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PRESS RELEASE

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DIRECTORS & OFFICERS (D&O) LIABILITY PREMIUMS DECLINE FOR THE FIRST TIME SINCE 1999 ACCORDING TO TILLINGHAST

Tillinghast's directors & officers (D&O) liability insurance premium index dropped 10% from 2003 to 2004, the first decline since 1999, according to the 2004 Directors & Officers Liability Survey, by the Tillinghast business of Towers Perrin. However, claim susceptibility, frequency and severity are still soaring. Tillinghast's survey, which included 2,455 participants, is the 27th in a series of studies on D&O liability claims and insurance purchasing patterns and the most in-depth study of its type.

According to this year's survey, much of the current softening in the D&O market is not due to a reduction in claim activity, but rather can be attributed to the entrance of new capacity. Competition is particularly fierce in excess layers for large public companies, where rates are dropping 10% to 15%. Despite the softening market, some pockets of hard market conditions remain, particularly in banking, health services, and real estate and construction. Looking at the historical data, it appears that 2003 was a turning point in the market; however, Tillinghast cautions not to expect the trend to continue.

Many feel this soft market for D&O insurance will be shorter and less pronounced due to lower investment returns than in the 1980s when cash flow underwriting was prevalent. Carriers will likely need to begin increasing rates in the short to medium term in order to maintain their return on equity.

Capacity increased 11% to \$1.5 billion in full limits from 2003, and a record number (99%) of U.S. participants reported having D&O insurance. Fewer respondents cited "cost" as the main reason for going without coverage (44% of participants in 2002 versus 26% in 2004). "The survey tells us that coverage is being offered broadly in the market, with decreased premiums, increased limits and enhancements, and fewer exclusions," said consultant Elissa Sirovatka, who leads Tillinghast's D&O Liability Survey program. "What's disturbing is that this is occurring at the same time frequency and settlement costs are still rising."

Among repeat participants, claim frequency increased 11% from 2003 to 2004 and claim susceptibility increased 6%. Average severity for repeat participants increased in three out of five claim classes, including employees/unions/physicians, competitors/suppliers/contractors, and shareholders/investors.

“The continued increase in the average cost to settle D&O claims combined with the significant number of open megaclaims makes a tough case for a sustained soft market. The claim conditions we’re seeing justify premium increases rather than decreases,” said Sirovatka.

Top sources of allegations from shareholder claimants (general breach of fiduciary duty, inadequate/inaccurate disclosure, including financial reporting and stock or other public offering) and employee claimants (discrimination and wrongful employee dismissal or termination) were the same for 2003 and 2004. Surprisingly, though, allegations citing accounting fraud also remained the same at 2%.

More than half (56%) of claims against 2004 participants are still open, which is up from 37% in last year’s survey. “The increase in open claims along with the increasing settlement costs will make it difficult for insurers to get a handle on their reserves for D&O liabilities,” said Sirovatka. “Couple this with premature pricing declines and a softening market, and insurers could be heading toward a D&O reserve shortfall if we don’t start to see more disciplined underwriting and adequate pricing.”

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