

THE WILLIS INDEX

The Directors' and Officers' Liability Insurance and Risk Management Quarterly
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MARKET CONDITIONS AND THE RESULTS OF THE MARKET SURVEY

The Willis Index conducts a quarterly survey of the Lloyd's and London company market in which we invite responses from over 90% of D&O insurers, asking them to comment on premium rates and coverage terms for the preceding three months and predict the next three months. The results are aggregated anonymously in this report.

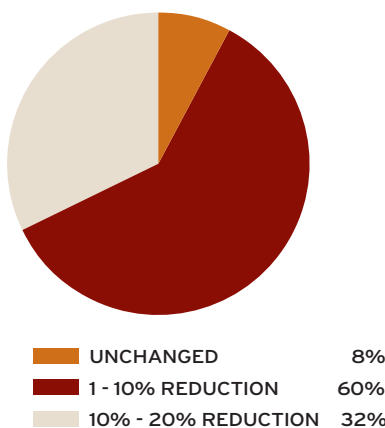


INSURERS' FESTIVE GENEROSITY CONTINUES!

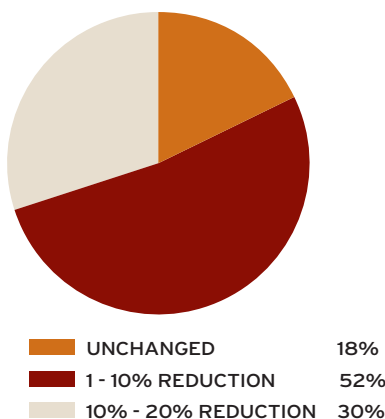
In the last quarter, insurers reported declining rates on over 90% of their business as they fought for market share to maintain their premium income. This trend looks set to continue into 2008 with the market continuing to experience overcapacity and reduced claims activity. The recently published Willis Re – 1st View, analysing the January 2008 reinsurance renewals notes that for professional lines the reinsurance market remains stable with a decline in treaty premiums and improved coverage which we expect to be passed on to our clients in 2008.

Several insurers launched new wordings in the last months of 2007 which continued the trend for enhanced coverage and increased flexibility in negotiating terms. Some of the key policy exclusions have been watered down or removed, and elsewhere coverage has been broadened to reflect changes in legislation, with insurers willing to consider more creative solutions to help meet clients' needs.

PRIMARY PREMIUM RATES - LAST 3 MONTHS



PRIMARY PREMIUM RATES - NEXT 3 MONTHS



Contents

Market Conditions and the Results of the Market Survey	1
Employment Practices Liability	2
Update on Corporate Manslaughter and Corporate Homicide Act 2007	5

