



Key Person Insurance Counters Daring Executives

The fatal plane crash that killed Micron's CEO, Steve Appleton is causing a stir of news reports regarding corporate succession planning and disclosures that should be brought to the board of director's attention. Due to their strong personality traits, CEO's are used to taking risks and many engage in adventurous and extreme activities. Even more importantly, CEO's have great incentives to continue growing a corporation and don't want to be told what and what not to do in their business or personal life.

Risky activities like rock climbing, car racing and piloting aircrafts are all expensive hobbies relished by many executives. Take for example Virgin Group's leader, Sir Richard Branson, who has ambitions of breaking world records, specifically circumnavigating the world in a hot-air balloon. Meanwhile, Larry Ellison, the CEO of Oracle Corporation, is an avid sailboat racer. He won the America's Cup in 2010, but more notably won a previous race in which six sailors perished.ⁱⁱ Oracle's shareholders may not be thrilled knowing the leader behind their investment is racing schooners in treacherous conditions on his free-time.

While studies show that there is a strong correlation between CEO's and risky activities, it's not the particular hobby that is of concern. Rather the real issue is the shareholders and investors having no idea if their corporation's leader is partaking in these activities during their free-time. Obviously the difference in danger between two hobbies such as motorcycle racing and playing chess is significant. The threat of an untimely death or disability of a CEO can cause a multitude of problems for a company. Moreover, a company without a proper succession plan in place will surely suffer if a CEO should be unable to work because of a freak accident.

Legally companies are not required to disclose a CEO's risky hobbies to shareholders.ⁱⁱⁱ "The Micron tragedy should be a wake-up call for boards," says William M. Mower, a partner at law firm Maslon Edelman Borman & Brand LLP.^{iv} The shareholders are investing in the firm. If the CEO could die at any moment because of some risky activity, the shareholders deserve to know about it.

While some are advocating it should be a legal obligation to inform the shareholders of a CEO's risky activities, others argue that disclosing hobbies to a board of directors is an invasion of privacy. Hobbies are meant to serve as a break from work – a form of enjoyment and stress relief. They are also chosen on a voluntary basis – meaning that there is passion behind pursuing a specific hobby. Gerard Arpey, a private pilot and former head of AMR Corp. claimed that, "Flying a pair of older prop planes for fun during his eight years running AMR 'was the thing that took me away from the madness of the airline business.'"^v

What is considered a risky hobby? Where do shareholders draw that line?

Piloting airplanes can be viewed as a dangerous hobby, but is it really? With the adequate amount of training and education, piloting a plane is not a risky activity. Compared to the amount of cars operated worldwide on a daily basis, there are much fewer aircrafts commuting across the sky. Logically there are not nearly as many plane crashes as there are automobile accidents. When a plane crash does eventually occur it becomes instantaneous headline material. Therefore as long as the CEO is an educated pilot, commuting to work in a private jet is not any more hazardous than driving their Lexus to the office.

The same concept of having the proper education in a particular hobby can be used to argue plenty of other activities of CEO's. Whether it's hunting, piloting or parachuting, the proper training in the respective hobby will mitigate the risks. Nonetheless, drawing the line between what is considered risky and what's not is a gray area. In other words, while someone can be an educated sailor, the risks associated with oceans such as extreme weather conditions and predatory fish still linger as a potential threat.

Inevitably, CEO's have earned their spots as the elite of the business world. They have the ability to do what they want. If boards tell them they will lose their jobs if they fly personal planes – they will simply move to a competitor where they can earn the same income and pilot their Czech ex-military jet whenever they wish. After





TOKIO MARINE
HCC

puncturing a lung in a 2004 non-fatal airplane crash, the late Micron CEO, Steve Appleton stated, "the older you get, the more risk you should take." Enough said.

Statistics show that the chances an American will become disabled for one year or more during their working career is 1 in 5.vii Given the extreme hobbies that CEO's tend to participate in, this ratio becomes even smaller. How can a board of directors combat this issue and protect their investment?

As of now CEO's are under no obligation to inform their board of directors of their hobbies. Stakeholders need to take other measures to insure their investment in a particular corporation or even its CEO. Key person life and disability insurance serves as an alternative form of financial risk management for corporations. This type of corporate planning helps minimize both the human capital and financial risk exposure to the company and ultimately, to shareholders. In fact, until CEO's are forced to disclose if they go sky-diving every weekend, key person insurance is the best form of protection for the future profitability and viability of the corporation. As a third-party purchased coverage, key person insurance will name the CEO as the insured and the company as the owner and beneficiary. Therefore, if the CEO is unable to work because of an injury sustained while piloting their own plane, the policy will pay a lump sum to the corporation.

In addition to key person insurance, HCC Specialty's Prestige Group has a number of disability solutions for high net-worth individuals. From executives to entertainers, HCC Specialty has the limits large enough to provide sufficient coverage for these individuals.

Contact

Kathy Bouras
kbouras@tmhcc.com
781-994-6000



Tokio Marine HCC- Specialty Group is a market leader in providing specialized insurance products for the sports, entertainment and promotional industries. We provide an unmatched portfolio of products including event cancellation, high limit disability, kidnap and ransom, weather, travel, event liability and much more. We cover major sports and entertainment events, professional athletes and entertainers and other unique assets.

Tokio Marine HCC - Specialty Group

401 Edgewater Place, Suite 400 Wakefield, MA 01880 781-994-6000

A member of the Tokio Marine HCC group of companies