



**HUB**



Broker Insight Report:

## **How Insurance Oversights Can Lead to Devastating Claims Denials**

# **DIRECTORS AND OFFICERS (D&O) LIABILITY**

# DIRECTORS AND OFFICERS (D&O) LIABILITY

Every public, private and nonprofit organization needs to be protected from within.

It may be hard to believe, but when you take on an executive role, you are putting your personal assets on the line. At the same time, your employer is taking a chance by putting you in charge of its daily operations, financial decisions and the overall future direction of the organization. A Directors and Officers (D&O) Liability policy will protect both you and your organization from the consequences of the decisions you make as an executive. Think of it as corporate and personal asset protection.

If a claim is brought as a result of a corporate decision you make, your D&O policy will kick in. Without one, you could lose the business **and** your personal assets. Your house, your cars, your child's college savings plan, your 401(k) and any other investments could be placed in jeopardy.

With the recent rise in D&O claims, many organizations that previously did business without this coverage are now seriously considering it.

As many as

# 31%

of businesses reported claims against their D&O Liability policies in the last five years, with nonprofits reporting the highest proportion of claims at 58%.<sup>2</sup>

**A breakdown of claims** experience by private companies shows that:

- **46%** were shareholder lawsuits
- **33%** were customer lawsuits
- **21%** were vendor lawsuits<sup>3</sup>

<sup>2</sup> Advisen Ltd. 2016 Advisen's Master Significant Cases & Actions database (MCSAd)

<sup>3</sup> Advisen Ltd. The Private Eye — A Spotlight on the US Private E&O Market (August 2013)

## A Few FAQs about D&O Policies

### Q: Who does a D&O policy cover?

A: A D&O policy protects current, past and present directors, officers and employees if they're named in a lawsuit that is either brought against them specifically, or brought against the company.

### Q: What's the difference between a D&O and a Professional Liability policy?

A: While a Professional Liability (also known as errors and omissions or E&O) policy covers you when a **client** sues for negligence relating to a professional service, a D&O policy covers exposures from internal corporate decisions, including lawsuits brought by creditors, vendors, suppliers, investors and competitors, state and federal regulators and shareholders.

### Q: Isn't D&O insurance just for public companies?

A: For public companies, direct shareholder or investor suits and derivative suits are leading causes of D&O claims. Privately owned companies don't face the same risk, but still need D&O insurance to protect them in the relationships they have with creditors, vendors, suppliers, competitors and regulators.



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**If my company is privately held, I might look at my ownership and say, I don't even have people on a board, or shareholders, so why do I need D&O?**

The D&O policy should really be called Personal and Corporate Asset Protection — and that's something everyone needs. A privately held company or a nonprofit, even without multiple shareholders, has to deal with creditors, vendors and business partners. If the organization goes into financial distress or bankruptcy, their vendors, suppliers, landlords and others will all be considered creditors. And all organizations deal with state, federal and local regulatory bodies that can investigate alleged improper conduct.

— Executive Vice President



## Top Five D&O Claims Denials

Even when you have D&O insurance with adequate limits, there are a number of reasons your claim could be denied. Here are the top five:

### 1. LACK OF ANTITRUST OR UNFAIR TRADE COVERAGE

A standard D&O policy may not cover your company for many common claims brought by your competitors or regulators.

### 2. OVERLY BROAD EXCLUSIONS

You should closely examine potential exclusions in your D&O insurance to make sure that coverage for your key areas of risk overlaps and doesn't potentially exclude a core part of your business.

### 3. OVERLY BROAD CONDUCT EXCLUSIONS FOR CRIMINAL ACTS/ILLEGAL PROFITS

Most D&O policies will contain personal conduct exclusions for actions relating to illegal profit, fraud and/or deliberate criminal acts by directors and officers. While there may have been no such activity on your part, many suits allege such claims and the policy must be properly worded to ensure you are afforded sufficient coverage to defend yourself.

### 4. COVERAGE EXCLUSION FOR CERTAIN REPRESENTATIVES OF YOUR BUSINESS

If a former company insider brings a lawsuit against you, the lawsuit could be excluded. Check your policy. It is important to closely analyze these exclusions to ensure they are not too restrictive or too favorable to the insurance carrier.

### 5. LATE REPORTING

Failure to report a claim in a timely manner could cause it to be denied. Though easy to avoid, this is one of the most common reasons for coverage denials. Your insurer will likely have an obligation to defend you, but will also require adherence to certain guidelines in order to maintain the defense. Make sure you understand your obligations to report claims and what role your insurer will play in the process.

## Real D&O Claims Stories

### **Unintentional breach of contract leads to D&O claim for nonprofit organization**

An inner-city, nonprofit organization that aims to help teens stay off the streets contracted a food truck for its annual picnic. Unfortunately, the organization was forced to cancel the picnic less than 24 hours before it was scheduled to begin. While there was no cancellation clause in the contract, the food truck owner sued the nonprofit for the cost of food and paper goods already purchased, along with employee salaries. The nonprofit's D&O policy covered the costs to defend the suit.

### **Lack of business planning leads to a D&O claim against a private company's board of directors**

When the head of a private shipping supply manufacturer passed away unexpectedly, it was left to the board of directors to choose a successor. Unfortunately, the man they chose promptly drove the business into the ground. A relative of the original leader sued the board for negligence in business succession planning. The company's D&O policy protected the board members and paid for their defense.

### **Executive of a publicly owned toy company is indemnified by the business's D&O policy**

A toy company on the verge of bankruptcy couldn't afford to pay its biggest creditor. Because the company lacked the capital to pay, the creditor went after the company's CEO. The CEO asked the company to pay his defense costs, but the company couldn't — it no longer had the capital. Instead, the CEO made a claim on the company's D&O policy, which responded, provided a defense and indemnified him.

## Protect what matters most.

Learn how directors and officers liability can protect you and your board from stakeholder claims.

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