PRIMARY PREMIUM RATES

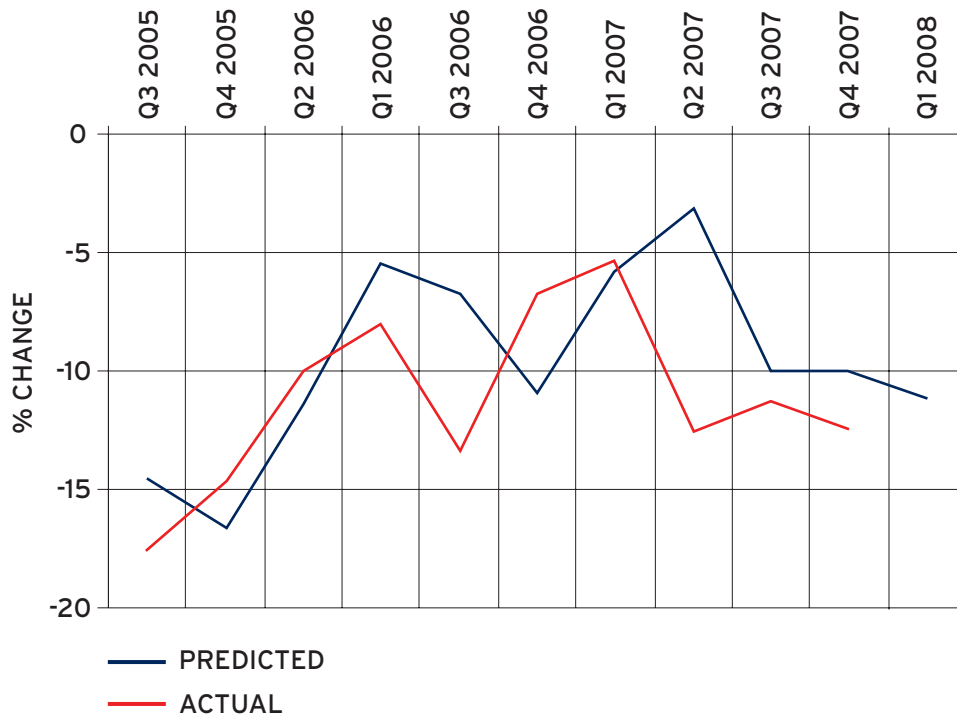
Over the last three months, only 8% of insurers reported flat renewals while of the remainder, 60% reported reductions of up to 10%, and 32% reported reductions of up to 20%. The averaged rate of decline of 12.4% experienced by insurers therefore marginally outstripped the 10% decline predicted in the preceding quarter.

Over the next three months the outlook remains consistent with predictions of continued rate reductions of 11.2% on average.

EXCESS PREMIUM RATES

Over the last three months excess premiums continued to fall at a faster rate than primaries with an average reported rate reduction of 15%, reflecting the more intense competition for excess layers. Over the next three months this looks set to continue with insurers predicting that rate declines will remain virtually the same at 14.4%.

PREDICTED VS ACTUAL RATE CHANGE



EMPLOYMENT PRACTICES LIABILITY

Employment Practices Liability Insurance (EPLI) is increasingly bought on a stand-alone basis. As EPLI claims are often triggered by lay-offs or reductions in force (RIFs), EPL claims frequency tends to increase in economic downturns. For smaller, private companies, EPL insurance buying trends are on the rise. For large corporations, an employment practices lawsuit is almost a certainty. For smaller companies, even a single plaintiff complaint can often turn into expensive and lengthy litigation. As some estimate that an uninsured EPL claim could bankrupt close to 50% of small companies, EPLI is an extremely valuable risk management tool that should not be ignored. Companies in the U.S. have bought EPLI for years, and this trend is spreading to the rest of

the world as claims, awareness and availability of the product increase.

Employment practices legislation and resulting claims are on the rise. According to recent Employment Appeals Tribunal (EAT) statistics, employment claims in the UK reaching tribunal have increased more than 50% in two years. Totalling 132,577 claims in the 2006 to 2007 period in the UK, employment litigation is increasingly costly⁽¹⁾ while the Equal Employment Opportunities Commission (EEOC) in the USA recorded more than 75,000 individual charges in 2006⁽²⁾. This trend is spreading to the rest of the world, with claims severity bringing a heavy financial burden to employers.

⁽¹⁾ Employment Tribunal and EAT Statistics (GB) Report 1st April 2006 to 31st March 2007

⁽²⁾ U.S. Equal Employment Opportunities Commission Charge Statistics Fiscal Year 2006

An employment practice violation is most commonly attributed to an employer's decision to hire, fire, promote, demote or deny employment benefits based upon a discriminatory attitude toward one or a class of employees. Harassment that causes a hostile working environment or other inappropriate employment conduct can also lead to an employee bringing a claim directly against either the employer itself or via the EEOC in the USA, the Commission for Equality and Human Rights in the United Kingdom or similar governmental agencies in other countries.

WHO IS AN INSURED?

Unlike other management liability products, when a dedicated EPLI policy is purchased, coverage is not contingent on an individual being named. A claim can be brought against the corporation itself, its directors and officers, and its employees.

