



The EPL Insurance Market: Where It Is, Where It's Going

In 1997, Griffin Communications, Inc. published THE EPL BOOK: A PRACTICAL GUIDE TO EMPLOYMENT PRACTICES LIABILITY AND INSURANCE. Soon to be released is our revised second edition of THE EPL BOOK. We thought it would be interesting to compare some of the information gathered from our insurance company survey to give a then-and-now comparison of the EPL insurance market and to peek into the future of EPL insurance.¹

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Underwriters at Lloyds were probably the first to market a low-limit, defense-only EPL insurance product in the mid-1980s, well before other insurers were aware that a potential market for such a product existed.

In early 1992, Lexington Insurance Company and New Hampshire Insurance Company (members of the American International Group) both introduced an EPL insurance product. While limited in scope when compared to modern policies, the introduction of a stand-alone EPL insurance product by major U.S. insurers garnered much attention and speculation about the future of such products. Reliance National, the Chubb Group and others soon introduced their own EPL insurance products. Since then, a steady stream of insurers have entered the marketplace.

In April 1998, the Insurance Services Office (ISO) introduced a standardized EPL insurance product, hoping it would gain widespread acceptance among smaller insurers. While ISO's new EPL insurance form was the first new product it had introduced in nearly 20 years, the scope of coverage paled in comparison to existing EPL insurance. Thus far, the ISO policy has not yet achieved what the original drafters had hoped for. Still, ISO's entrance into the EPL market indicates that EPL insurance has achieved a certain legitimacy that had eluded it in prior years among many buyers, agents and brokers.

Purchasing Habits

In recent years, business, industry and public entities have become more aware of the potential for catastrophic loss from employment-related litigation. This heightened awareness appears to have motivated a larger number of employers to purchase coverage for employment practices liability. This is in contrast to previous years, when insurers and brokers reported a large number of insurers inquiring about EPL insurance, but with few sales. Many insurers and brokers we contacted reported receiving orders on between 10-20% of all proposals.² This compares to reports of 5-10% in 1996, when we conducted an informal telephone poll.

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Although brokers and insurers both report increased interest in EPL insurance by employers, the percentage of organizations actually purchasing EPL insurance still remains relatively low compared with general liability or other standard forms of business insurance. A 1997 survey of employers conducted by The Society for Human Resource Management (SHRM) and Jackson Lewis revealed that 22% of respondents reported purchasing EPL insurance.³ Insurers and brokers alike described the EPL insurance market as having huge potential for future sales.

Market Profile

The EPL Book began surveying EPL insurers in 1996. At that time, we identified 23 insurers actively writing EPL insurance, primarily in the form of a stand-alone product. Because some insurers offer more than one policy form, the total number of policies reviewed at that time was 30. In 1998, the number of insurers responding to our survey rose to 39, with 60 separate policy forms submitted and evaluated. The actual number of insurers writing EPL insurance is likely higher than our surveys indicate. We estimate that the total number of insurers that cover liability arising out of employment practices through stand-alone, D&O, general liability, umbrella, professional liability, and association and other specialty programs probably exceeds 60. Because many insurers offer more than one policy form, the number of different EPL insurance policy forms may well exceed 100.

It is interesting to note the composition of the total EPL market capacity as measured by available limits per policy. Exhibit 1 shows the distribution of policy limits by number of insurers for survey years 1997 and 1998. In addition to a substantial increase in the number of insurers actively competing in the marketplace, a similar increase in available capacity occurred.

