SIMMONDS ON BANK INSURANCE

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Tougher Insurance Renewals Coming

I predict you're in for a bumpy ride if your bank's insurance is coming up for renewal over the next few months. I see big changes in the overall insurance marketplace for banks. There are actions you can take, though.

Over the last two years, many insurance agents have been telling their bank clients of the "hard insurance market." I have not seen it — until now. Most of the bank renewals I saw in 2009 and 2010 offered better premiums and/or better coverage than prior policies (some 50% better). Same thing early this year. A few months ago I started seeing changes as my $1 billion banks renewed. In July I started seeing signs that change was coming even to the smaller banks.

WHAT'S HAPPENING? What are the signs I see of a pending market change? Bank insurance underwriters are asking more questions about a bank's operations, financials, regulatory issues, and personnel. Insurers who would quote on any application submitted in the spring are now pulling back from quoting on certain banks.

Banks with July and August renewals saw premiums higher than those who renewed in June. In several cases, insurers declined to quote banks I am confident they would have quoted a few months ago. I am hearing push-back from underwriters on requests for higher limits of coverage. Banks in the renewal process are starting to be asked tougher questions.

There is also a distinct difference in how insurers are viewing banks with assets over $1 billion. Underwriters are much more cautious. I have not seen a three-year renewal on a billion-dollar bank in months and months.

Smaller banks seem to be lagging in the changes I mention above. I have several clients in the $100 million to $400 million range who have seen premiums below their prior policy premiums. Coverage terms are still fairly liberal. Most clients from $400 million to $900 million are seeing stable renewals and competitive terms.

There also seems to be a difference in underwriter temperament when there is competition from other insurers for an account. They do not want to lose a good account and are willing to fight. Competing insurers are pushing incumbent carriers with attractive terms, scrapping for new business.

By the way, commercial insurance buyers other than banks are still in a "soft market" (read: buyer's market). This is largely due to the capacity that continues to exist in the overall insurance market. There is no shortage of capital in insurance, and the slow economy is not stretching insurers to expand coverage. It's all supply and demand — the supply of insurance is high and the demand is stable or declining. Low prices are the result.

I'm not sure why the bank part of the insurance market is firming, relative to the rest of the commercial market. Maybe this is the start of an overall hardening of the market. Perhaps bank insurance is acting as bellwether.

WHAT SHOULD YOU DO NOW? If your bank's bond and/or executive risk insurance renewal is coming up, get started early.

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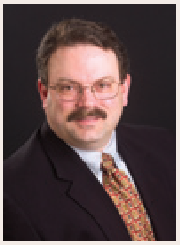
Bank Insurance Commentary | Dishonest Acts By Dishonest Employees



Ninety-five percent of bank bonds I review include a clause that excludes claims of embezzlement when the employee is known to have committed a past dishonest act.

The example I regularly use is of a 55-year-old teller who, when she was 17, stole a car.

Let's say that the employee has been a good employee for 15 years. One day, in a conversation with a bank officer, the employee reveals her youthful indiscretion. Nothing really unusual, two adults talking about their past. The officer goes on her way, noting how the teller has turned her life around. Two years later our "trusted" teller is found to have stolen $200,000 from the bank.

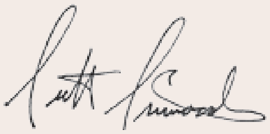
Won't you be surprised to learn that your bond excludes coverage, as 95% of bonds do? The standard language in most bond forms excludes coverage for an employee who is known by a bank officer to have committed a past "dishonest act." Further, most bonds do not define dishonest act.

Is coverage excluded for an employee who has "stolen" a pad of paper? How about an employee who has made personal phone calls, or surfed *ESPN.com* during working hours?

Your insurance may not give you guidance. Most would agree that each of these events are dishonest. How about telling a lie about being sick? How about being unfaithful to a spouse? How about an exaggerated claim on an employment application?

Some insurers put a dollar value on their exclusion so that coverage is only affected if the value of the dishonest act is more than $5,000 and has a relationship to the individual's employment. That, I think, makes sense. The current broad exclusion is needlessly restrictive, going well beyond the intent of most insurers. If you cannot get your insurer to define dishonesty, be sure your officers understand the restrictions of coverage. Anyone who becomes aware of an employee's past dishonesty should report the facts to an appropriate person at the bank. You can then put your insurer on notice so that waivers can be put into place.

I have drafted a letter that can be sent annually to bank officers reminding them of the bond policy clause, and helping you to avoid claims problems in the future. Better yet, get your insurer to define dishonest act.



Scott Simmonds, CPCU, ARM, CMC

Real Questions | Q&A | Real Answers

Q: Do I have to have debit card coverage on our bond if I have cyber liability insurance?

A: This points to a common point of confusion in bank insurance: "Why do we need a bond, D&O, and cyber liability?"

First, let's put some context in place. The bond provides coverage for losses to bank assets caused by fraud and theft. The bond is "first party" coverage — it pays for losses to your bank's money and assets. The peril is fraud.

Executive risk insurance (of which directors' and officers' is a part) is liability coverage. It protects the bank from the expenses of lawsuits and legal liability — actions against the bank by third parties.

- Bank robbery – bond
- Employee theft – bond
- Computer theft – bond
- Fund transfer fraud – bond
- Theft from an ATM – bond
- Debit card fraud – bond
- Stockholder suit – executive risk
- Employee discrimination suit – executive risk
- Suit brought by a mortgagee – executive risk
- ERISA suit – executive risk

Now to complicate matters: Many insurers do not cover liability coming out of your computer systems in executive risk policies. Therefore, a bank would need to buy a separate liability policy for such — AKA cyber liability insurance.