Employees can include all of the following:

- both full and part time workers;
- volunteers;
- seasonal and temporary staff;
- leased employees; or
- independent contractors and consultants performing work for the company.

An important clarification is that past, present or future employees can fall into any of the above categories. Therefore, even an employer's hiring decisions, if found to be discriminatory, can trigger very expensive litigation.

WHO BRINGS A CLAIM?

Employment practices claims can be brought by an employee directly against the company or via regulatory agencies such as the Equal Employment Opportunity Commission (USA) or the newly created Commission for Equality and Human Rights (UK). These agencies can also bring claims against the company themselves, as well as impose fines and penalties for discriminatory behaviour. In addition to single plaintiff claims, US class actions have increased in prominence in recent years, with cases such as *Dukes vs. Wal-Mart Stores, Inc.*, a gender discrimination case which includes more than 1.6m current and former female employees in the company's retail and warehouse stores.

DISCRIMINATION

Discrimination in the workplace is the most common allegation in an employment practices lawsuit. Gender discrimination cases, or "glass ceiling cases", are often attributed class action status. Single plaintiff discrimination claims can be equally as costly, however, and are especially common in the financial services industry. Earlier this year, a gender discrimination case was filed against BNP Paribas plc in the UK. A female employee complained of unequal treatment after returning from maternity leave and a "culture of sexism". She is seeking EUR2m in compensation.

The *Dukes vs. Wal-Mart Stores, Inc.* class action case (currently pending) alleges that the company engaged in a practice of discriminating against women in terms of promotions, pay, training and job assignments. Plaintiffs are seeking injunctive relief, front pay, back pay, punitive damages, and attorneys' fees. The class action certification status was re-certified by a US federal appeals court this year and is expected to be one of the costliest EPL settlements in history.

In 2000, an EU directive required all EU member states to implement age discrimination laws by year end 2006. The Employment Equality (Age) Regulations came into force in the UK in October 2006 and age discrimination claims immediately increased by just under 1,000 in the pro rated time period for the EAT annual survey. It is expected that with this legislation, the increase in claims will grow at similar rates to that in the USA - which grew by up to 40% - when the Age Discrimination in Employment Act (ADEA) was passed in 1967. A closely watched age discrimination case in the US settled 4th quarter 2007 when Sidley Austin LLP, the international law firm, agreed to pay USD 27.5m on behalf of 32 former partners in a case brought by the EEOC. The partners in question had been demoted to counsel status in 1999, when most had reached their 50s and 60s. As many law firms mandate a retirement age, this test case has received much attention. The EEOC proved that the demoted partners were classified as employees, rather than employers, as they did not hold adequate voting power on management issues at the international firm. Therefore, the ADEA



act applies and it was found the partners had been victims of age discrimination.⁽³⁾

Other types of discrimination in the workplace bring significant claims statistics as well. The largest historical EPL award was a settlement in a racial discrimination case. In *Motisola Malikha Abdallah, et al. vs. the Coca Cola Company*, Coca-Cola was found to be at fault over a five-year period in a racial bias claim. The worldwide case was settled for USD 192.5m in 2000. In addition to gender, age and racial discrimination, the EAT and EEOC are recording increased claims statistics for discrimination on the basis of religion, disability, pregnancy, sexual orientation and even family responsibility.

WORKPLACE HARASSMENT

Harassment is usually defined within the constructs of an EPL policy as unwelcome advances, requests for favours or conduct (either sexual or non-sexual) that:

- a) are made a condition of employment,
- b) are used as a basis of employment decisions,
- c) create a workplace environment that interferes with job performance, or
- d) create a hostile, offensive or intimidating workplace environment.

Allegations of bullying often accompany harassment claims and usually the harassment is based on a factor or category that is prohibited by law, including sex, race, national origin, disability, etc.