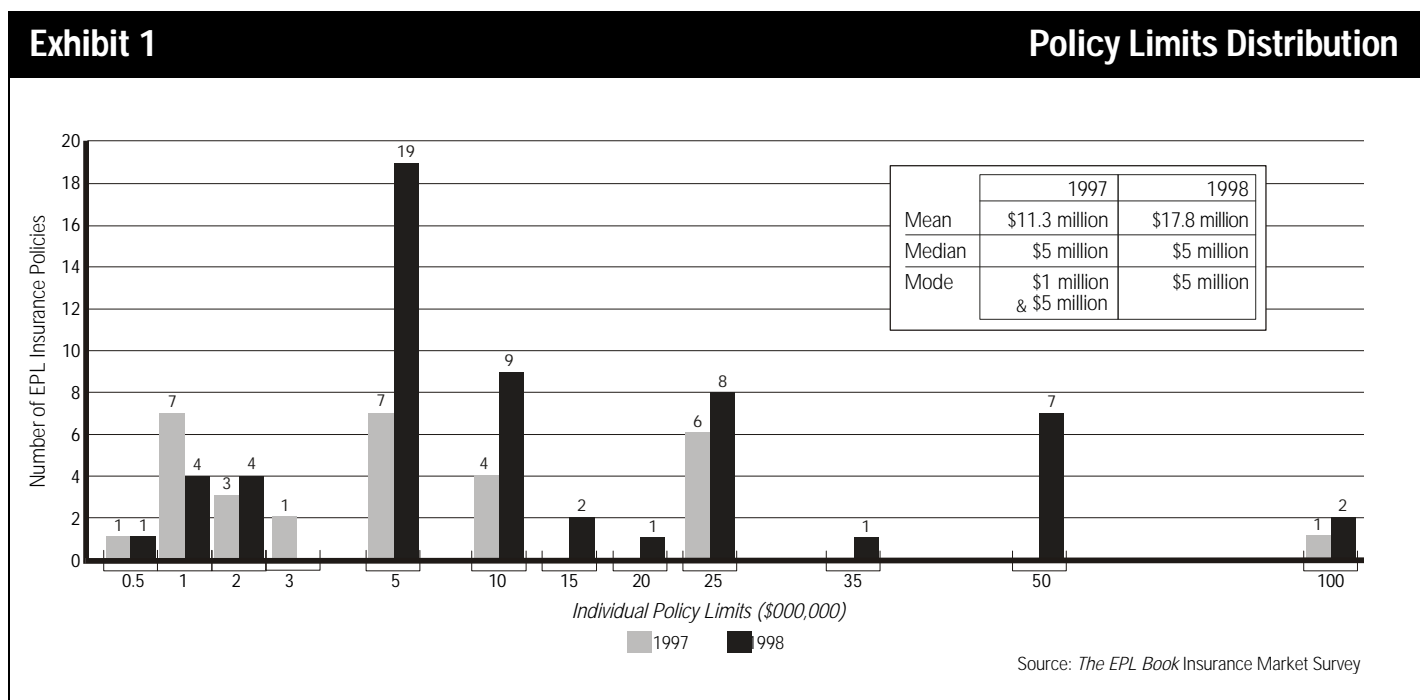


Exhibit 2**EPL Insurance Capacity**

	1997	1998	% Change
Number of Insurers	23	39	70
Number of Policy Forms	30	60	100
Total Per-Policy Capacity	\$340.5 million	\$1.0325 billion	203
Total Per-Insurer Capacity	\$293.5 million	\$713.5 million	144
Mean Policy Limit	\$11.3 million	\$17.8 million	58
Median Policy Limit	\$5 million	\$5 million	no change
Mode Policy Limit	bimodal at \$1 million & \$5 million	\$5 million	N/A
Range	\$95.5 million	\$95.5 million	no change

* Calculated using maximum policy limit only for insurer offering multiple policy forms.

Source: *The EPL Book* 1997 and 1998 surveys

Exhibit 2 summarizes total market capacity, mean,⁴ median,⁵ mode⁶ and range of maximum available per policy limits for 1997 and 1998. In addition, information regarding the number of insurers writing EPL insurance, as well as the number of different policy forms available, is provided.

In calculating limit-capacity figures, we used the highest per-claim limit for each individual policy. We separately calculated total aggregate capacity based on each insurer's maximum individual policy limit. For example, if an insurer offers three different EPL products with limits of \$5 million, \$10 million and \$15 million, we used only the highest figure in our second calculation. The purpose of the second calculation method was to give consideration to the fact that some insurers that offer multiple policy forms may draw capacity from a common source. In such instances, counting individual policy limits separately would tend to inflate the total-capacity figures.

While our survey response data was not definitive, it provides readers with a relative indication of market conditions between the two survey periods. The compiled data indicates that:

- ◆ The number of insurers writing EPL insurance that responded to our survey increased from 23 in 1997 to 39 in 1998.
- ◆ The number of different EPL insurance policy forms increased by 100% (from 30 to 60 separate policy forms).
- ◆ The total EPL insurance market capacity has increased over 140% in one survey period.
- ◆ Total EPL capacity, as measured by our survey, is at least \$715 million and may be as high as \$1 billion.
- ◆ The available median policy limit of \$5 million has not changed.

Much of the increase in capacity is due to the addition of a second insurer offering single policy limits of \$100 million and seven insurers offering limits of \$50 million.

