Is Reputation Insurable? Some Carriers Think It Is

By **Ganesh Setty** · 2023-03-24 15:43:29 -0400 · Listen to article

Corporations are certainly no stranger to social media's growing influence on balance sheets and public relations nightmares borne by the 24-hour news cycle, like Adidas' recent termination of its partnership with Kanye West following his antisemitic statements, or backlash United Airlines faced in 2017 after a passenger was forcibly dragged off a flight.

Insurers have now started to step in and offer products that cover the actual drop in business a company may suffer from a hit to its brand or reputation, although the market is still in its infancy.

"The proportion of the asset base of larger companies, and for the majority of companies these days, has shifted from the tangible and physical to the intangible. Reputation and brand are a core part of that," Neil Kempston, head of Beazley's Incubation Underwriting team, told Law360. The team focuses on designing, testing and underwriting new insurance products.

While certain insurance policies, such as those covering ransomware cyberattacks and data breaches, already provide reimbursement for public relations and crisis consulting costs associated with some events, they stop short of covering the actual loss of a company's reputational value.

Such products "tended to focus on less about the reimbursement of loss value because it's a challenge to quantify," Scott Bolton, director of Aon's GBC Crisis Solutions, said, adding that the reimbursement for reputational loss itself is a "much more recent phenomenon."

"And I think perhaps part of this change in the insurance space is we're all becoming more articulate because our clients as well are moving ahead with how they look at reputation and how they place reputation within their assessment of risk to the organization," Bolton continued.

As Reputational Risk Concerns Rise, Insurers Respond

According to Aon's global risk management survey, corporate executives have consistently ranked damage to brand or reputation as a top-five concern since the brokerage launched the survey in 2007, Bolton noted. With these concerns on the rise, a number of insurers have started to provide policies designed to respond to reputational damage.

In the case of Beazley, a publicly available sample reputational harm insurance policy contains provisions covering a company for costs it incurs in mitigating reputational harm, costs from responding to some event and the actual loss of reputational value itself.

"What has been missing is an all-risks proposition for this amorphous topic," Kempston said, adding that buyers of Beazley's reputational harm policy, while tailorable to the needs of an individual policyholder, are "typically reasonably large or sophisticated organizations with one or more public-facing brands."

All-risks insurance generally aims to provide coverage for any risk that a given contract does not explicitly exclude.

The policy provides coverage for lost operating profit by taking the difference between expected revenue and actual revenue following some negative reputational event and then multiplying that difference by a pre-agreed operating profit margin, further subtracting any other applicable insurance, including business interruption coverage, that is otherwise available.

That value is then multiplied by a pre-agreed "allocation percentage" representing the proportion of profit loss Beazley will cover following an insured's payment of a self-insured retention, Kempston said, adding that the percentage "can be 70% but can be varied depending on the risk."

Beazley generally requires a revenue gap of at least 10% for coverage to be triggered and further assesses reputational loss in three-month chunks across a 15-month indemnity period, Kempston said.

And in the case of a coverage dispute, a policyholder and insurer can choose a forensic accountant whose sole mandate is to determine whether there is a causal link between some reputational harm and reduction in revenue, or whether there has been a reduction at all.

But other reputational harm policies, such as those from Steel City Re, take a different approach. Steel City Re instead offers parametric coverage, in which after some reputational loss, the insurer automatically applies a preset coverage amount based on the level of reputation impairment once a policy is found to be triggered.

That makes the need for any adjuster or forensic accountant a "nonissue," Nir Kossovsky, the company's CEO, told Law360, adding that the insurer requires an "initial quantitative impairment" to occur within 90 days following some reputational event, and the impairment must persist for at least 140 days.

"It's really not much more complicated than determining the cost of loss in a total automobile wreck, where the adjuster looks up the vehicle, make, year and mileage of a car in a table, usually Kelley Blue Book, and based on the KBB model, declares the value of the loss," he said.

Kossovsky described Steel City Re's offering as an "ecosystem" that provides an "intelligence-based" risk management and oversight process, an insurer's third-party authentication of that process and a communications strategy, which he said can be especially helpful as companies grapple with ESG-related strategic decisions.

