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D&O RISK & LIABILITY

Financier Worldwide canvasses the opinions of leading professionals around the world on the latest trends in D&O risk and liability.



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HONG KONG



Respondents



DAVID HO
Head of Financial Lines – Asia
AIG
+65 6319 7080
david.ho@aig.com

David Ho was appointed head of financial lines – Asia in September 2019. He brings with him over 20 years of financial lines underwriting experience specialising in directors & officers and employment practices liability, professional indemnity, crime and cyber insurance. Prior to moving to Asia in 2015, he led AIG Financial Lines' major accounts division focusing on the largest financial institutions in North America. He has been with AIG since 2003. He holds a Bachelor of Arts degree in Economics from Pace University in New York.



COLLIN BENTLEY
Major Loss Claims Manager, Financial Lines
AIG
+612 9240 1740
collin.bentley@aig.com

Collin Bentley is the major loss claims manager across the Asia-Pacific region. He has over 20 years of experience handling financial lines claims. At different times in his career, he has worked in Singapore, China and Australia. He is an Australian legal practitioner qualified in New South Wales. He also holds a Bachelor of Arts degree majoring in Asian Studies from the Australian National University.

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Q. Could you outline some of the key factors currently driving the personal risks facing D&Os in today's market?

A: The Hong Kong D&O market is driven primarily by the regulatory environment. Regulatory scrutiny manifests itself as a by-product of economic volatility and emerging market risks that could ultimately impact stakeholders, including shareholders, creditors and customers. Hong Kong is a market where class action law does not exist. Regulators are keen to protect the interests of stakeholders due to Hong Kong's importance as an international finance hub. This was demonstrated in 2019 with the Securities & Futures Commission (SFC) showing increased interest in listed companies. In its July-September 2019 report, the SFC disciplined six licenced corporations and nine licenced representatives in that quarter alone.

Q. In what ways have the personal risks faced by D&Os changed over the past few years? What major new risks have arisen?

A: The personal risks faced today by D&Os can be boiled down to a couple of key

issues: flows of western capital and a desire by regulators to prevent market abuses. As international investment has flowed into Hong Kong, so too have demands for stakeholder rights. In 2019, Asia became the second most active region, after the US, for activist investor lawsuits. We expect this trend to continue, particularly in Hong Kong, as local companies bid to attract foreign capital. Technology companies are particularly susceptible to allegations of poor governance standards as they may seek dual class shareholder structures which may not be in the best interest of stakeholders. These perceived weaker governance standards could increase allegations of misconduct against D&Os.

Q. How might the personal risks facing D&Os evolve in the months and years to come? To what extent are they becoming more complex, international and unpredictable in scope?

A: 2019 was an unpredictable year in Hong Kong. Political turmoil, recessionary pressures and supply chain disruptions caused by cyber incidents or the emerging spread of novel coronavirus are going to keep pressure on D&Os for years to come.



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As the recession drags on, we will see more companies succumbing to financial stress. Every month in 2019 saw a higher amount of corporate bankruptcies per month than over Hong Kong's 25-year average – in some months, the number of bankruptcies was quadruple the 25-year average. Certainly, there will be a lot of stakeholders questioning and challenging management over their decisions. Broad cross-border laws like the General Data Protection Regulation (GDPR), which imposes European Union data privacy laws on non-EU companies that have EU customers, may further accelerate Hong Kong companies' adoption of a more western-style view of risk management as they attempt to combat the potential for fines and increased stakeholder scrutiny.

Q. In terms of D&O insurance, what steps should companies take to ensure they offer their D&Os an appropriate level of coverage?

A: Companies should align with a knowledgeable broker or agent, who understands the company's D&O exposures and the D&O insurance marketplace. Every company has a unique

set of risks and exposures; understanding the exposures and matching these with its tolerance to take on balance sheet risk is the first part of the equation. D&O insurance is one of the most personal of all commercial insurance products on the market as a director or officer's personal wealth could be at risk in circumstances when there is a legal action against them. There may be times when the director or officer's company cannot indemnify them because of insolvency or liquidation, or will not indemnify them because it is prohibited from doing so. At that point, a D&O policy is the last line of defence before the D&O's personal assets come into play. This is why D&O insurance has always been a great way to attract the best and brightest minds to a company. Therefore the decision to purchase D&O insurance is best made at board level.

Q. What advice would you give to both companies and D&Os when they are assessing the merits of a particular D&O policy? Which elements are of paramount importance?

A: It is imperative that companies know who they are dealing with. They must know

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who is on the other side of the transaction handling and paying the claim. The D&O insurance market is a competitive market, but not all D&O insurers are equal. Companies and their D&Os should ask questions of their agent or broker, or if possible, speak with the underwriter at the insurance company. Some companies are built to handle all claims, from the simple to the complex, while other companies may sub-contract this out to a third-party and will not be involved in the handling of a claim, sometimes to the detriment of the policyholder. It is important to partner with a reputable insurance carrier that understands not only your D&O needs, but is committed to the Hong Kong market so it can handle your claims now and in the future.

Q. How have D&O insurance policies evolved in recent years? Have there been any general changes in terms, exclusions, pricing and so on?

A: Originally D&O policies were, as the name suggests, meant to cover directors and officers against allegations of managerial misconduct. They have evolved over the years to include more exposures of

the company, so something like a securities claim that names only the company can be picked up. The evolution of D&O policies in Hong Kong has seen the granting of more extensions to the policy – some are specific to individuals, such as public relations expenses and extradition costs, while other extensions are specific to the company, like extensions for wrongful employment practice-related allegations or coverage for regulatory investigations. Coverage has also been broadened by limiting the impact of exclusions, often by providing carve backs to exclusions to provide an element of cover, like defence costs or deleting the exclusions outright. Until recently, pricing had been on a long downward trend. Over the past couple of years, however, pricing has started to firm up, mainly due to increasing frequency and severity of claims and market dynamics as insurance carriers adjust their appetites. Claims are particularly acute for Hong Kong companies that list their shares on a US exchange.

Q. In your opinion, have there been any recent, high-profile D&O claims cases in which the outcome proved to be particularly significant? How might such



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cases impact on how D&Os view the risks they face?

A: Traditionally, large sized policyholders are the ones who have experienced the largest claims in terms of volume and severity. Recently, however, this has changed. Investors have started to challenge smaller, publicly traded Hong Kong companies, alleging conflicts of interest, market manipulation and ultimately, fraud. This has, in turn led to actions being brought against these companies by regulators, their D&Os, and in a relatively new development, D&Os against fellow D&Os. The allegations may ultimately not be substantiated, but there is no doubt the costs to defend against them, or any settlement, will potentially be significant. The Hong Kong D&O insurance market is certainly keeping a close eye on developments in this space. □



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DAVID HO Head of Financial Lines – Asia
+65 6319 7080
david.ho@aig.com

COLLIN BENTLEY Major Loss Claims Manager,
Financial Lines
+612 9240 1740
collin.bentley@aig.com

CYNTHIA SZE Head of Financial Lines
+852 3555 0173
cynthia-lk.sze@aig.com

SCOTT JUDY Head of Distribution, Hong Kong
+852 3555 0368
scott.judy@aig.com

