Regulatory Crackdown on Hedge Funds Drives Rates Higher for Insurance Covering Lawsuit Costs

Insurers Quoting Rate Hikes of 5% - 10% for Directors and Officers and Errors and Omissions Coverage Due to Supply and Demand, Insider Trading and MF Global Collapse, Says SKCG Group

White Plains, NY – March 13, 2012 – Call it the "Galleon Effect." Anticipating more insider trading investigations and investor lawsuits as well as increased claim payouts, insurance companies are asking for higher rates for hedge funds' Directors and Officers (D&O) and Errors and Omissions (E&O) insurance after more than two years of price cuts. According to an analysis by SKCG Group, the risk management and insurance advisor to many of the world's largest hedge funds, carriers are quoting average rate hikes of between 5% to 10% for this insurance that fund managers buy to protect themselves from the costs of investigations and lawsuits. Even the best-run hedge funds are beginning to see requests for increases, while insurers want premiums that are 15% higher, or more, from fund managers with poor performance and large redemptions.

Insurance companies are responding to expectations of a more aggressive approach by regulators towards Wall Street as fraud and debacles such as MF Global continue to dominate the headlines and force carriers to pay out more claims. The SEC is focusing on compliance issues, including insider dealing and the role of expert networks, while the FBI says it has enough information to keep its investigations of suspected illegal insider trading at hedge funds going for at least five more years.

"Insurance carriers know that hedge funds are in regulators' cross hairs," said Richard Canter, President and Chief Operating Officer of SKCG. "More than just insider trading, the SEC is cracking down on a variety of areas and, when regulators come knocking, the cost to defend these funds is seldom cheap and the insurers may be on the hook for it."

Investigations and any resulting law suits can cost tens of millions of dollars, according to Canter. At the deposition stage, a fund can burn through as much as $1 million a month.

The cost of E&O and D&O insurance had declined in recent years, to the benefit of hedge funds, as insurance companies initially increased rates following the Madoff scandal, expecting a flood of lawsuits and investigations. Those lawsuits did not materialize as predicted, making this niche of the property and casualty insurance market particularly attractive to the new insurance company entrants who flooded in. Combined with the fact that fewer hedge funds were launched in the wake of the 2008 credit crisis, this created more supply than demand for coverage, and drove premiums down dramatically, sometimes by as much as 50% for smaller, newly-launched hedge funds.

SKCG predicted last year that increased regulatory actions would drive insurance costs higher and had recommended that hedge funds take advantage of the low rates and broad coverage terms while market conditions were favorable. Prices still remain attractive on a historical basis, SKCG is quick to point out, but may not remain this way for much longer.

Because supply remains greater than demand, insurance companies may not always get the rates they are looking for, says Canter. "But clearly, they are starting the conversation with requests for 10 percent increases, and are eyeing those higher 2009 price levels as a goal for the next few years," Canter added.

About SKCG Group

SKCG Group is one of the largest privately-held insurance and risk management advisory firms in the United States. SKCG serves U.S. and international commercial and private clients who require sophisticated advice addressing multiple risk factors. SKCG's technical expertise in identifying and analyzing risk, coupled with its ingrained culture of senior-level attention and client service, results in high levels of customer trust and loyalty. From insurance and private client services to group benefits and retirement planning services, SKCG's marketplace success is due to its industry knowledge, analysis, experience and unique carrier relationships. Among SKCG's numerous disciplines are Real Estate Owners and Developers, Financial Service Firms including Asset Managers and high net worth individuals and families. SKCG is a subsidiary company of AssuredPartners, Inc. To learn more please visit www.skcg.com.

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Media Contacts:

Will Thompson
Hedge Fund PR
(267) 221-6056
Will@HedgeHundPR.net

Mitch Ackles
Hedge Fund PR
(305) 444-9868
Mitch@HedgeFundPR.net

SKCG Sales Contact:

Richard Canter
President, COO
(914) 761-9000
RCanter@SKCG.com