Benchmarking Limits of Liability: A Greater Percentage of ESOP Companies are Purchasing Higher Limits of Liability

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It has been a little over five years that we had researched our affinity program database to report on the limits of liability being purchased by ESOP Association members for their executive liability insurance. As a result, we have prepared this update to determine if purchasing habits have changed among the over 240 members in this program.

For background purposes, this affinity program offers members the ability to purchase Director's and Officer's Liability (D&O), Fiduciary Liability, Employment Practices Liability (EPL), Crime and Cyber Liability on a group basis thereby providing members with more competitive policy premiums and coverage terms than if they were purchasing this protection by themselves in the traditional marketplace. The program is underwritten for Association members on an *exclusive* basis by Great American Insurance Company and is endorsed by the Association.

In this article, we will compare the policy limits of liability for ESOP Association members are purchasing based on (i) corporate asset size and (ii) employee count for the D&O, Fiduciary and EPL. Typically, the D&O, Fiduciary and EPL coverages can be purchased under one policy. The criteria of corporate assets and employee count is normally how insurance company underwriters base their premiums. Also, these benchmarks are sometimes used by policyholders when comparing themselves to other ESOP companies.

Shared Vs. Separate Policy Limits:

Before we discuss the results of our benchmarking study, it is important to note that ESOP companies generally are able to purchase their policy with limits being either "shared" or "separate" for the D&O, Fiduciary and EPL coverages. A policy limit that is "shared" involves the coverage or limit spread among the three aforementioned coverage types. So a claim payment involving one coverage of the policy would reduce the policy limit available to pay potential future claims involving the other two coverages. Policy premiums are typically lower if coverage is purchased on a "shared" basis. Having a policy with "separate" limits means that a separate limit applies to each of the three coverages independently.

Our observations from this study indicate ESOP companies are purchasing (i) higher limits of liability than they were five years ago and (ii) a greater percentage are purchasing "separate" limits rather than having the limits "shared" among the three coverages. Our 2008 study concluded that only 13% of the ESOP companies purchased "separate" limits of liability.

Today, 56% of ESOP companies are purchasing "separate" limits of liability!

Thus, more ESOP companies than ever before are spending a little more premium for the better protection.

Comparing Policy Limits of Liability Based On Corporate Asset Size:

For our benchmarking analysis, we divided the Association members purchasing these coverages into three categories based upon the size of their corporate assets. The categories are:

Category I: Corporate Assets less than $10MM

Category II: Corporate Assets between $10MM to $50MM

Category III: Corporate Assets over $50MM

Of the approximate 200 or so companies whose data was analyzed, about 51% were companies in Category I. Another 44% in Category II and 6% in Category III. Here is what we found out:

The average amount of policy limit for ESOP companies in Category I is $1.73MM, or rounded up, $2MM. Some 51% of ESOP companies in this category maintain limits of $1MM while 44 % carry $2MM or more.

The average policy limit for ESOP companies in Category II is $2.45MM with 40% of ESOP companies in this category having a $1MM policy limit. Approximately 60% have limits at least $2MM or greater. Of this 60% roughly two thirds of ESOP companies have limits in the $3MM to $5MM range.

We noticed those ESOP companies in Category III are companies that have their policy limits set as high as $15MM. Also, the overall average limit for companies in this category are $5.40MM with 67% in this Category having limits between $3-5MM.

As you might expect, as the size of the company's assets increased, so did the limits of liability being purchased. Compared to the similar study completed over five years ago, higher limits of liability are being purchased by ESOP companies representing Category III ($3.8MM average limit five years ago to today's average of $5.40MM)and slightly higher limits for those in Categories I and II.

Comparing Policy Limits of Liability Based on Employee Count:

Because many of ESOP companies purchase Employment Practices Liability (EPL) as part of their policy package, employee count is often a valid criteria for comparing policy limits. From a Fiduciary Liability standpoint, employee count may also be useful for benchmarking purposes as it relates to the number of active plan participants.

For this comparison, we used a total of four (4) categories of TEA members in this study. They are:

Category I: Employee Count less than 50

Category II: Employee Count of 50-100

Category III: Employee Count of 100-250

Category IV: Over 250 Employees

The majority (55%) of ESOP companies in our group have 100 employees or less.

Like with what we saw in our corporate asset comparison, those ESOP companies having higher employee counts purchase higher limits of liability.

ESOP companies having 100 or less employees (Categories I and II) carry an average of $1.8MM limit. Approximately 60% of ESOP companies in this category carry $1MM limits and roughly 27% carry $2MM.

Those ESOP companies with 100-250 employee count, Category III, have an average policy limit of $2.5MM while 41% of this group carry limits of between $3-5MM.

ESOP companies with more than 250 employees, Category IV, carry an average limit of $3.4MM. A convincing 80% of this group carry limits of between $3-5MM.

ESOP Companies Represent a Variety of Industries:

In general, ESOP companies participating in this affinity program range from small to large, all are privately held, represent many different types of industries and are domiciled in almost all of the fifty states. Not surprising, the majority of the policyholders are made up of professional type firms (engineering, architectural, environmental, financial, healthcare and insurance). This group represents roughly 46% of the policyholders. Manufacturing/ Distribution represent 24% of the group. Roughly 13% are in the Construction and Transportation sector. Media/Communications and Retail represent 10% and 7 % respectively.

Some final thoughts to share is when considering what limit of liability to purchase, keep in mind that defense costs (legal fees) paid on a covered claim will erode the policy limit of liability. Legal fees to defend a claim can exceed $500,000 and even beyond $1,000,000. In addition to corporate asset size and employee count, consider whether your policy "shares" the limit with the other coverages offered by the policy (see above explanation)or on a "separate" basis. Also consider whether your policy also insures other retirement plans like a 401(k) and the percentage ownership of your ESOP of the company. The higher percentage of employee ownership, the greater the potential of a significant size claim.

The author, Jeffrey S. Gelburd is Vice President of Murray Securus (an ESOP company) which administers the Executive Liability Insurance Program endorsed by The ESOP Association. This Program marks its 25th anniversary in 2014. The author would like to acknowledge appreciation to the Association for their support, the underwriting partners at Great American Insurance Company who provide this protection, the ESOP professionals who offer advice and counsel and to the over 200 Association members that participate in this affinity program. He can be reached at jgelburd AT murraysecurus.com or 717-620-2476.