOSS: FINANCIAL LINES CLAIMS

(ANALYSIS BASED ON PRODUCTS)

By value of claims

- Professional indemnity (e.g. negligence/misadvice) **61%**
- Directors and officers (e.g. breach of trust/fiduciary duties) **28%**
- Crime **5%**
- Initial public offerings **1%**
- Cyber **1%**
- Other **4%**

By number of claims

- Professional indemnity (e.g. negligence/misadvice) **76%**
- Directors and officers (e.g. breach of trust/fiduciary duties) **19%**
- Crime **4%**
- Cyber **1%**
- Mergers and acquisitions **<1%**
- Other **<1%**

Source: Allianz Global Corporate & Specialty. Based on analysis of 14,130 insurance industry claims between July 2013 and July 2018.

Professional indemnity claims account for 61% of financial lines claims by value.

Cyber-related incidents are an emerging claims issue, ranking as the fifth top cause of loss, according to value.

frequent in the future with globalization and regulatory developments in emerging markets. In Asia, financial lines claims are already increasing in size and frequency as regulators and prosecutors step up their activities, and with increased purchasing of D&O and professional indemnity insurance.

"We see more intense regulatory enforcement in Latin America and Asia, markets that do not always follow US or European understanding of law," says Kammertoens.

4 GROWING COMPLEXITY

Financial lines claims are growing more complex, in particular for international companies. Large claims are more likely to involve multiple parties and multiple jurisdictions – co-operation between regulators in different jurisdictions has been increasing, while one incident may spark litigation in more than one country.

For example, the diesel emission testing allegations have triggered regulatory investigations and litigation in the US, Europe and Australia involving a number of car manufacturers. D&O insurers have received claims notifications related to the emissions issue, which has already seen multi-billion dollar settlements in the US and pending class actions in Germany.

Large complex D&O cases have implications for insurance claims, where some insurers in higher excess layers may look to avoid participating in settlements.

"Clients and their brokers need to consider carefully which insurers they use," says Kammertoens. "It is important to retain and work with strong primary and excess insurers. It is not a question of money, but about the ability to reach a settlement with the entire tower."



Australia has experienced a sharp rise in D&O activity in recent years, caused by more litigation.
Photo: Adobe Stock

5 COLLECTIVE REDRESS GAINS GROUND IN EUROPE

Incidents like the emissions scandal have led to calls for collective actions procedures in Europe, resulting in regulatory changes in some member states and at an EU level.

For example, in July 2018 the German parliament approved a new class action law, which was implemented in November. The Model Declaratory Proceedings Act introduces for the first time the prospect of class action-style litigation for consumer claims. The act will enable certain institutions to bring claims on behalf of groups of consumers in order to obtain a declaratory judgment on behalf of all claimants.

“The introduction of a collective action framework in Germany could be important in the long term,” says Kammertoens. “It is a first step towards class actions and could lead to an increase in internal D&O liability claims. D&O actions are likely to follow successful collective actions, which could result in a larger exposure for both companies and directors.”

Class actions could also become a bigger driver for financial lines claims across the

European Union under proposed changes to consumer protection law. In April 2018, the European Commission outlined plans for so-called “representative actions” that would allow a qualified entity, such as a consumer organization, to seek redress on behalf of a group of consumers.

A number of EU countries already allow for collective redress. Notably, the Netherlands allows consumers and investors to use representative collective actions or class settlements to obtain mass damages. There have been a number of collective actions by investors and/or consumers in the Netherlands, as well as Germany and the UK.

Despite measures to avoid abuse or unmerited litigation, the trend towards collective actions in Europe is still likely to result in increased exposure for directors and officers and their companies, says Kammertoens.

“It should make it easier and more cost-efficient for consumers to obtain awards for damages, which could eventually lead to higher compensation costs for companies.”

6 CYBER NOTIFICATIONS INCREASING

Cyber-related losses in financial lines insurance are beginning to emerge with a clear tendency of an increase in claims notifications already evident.

“Data protection violations are one of the most frequent reasons for cyber-related claims notifications,” says **Szandra Sardy, Cyber Claims Specialist at AGCS**. The UK has seen a number of class actions launched following data breaches, including British Airways, Equifax and Ticketmaster. Having to comply with the recently introduced General Data Protection Regulation (GDPR) in Europe and related financial reporting has also led to shareholder actions in the US, including media company Nielsen Holdings and Facebook.

Perpetrators use various methods to gain access to data owned by companies. “For example, social engineering combined with phishing emails is one method,” says Sardy. “This means that, at first, perpetrators research information about individuals with privileged access to confidential data or with the authority to make payments for a company. This makes employees in departments such as human resources or accounting targets.

“Publicly-available information on social networks is used to identify possible victims and understand who they report to within their organization. Based on this, sophisticated phishing emails are being faked, tricking the victim into believing that it is their manager requesting information or payment. Such emails are often backed up with fake phone calls reinforcing the sense of urgency and confidentiality.”

Another method is introducing malware into a company’s computer system that enable perpetrators to view or even manipulate data. Long periods of time may elapse between infection and noticeable malicious activities within the system. “This means, such intrusion may go undetected for months and can spread undisturbed meanwhile,” says Sardy. As soon as the company becomes aware of their network issues, it will need to retain IT experts specialized in different areas of analysis, remediation and restoration.

“Such IT services can cost millions of euros or dollars, as it may require several teams of experts investigating what has happened, what kinds of different malware were used, which accounts and hosts have been compromised and then to advise how the infection can be contained and remediated,” says Sardy.

“This is money well spent if the experts can save the company from business interruption and large scale data breaches. It is essential to have immediate access to a strong network of IT experts who can provide the specialized know-how and technical equipment needed.

“What the different methods of cyber criminals have in common is that they are carried out in a highly professional manner. Companies are not facing individual hackers but transnational organized crime with enormous profit margins,” Sardy concludes.

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