Harassment by its nature is more likely to involve single plaintiff actions, and as a result, employers tend not to expect the settlement awards to be as costly. However, a recent suit brought against Deutsche bank in the UK contradicts this theory. The plaintiff alleged a deliberate bullying and harassment campaign over the course of her employment and was eventually awarded GBP800k in compensation for pain and suffering, loss of earnings, etc.. In the U.S., a similar harassment campaign can bring much costlier awards. UBS AG was sued in 2005 by a female director of one of its trading desks. She claimed bullying remarks had been made and was fired in retaliation due to her complaints about certain expense account cultures at the bank. The jury awarded USD9m in compensation and a further USD20m in punitive damages. Although UBS did appeal and the two parties subsequently settled, this single plaintiff harassment claim provides a stark warning to company executives.⁽⁴⁾

WRONGFUL TERMINATION OR DEMOTION / UNFAIR DISMISSAL

Of the 132,000+ claims filed in the UK in the 2006 to 2007 annual period in respect of EAT statistics, more than a third alleged unfair dismissal. Although the unfair dismissal award is capped at GBP60,600 claim costs can spiral if additional allegations which have no statutory limitation are tagged on to the original complaint. In jurisdictions where an employment contract forms the basis of the employment relationship, it is important to remove any contractual exclusions in the policy.

LIBEL / SLANDER / DEFAMATION OF CHARACTER CLAIMS

Allegations of slander or character defamation often occur after an employee has left a company. Failure to give an adequate reference is also deemed to be a defamation of character. A senior banker at Abbey National plc was bullied and harassed on the basis of her sex and failed pregnancy during her employment. Shortly afterward, she was made redundant. Ten years after her redundancy, she was researching her personnel file and learned that Abbey had not given any references to any other companies to which she had applied, thereby “destroying” her career. The employment tribunal agreed that she had suffered a defamation of character and awarded her GBP1m in compensation.⁽⁵⁾

WAGE AND HOUR DEFENCE COSTS COVERAGE

In the last year wage and hour defence costs coverage has been available in limited markets. This is of particular concern for companies with operations in the USA. Although usually sub-limited, and occasionally offered with a co-insurance payment, this coverage is an exciting new extension for companies. These “off the clock” claims allege that employees were forced to work unpaid extra hours, were not paid appropriate overtime, or were not given adequate breaks throughout the working day. The defence costs provision is especially pertinent as wage and hour claims can linger in the courts before they are granted class action status. Wal-Mart Stores, Inc. has been defending 20 wage and hour claims in recent years, nine of which have been granted class action certification. Court awards include a USD 198m judgement in the *Savaglio v. Wal-Mart Stores, Inc.* case, of which USD 115m comprised punitive damages and USD 26m comprised defence costs.⁽⁶⁾ Although currently under appeal, the cost of defending such actions is significant and any defence costs cover, even if sub-limited, can be helpful.

⁽³⁾ *Advisen MSCAd (Cases and Actions)*

⁽⁴⁾ *GenRe Loss & Litigation Report October 2007*

⁽⁵⁾ *GenRe Loss & Litigation Report October 2007*

⁽⁶⁾ *Wal-Mart Stores Inc. 10-Q for quarterly period ending 31st October 2007*



NEW TRENDS IN EMPLOYMENT CLAIMS

As employers are increasingly required to allow employees flexi-time and family responsibilities leave, a new class of discrimination has arisen. Family responsibility discrimination (FRD) – discrimination against employees who require time to care for family members, including parental leave, flexi-time, paternity leave, etc. – has resulted in an increase in EPL claims in the states. It is expected that these claims trends will increase elsewhere and this is an area that will be closely watched as companies strive to comply with legislation encouraging flexible working hours.

Another of the trends in EPL suits is the marked increase in retaliation claims by employees. In fiscal year 2006, the EEOC recorded allegations of retaliation in close to 30% of all EEOC charges⁽²⁾ The 2006 US Supreme Court decision in Burlington Northern vs. White widened the scope for retaliation claims when it held that a claim can be pecuniary in nature or result in termination for an action to be brought. This has been a growing area of concern in the USA and it is expected this trend to continue elsewhere.