Pricing

Price competition has increased, with overall rates reported by some insurers dropping 10-20% per year over the past two years. Reasons include the following:

- ◆ Continued soft global insurance market
- ◆ Increased capacity
- ◆ Relative increase in supply versus demand

Some insurers expect prices to begin to flatten out beginning in 1999, but perhaps with slight increases for some insureds. If prices do rise, insureds with operations in high-litigation states such as California, Texas and Michigan will be impacted most. Some insurers say they may refuse to write new business in these states. Insurers also are likely to avoid public entities, professional entities, the entertainment industries, and other industries or companies with historically poor loss ratios. As more historic data is collected and gathered, insurers should be better equipped to actuarially underwrite the EPL exposure based on geographic location and industry.

While the outlook may be grim for some insureds with bad loss experience, even those in high-risk industries or geographic locations may still experience price decreases or at least stability. The essential factor will be how well these insureds manage the employment exposure using proven risk management techniques.

Coverage

Between the time of our first market survey (published in 1997) and now, many older EPL policy forms have been replaced with new versions. Some policy forms not replaced may be modified by endorsement to eliminate or limit the scope of certain exclusions. In both instances, current policy forms provide broader coverage than they did just a year

Exhibit 3 EPL Insurance Exclusions Usage	
<i>EPL Insurance Policy Exclusion</i>	<i>% of Policies Reviewed Containing EPL Exclusion</i>
ADA Accommodation Expenses	68
Assault & Battery	21
Back Pay	3
Bodily Injury	77
Breach of Contract	38
Class Action Lawsuits	0
Consequential Loss	15
Cost of Arbitration Hearings	7
Failure to Exercise Care When Terminating	7
Punitive Damages	65
Front Pay	16
Intentional Acts	23
Liquidated Damages	20
Loss Arising Out of Changes in Operations	
Acquisition	5
Change in Control	2
Downsizing or Reduction in Force	8
Merger	3
Plant or Facility Closing	11
Reorganization	10
Temporary Shutdown	2
Non-Monetary Relief/Damages	52
Personal Injury Offenses	8
Prior Acts	38
Prior Knowledge	57
Prior/Pending Litigation	45
Property Damage	53
Loss of Use	77
Retaliatory Actions of Employer	5
Strikes/Lockouts	47
Violation of Laws	3
Any Law	5
FMLA	2
OSHA	52
Pollution Laws	33
RICO	8
SEC	0
WARN	75

Source: *The EPL Book 1997* and 1998 surveys

ago. Most notable in new policy forms is fewer exclusions. Downsizing, class-action, punitive damages, breach of contract and other exclusions appear far less often today. Exhibit 3 shows the relative frequency with which certain exclusions appear in EPL insurance policies.

Changes in the scope of coverage are not only limited to a reduction in the number and breadth of exclusion. In some instances, coverage is available for exposures such as third-party liability and punitive damages.

While there has been an increase in the availability of coverage for employment practices liability vis-à-vis the addition of such coverage to D&O, umbrella, general liability and other policies, the market for stand-alone products remains strong.

Conclusion

After many years of limited interest, EPL insurance is being accepted by a growing number of employers as a necessary business insurance policy. While prices have been in free-fall for the past two years, many insurers predict stability at least for the short term as markets seek a reasonable balance between broad coverage and reasonable pricing.

Many sources we spoke with acknowledged that any major changes in pricing and coverage would likely reflect greater reliance on historical losses and other actuarial data as insurers become better able to determine the adequacy of their underwriting and pricing. ☞

For more information about THE EPL BOOK or to order the latest revised edition, call our customer service center at 800/205-6218.

NOTES

- 1 Information regarding the current state of the EPL insurance marketplace was gathered from the following sources: Insurance company survey responses to EPL Book surveys collected in 1997 and 1998, insurance company interviews, broker interviews, interviews with wholesalers, interviews with employers and other published data.
- 2 A recent CPCU Journal article reported insurers writing between 5–15% of accounts quoted.
- 3 The actual percentage may be higher, however, as 30% indicated that they did not know whether the organization purchased such insurance.
- 4 **Mean**—Statistical measure of central tendency.
- 5 **Median**—A statistical average indicating central tendency where one-half of the items being averaged fall below and on-half fall above the midpoint.
- 6 **Mode**—A statistical measure of common tendency or average that identifies the value of the variable giving the greatest height on a graph of the frequency distribution.

FURTHER READING

To review previous discussions in The Risk Management Letter on topics related to this article, please refer to the following issue:

- “ISO’s New Employment Related Practices Liability Policy” (Volume 18, Issue 8)

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