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What drives corporate insurance demand? Evidence from directors' and officers' liability insurance in Korea

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What drives corporate insurance demand? Evidence from  
directors' and officers' liability insurance in Korea \*

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**Abstract**

This paper provides empirical evidence that increasing risk results in higher demand for hedging among firms. Through a natural experiment exploring the Korean Government's legislative change on shareholder class action, I show that firms increase the liability insurance coverage for their directors and officers in response to increased litigation risk, despite the increase in costs associated with buying further coverage. I further test the heterogeneous effects in two dimensions of corporations: industry classification, and type of shareholder-management relationship. The results confirm that firms in high litigation risk industries and those with high agency conflicts between shareholders and management increase their insurance coverage relatively more. Overall, the results demonstrate that corporations adjust their hedging demand in response to changing risk environment and that the adjustment depends on the level of risk exposure of individual firms.

*JEL classification:* G22, G32, G34, K22

*Keywords:* Corporate insurance demand; D&O insurance; Shareholder class action; Law change

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