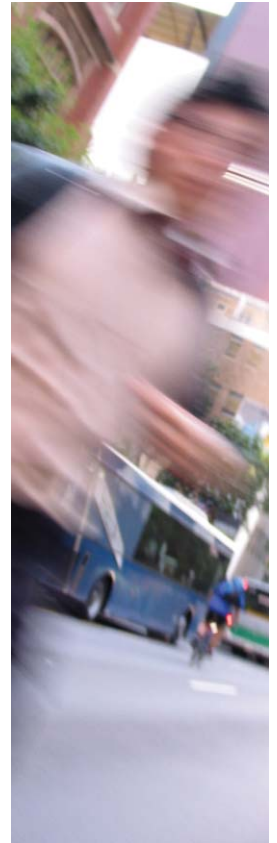
UPDATE ON CORPORATE MANSLAUGHTER AND CORPORATE HOMICIDE ACT 2007

In our Q1 2006 Index we looked into the crystal ball to examine the implications of the 2005 Bill “Corporate Manslaughter: The Government’s Draft Call for Reform” for directors and officers. Almost two years on the Corporate Manslaughter and Corporate Homicide Act 2007 will finally come into force on 6th April 2008. We thought it would therefore be timely to issue a brief recap of what the implications will be for directors and officers, and what changes, if any, have been made to D&O policies to reflect this new piece of legislation.

IN SUMMARY

There have been significant extensions in coverage under employment practices policies in recent years. High limit, broad-form catastrophe cover has been available in Bermuda, and markets that are able to offer punitive damages extensions are especially attractive. Punitive damages often accompany an EPL award, as in the UBS case. These are not solely limited to class action claims either.

As employment practice claims increase in frequency and severity, many companies are turning to dedicated EPL policies as protection. Willis is working in conjunction with some insurers to develop online risk management services, which include training on employee terminations, sexual harassment and model employment policies. Many coverage options are available, ranging from large limit/high deductible catastrophe cover for large global corporations to low retention options suitable for smaller private companies. Please ask your Willis Client Advocate for additional information.



WHAT IS THE NEW OFFENCE ?

An organisation is guilty of corporate manslaughter (in Scotland, corporate homicide) if the way in which its activities are managed or organised causes a death and amounts to a gross breach of a relevant duty of care to the deceased. The breach must have been significantly contributed to by the way that the organisation’s activities were managed by senior management.

WHO CAN BE LIABLE ?

The offence is applicable only to companies and corporate bodies operating in the UK. It also applies to partnerships, employers associations and trade unions if they employ people, and to Government departments and police forces.

The Act **does not apply** to individuals such as directors or officers. However, individuals can already be prosecuted for gross negligence manslaughter and for health and safety offences – the new Act does not affect this position.



PENALTIES

The Act imposes the possibility of unlimited fines upon organisations found guilty of the offence. In addition to the fine, the courts may require a guilty organisation to publicise details of its conviction and fine and may also impose remedial orders requiring the organisation to take steps to mitigate the risks that led to the death.

D&O INSURANCE

Most D&O policies contain an exclusion of claims for bodily injury, which would preclude direct claims against directors and officers alleging manslaughter. However in response to the draft version of the Corporate Manslaughter Bill, many insurers began to “write back” cover for the legal costs associated with defending a claim. While the intention here was positive, this did little to address the potential concerns of directors and officers who cannot be prosecuted for a Corporate Manslaughter offence.

To rectify this position, many insurers have now redrafted their policies to provide defence costs for directors and officers who are prosecuted for the existing offences of gross negligence manslaughter and other health and safety offences - providing some comfort that directors and officers will have the funds to defend themselves should they be faced with a prosecution.

Should you have any queries about the cover provided under your D&O policy, you should not hesitate to contact your Willis Client Advocate. For an electronic copy of our original guidance note in the Q1 2006 Index please send an email to d&o@willis.com.



Willis is one of the world's leading risk management and insurance intermediaries. We have approximately 16,000 professionals in over 300 offices around the world.

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