Umbrella Product Partnership Considerations

By Bob Jones

To some people an umbrella policy is a mysterious product, but it's merely a way of providing excess casualty insurance to personal homeowner and automobile policies, or commercial general liability, automobile liability, and other miscellaneous coverages for businesses. The earliest umbrella policies appeared in the late 1950s as demand for higher commercial liability limits was provided by Lloyds of London. According to research done by Jim Robertson, President and CEO of Interisk Limited, some of the early United States' markets include, "…Indemnity Insurance Company of North America (INA), in June 1957; Continental Casualty Company (CNA), in 1958; Employers Surplus Lines Insurance Company, in January 1959; and The Travelers Insurance Company, in September 1959. In 1960, American Reinsurance Company, Employer's Reinsurance Company, Employers Mutual of Wausau, and General Reinsurance Corporation also were reported to be markets for umbrella coverage."[1]

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Definition

Umbrella Insurance refers to liability insurance that is in excess of specified other policies, and it also may provide primary insurance in excess of a self-insured retention for losses not covered by the other policies. Umbrella insurance was named from a policy that is above other coverages, much like we use an umbrella above us to keep us dry from rain or snow. *Excess insurance* is similar in that it pays after an underlying primary policy is exhausted, and it follows the underlying form(s) to ensure that there is no "drop down" of coverage. The two terms are often used interchangeably.

Demand for umbrella or excess insurance

With the increase in lawsuit verdict amounts there has been an increased demand for excess limits of liability by both commercial and personal insureds. Because of the increased demand, companies that can offer excess limits of liability will help retain their good business and attract additional business that they may not have been able to write without the ability to provide excess liability limits.

Commercial insureds are seeing an increased demand by risk managers to provide limits of $5 million or more to comply with job bids, especially for larger corporations, and for projects in major metropolitan areas. Although the total commercial liability limits available vary, today larger national and global entities often purchase

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limits of up to $1 billion dollars. These limits are usually offered by specialty markets and Lloyds of London and are sold in increments of $25 million to $100 million dollars. Most regional commercial writers only need limits of $5 million to $10 million to fulfill their client's maximum needs, with nearly 90% of the business written falling in the $1 million to $2 million limit category.

The demand for personal and farm umbrella has increased over the past 20 years, as well, due to the increased verdicts and increased asset size of individuals. A simple search of state filings shows personal umbrella limits available of up to $100 million, according to one national carrier's filing. The limits in excess of $10 million are usually reserved for high net worth individuals, and they are typically written by companies that provide specialty programs for that specific market niche. Regional companies typically provide limits of $1 million to $5 million with the bulk of the policy count being in the $1 million to $2 million range.

An additional reason for the increased demand is that agents are encouraged to offer personal umbrella policies to their customers by their errors and omissions carriers, "By reaching out to your customers to notify them of the benefits and cost of a personal umbrella, you have further protected yourself if a customer is involved in a significant claim. Developing an umbrella campaign is a great way to identify exposures your agency does not insure and 'round out an account.' Additional sales will probably result, plus it's an effective way to enhance your agency's errors and omissions protection." [2]

I don't see the demand for commercial or personal/farm umbrella changing in the future. Without significant tort reform, I predict a continued growth in demand for increased casualty limits fueled by verdict size, risk managers' requirements, and insurance agents' errors and omissions carriers.

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Evolving Market

During my years of underwriting personal and commercial umbrellas, there have been many changes. First, and of utmost importance, is an increase in underlying limits attachments to keep up with severity trends over the years. This is most evident in commercial automobile where we see $1 million combined single limits as the most common attachment point, while many excess and umbrella writers require $2 million or higher limits for long haul exposures, hazardous hauling, or for larger fleets. Personal umbrella carriers are most commonly requiring $250,000/$500,000/$100,000 for private passenger auto today, when it was most common to require $100,000/$300,000/$50,000 five to ten years ago. There is a similar higher attachment trend for general liability requiring $1 million occurrence limits with a $2 million aggregate, and higher underlying general liability limits for hazardous classes. Comprehensive personal liability, including farm owners' liability attachments, have also moved up from $100,000 Combined Single Limit (CSL) to $300,000 CSL. Excess underwriters are increasing the retention for umbrella attachments in order to reduce the frequency of umbrella claims. Underwriters view the higher attachment as more valuable than rate increases to most cases, because the higher attachment can reduce frequency and improve profitability more effectively than rate increases.