The value of such a product "comes from various stakeholders' appreciation that a firm has put in place an effective, insurance-authenticated quality risk management and governance system overall that is mission-critical," Kossovsky continued, "because insurance can tell a story of quality that is simple to understand, completely credible and convincing."

The bond market also values the use of reputation risk insurance because it stabilizes cash flow and the equity markets, since the product can help reduce the risk of a panic-driven sell-off, what Kossovsky called the "hallmark of a reputation crisis."

Court Battles Have Yet To Arise

Given its novelty, coverage of reputational loss itself has not yet been tested by the courts, Tamara Bruno, a Pillsbury Winthrop Shaw Pittman LLP partner who represents corporate policyholders, told Law360. And according to Aon's Bolton and Beazley's Kempston, as of early March, no claims have been filed yet on the respective insurance products they offer covering reputational harm specifically.

Bruno further highlighted provisions in the sample Beazley policy that she said prospective policyholders should be aware of.

Under its so-called strategy cooperation provision, if the insurer recommends any strategy "to mitigate or minimize any actual or potential harm" and the insured opts to manage an event on its own, coverage is excluded for pre-loss crisis mitigation costs and crisis costs incurred after the point the insured followed its own course, but not the reputational loss itself.

"Larger companies would not be happy if the insurance company got to tell them how to respond to a crisis," Bruno said. "Maybe that's OK for smaller companies that might not have a lot of sophistication on this anyway ... but once you get to a certain size, executives may not be willing to do that off the bat, so that's certainly something companies should think about."

Aside from the usual exclusions barring coverage for deliberate fraudulent or criminal acts, for example, the policy also contains a "formal business and corporate strategy" exclusion barring coverage for loss "arising from the failure or nonperformance of any business or corporate strategy that has been expressly considered at the insured organization's senior executive level."

"It seems like that exclusion has a significant possibility of being invoked for many of the things that you would think this would otherwise respond to," Bruno added.

For the insurer's part, Beazley's Kempston called the provision a "moral hazard exclusion" intended to protect the insurer from situations where an insured "elects itself into a scandal, for whatever reason that may be," noting that "it would be rare for that to happen."

"If there is an intended advertising campaign that backfires, the product is designed to respond to this type of event should no other exclusions apply," he said.

The Beazley policy's use of a revenue growth trend in the calculation of expected revenue is also something to keep in mind, Bruno continued. She said that if a company's revenue was trending downward for quite a while before some negative reputational event, the size of the resultant revenue drop from the event may need to be significantly larger for the policy to be triggered.

And given that the policy excludes from its calculation of reputational loss value any separate, applicable insurance coverage a policyholder may have, such a provision tees up the possibility of further unexpected coverage litigation, Bruno added.

"Usually more insurance is better, but it's unfortunate that insureds sometimes do get stuck in the middle of inter-insurer disputes," she said.

Reputation Coverage Faces Obstacles To Growth

> Over the long term, Kempston said one of the obstacles in growing the product is that it involves another premium for companies to spend, which he said brings some challenges given the prevailing market conditions.

"Often there are companies that need the limits to be much bigger. That's just a part of growing a new product into a new area, which becomes easier as you grow a portfolio," he noted, adding that the maximum coverage limit Beazley can provide currently is $20 million per risk.

Reputation insurance policies Aon offers, meanwhile, typically provide up to $5 million to $15 million in coverage, Bolton said.

"Look at cyber insurance eight years ago, and it's probably pretty shocking," Bolton continued. "Cyber insurance now is much more articulate as clients, brokers and markets collectively have taken that journey forward and we understand the peril much better. I think the same could be said around reputation."

If a dispute on reputational loss coverage eventually makes its way to court, Jassy Vick Carolan LLP partner William Um said business interruption disputes concerning the specific value of a given loss, such as hurricane or flood damage cases, can provide a roadmap for what reputation insurance disputes may look like.

While reputation is certainly insurable in theory, the amount of coverage the market can provide and the corresponding premiums required are key factors in whether the largest companies will consider purchasing such policies, Um agreed.

"Almost everything is insurable. It's just a matter of what the price is," he said.

--Editing by Emma Brauer.

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