To the question… Debit card coverage is a part of most bonds. It protects the bank from losses due to fraudulent use of a debit card. The cyber liability policy does not come into play, as the loss is to the bank's assets. We need to add debit card coverage to a bank's bond, as the basic bond forms exclude incidents involving a debit card.

Note: Your questions for this section are welcome. Email *Scott@ScottSimmonds.com.*

Diary of a Typical Bank Insurance Review

Well over 75% of the calls I get are from bankers who want a review of their bank's insurance coverage. The process is straightforward. Send me your policies and other information. I'll review it, ask some questions, and report the issues I find. Once I get the info I need, I can finish a review and have your bank moving towards improved insurance coverage within 15 days.

Here is the timeline from one of my recent projects:

■ **DAY 1** CFO of ABC Bank emails me. He is interested in a review of his bank's insurance. We discuss his bank's situation, current insurance, and his objectives. The call takes less than twenty minutes. Later that night I email a proposal that outlines the project's objectives, accountabilities, and fee.

■ **DAY 5** The CFO gets back to me, asking to move forward. He signs the proposal and cuts me a check for my fee. I email him a letter to send to his agent requesting information for the project — summary of insurance, loss runs, and the like.

■ **DAY 8** I receive a box of the bank's insurance policies, sent by the CFO. I start my review of coverage. (Note: more and more banks are scanning their policies and emailing them. This speeds up the review process.)

■ **DAY 10** I receive information from the bank's current insurance agent. Since I have the info I need, I call the CFO and we set a date for the review conference call.

■ **DAY 15** I email the CFO a copy of my findings to be used in our phone call later in the day. At the appointed time we review the issues and I provide my recommendations. The CEO, CFO, and SVP of the bank are on the call. We set action plans and accountabilities for each issue. We set a date for the next conference call to review progress.

A Complete Insurance Review in 15 Days

To start the process, just send me an email at *Scott@ScottSimmonds.com* or call me at 207-284-0085. After a short conversation, I will send you a proposal, bank references, and everything you need to make the decision to go forward.

Once I complete a review of your bank's insurance, you will have a better understanding of your insurance. You'll know the coverage you have, and the coverage you don't have. You'll have specific recommendations on how to improve your coverage, and tactics to broaden your insurance protection.

It all starts with a phone call or an email. ■

Bank Insurance Teleseminar – October 18, 2011

Insuring Your Lender Risks - How your bank's insurance should respond to customers who fail to buy insurance, mistakes your lenders make, foreclosures, and other perils of the loan transaction.

- Mortgage Impairment
- Forced Placed Insurance
- Mortgage Error & Omissions
- Lender's Single Interest

Fast-paced, information-packed, unbiased insight into bank insurance coverage issues. Practical, easily implemented ideas every bank can use.

When: Oct. 18, 2011 – 1:00 p.m. Eastern
Where: Call in and listen from any phone

Bankers, register for free by emailing *Scott@ScottSimmonds.com* or go to *www.ScottSimmonds.com/teleseminar*. No obligation, of course. Seats are limited. Register now. ■

Listen To Our Prior Bank Insurance Teleseminars

AUGUST, 2011 – WHAT YOU SHOULD KNOW ABOUT YOUR BANK'S INSURANCE

JUNE, 2011 – D&O FOR DUMMIES

APRIL, 2011 – BANKER'S BOND BUGABOOS.

FEBRUARY, 2011 – BANK INSURANCE 101.

Email *Scott@ScottSimmonds.com* for free access. ■

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How Much Coverage? – Recommended insurance limits for banks. Do you have enough? Includes bond limits, executive risk, umbrella liability, cyber liability, and property insurance.

Questions to Ask Your Insurance Agent – Sixty questions to ask your insurance agent to help you understand your bank's insurance coverage.

How to Fine-Tune Your Bank's Insurance Program – Straight talk on your bank's insurance coverage.

Professional Gratitude

"As we approached renewal time for our insurance policies, our Board wanted to be sure we invested wisely in insurance and obtained adequate coverage. In the past, we've always relied on our existing agents for insurance recommendations. Having someone like Scott who knows the insurance needs of banks and doesn't sell insurance directly was something we felt we needed. His unbiased approach and expertise was something we lacked in the past."

- Tom Bevivino
Severn Savings Bank
Annapolis, MD

Continued from page 1

Involve multiple insurers in the process — perhaps multiple agents. Negotiate with your insurer. Policy terms and conditions can be improved right up until the time your policy renews — or when you have a claim.

If circumstances keep you from using alternative insurers and agents (due to community relationships, stockholder issues, claims, or the fact that your bank owns your agency) at least get your insurer to commit early. Push for renewal quotes 60 or 90 days before the expiration of your current insurance. Lock in terms.

Push for three-year policies. As the market changes, they will be harder and harder to get. Bigger banks, as I said before, are currently having trouble getting terms beyond a year. If you do get a multi-year policy, understand the terms by which your insurer can non-renew or amend the premium rates.

If you're in the middle of a policy period, there are still actions you can take to improve your coverage. Underwriters will consider coverage enhancements in the middle of a policy term — the terms just may not be as favorable.

The only time you cannot improve your insurance is after you're told a claim is not covered.

Consider a review of your insurance so as to know the issues presented by your current insurance. A review can also help you be strategic at your next renewal. Having a plan will put you in the best position. After a fifteen-minute phone conversation, I can get you a proposal that outlines my fees for a review and the process I go through. Send me an email or give me a call. ■

Get an advance copy of future issues of this newsletter plus additional commentary and ideas on managing your bank's insurance by joining my "Inner Circle." Just send me an email — Scott@ScottSimmonds.com *— and I'll send you the super-secret-coded website. No obligation.*

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