In the modern underwriting environment, it is an underwriter's job to ensure that there is no known exposure that might expose an umbrella policy to first dollar losses. This is particularly important because the small percentage of premium charged is not adequate to pay first dollar losses. It is an umbrella underwriter's job to condition the umbrella policy to eliminate coverages that are not covered by the underlying policies. For instance, if the underlying general liability policy excludes coverage for mold,

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then the umbrella should also exclude coverage for mold. Another example of the need to condition the umbrella is in a case where there is a sublimit in the underlying policy, a limit of liability that is lower than the required attachment should be excluded in the umbrella, which is often the case in Cyber Liability where limits of $50,000 to $100,000 are common.

Companies continue to be more sophisticated in their excess pricing. In personal umbrella for instance, we are now seeing some companies use rating systems that consider financial scores and more detailed rating territories, and require sub-limits for certain coverages. Commercial trends include using manual premium as a base to price the excess layers, monitor price on a monthly basis, compare primary charged price against manual price, and use the higher of the two.

Language has also evolved. Most forms now follow form automobile liability to ensure there is no drop down exposure to the many different coverages in an automobile policy. Insurers have developed a myriad of endorsements to exclude exposures that either can't be underwritten, or require special attention to be supported by an umbrella policy.

As umbrella products become a larger percent of a company's casualty volume more attention is placed on the sustainability of the product. As such, companies are reviewing rates on a more frequent basis. Many companies are adding umbrella rate reviews to their scheduled profitability reviews rather than waiting for loss ratios to become problematic before making a change.

Reinsurance Partnership

Many primary companies rely on their reinsurer for assistance with umbrella underwriting because the exposure is often in excess of the their reinsurance retention. A good reinsurance partner should have the resources to support primary companies with guidelines, educational support and claims and underwriting assistance.

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The viability of a long term product is reliant on its profitability, so umbrella program rates should be a coordinated effort between the reinsurer and primary company, and the effort should balance the need for profitability with the requirement to be market competitive. A reinsurer dedicated to the umbrella line of business should assist with rate comparisons, pricing suggestions, and actuarial support if needed to support their company partners with state filing requirements.

Rates should be reviewed by the reinsurer and the company on a bi-annual basis to ensure the program is up to date, and to eliminate large rate changes from period to period, as significant increases will likely impact client satisfaction and client retention. More frequent, but smaller rate increases are more sellable than less frequent but larger rate increases. Commercial excess factors can be developed from rating entities such as the Insurance Service Office or the Association of Insurance Services along with public rate and loss data from state filings. While most service providers can provide policy support for personal umbrella, they don't provide pricing support. Personal umbrellas are usually proprietarily rated based on unit rates for an individual's owned property, number of automobiles, secondary dwellings, watercraft etc. Although many companies' personal umbrella parameters are similar, there are variances that make a rate analysis difficult. For that reason, comparative analysis and historical loss analysis are two ways of ensuring a personal umbrella program is viable over the long run. Reinsurers and primary companies should work together to prepare a personal umbrella comparative analysis and review rate adequacy on a regular basis to avoid significant changes in underwriting and rating guidelines.

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Maiden Re provides Property & Casualty Treaty reinsurance for standard property & casualty lines of business, providing coverage on both an excess of loss and pro-rata basis, according to the unique needs of each ceding company, with a focus on working-layer coverage, and umbrella programs., fostering close, collaborative client relationship.

[1] www.irmi.com/articles/expert-commentary/how-umbrella-policies-started-part-2-the-first-umbrella-forms

[2] www.insurancejournal.com/magazines/features/2013/06/17/295219.htm