Directors and Officers Liability Insurance for Nonprofits

Many nonprofits, particularly those that are newly formed or in the startup mode, report some difficulty affording the cost of D&O insurance. Nonprofit buyers have many options. Those wishing to shave dollars off the annual premium can often do so by choosing only those policy provisions considered most critical. Many insurers offer a range of policy forms containing various provisions. For example, a volunteer-run nonprofit without paid staff may forego employment practices coverage until it hires staff. Two other alternatives are available. First, some insurance agencies offer premium financing - even on a relatively low cost liability policy. If affording a lump sum premium is a concern, inquire about the availability of premium financing from your insurance provider. Finally, some start-up nonprofits address the question of cost by charging each board member a fraction of the policy premium.

How do we know if were paying too much for D&O?

There is great variation among nonprofit D&O policies. Due to the differences in coverage, premiums will vary, too. When evaluating D&O policy costs, you have to review the premium in relation to the polices coverage, limits and deductibles. Another way to determine if you are paying too much is to request quotations from different insurance companies. Consider securing competitive bids every three to five years.

Several members of our board are active on other nonprofit boards. Will our D&O policy protect their outside activities?

Most policies exclude coverage for claims resulting from any insured serving another organization. The rationale is that as a long-standing rule of risk management, "dont assume liability for activities that you don’t control." Check your policy for a provision that limits or excludes coverage for "outside" board or volunteer activities.

Directors and officers are insureds under my commercial general liability (CGL) policy. Why do I need D&O?

Including volunteers under a commercial general liability policy (CGL) is a good idea but it does not provide "complete" protection. A CGL policy insures a nonprofit for very different types of claims than a Directors & Officers Liability policy. The general liability policy protects the organization, its directors, officers, employees and volunteers (if endorsed as an Additional Insured) for claims arising from bodily injury and property damage. The policy covers the negligent acts of the "insureds" that cause injury to another person or damage to the property of another (subject to policy provisions).

In contrast, a D&O policy insures against the "wrongful acts" of the organization, its directors, officers, employees and volunteers (depending upon the definition of "Insured"). Each policy defines "wrongful act" differently, but in general it means the actual or alleged acts or omissions including breaches of duty that the directors, officers or other insureds may perform. Most D&O policies exclude coverage for bodily injury or property damage, unless the policy includes

Employment Practices Liability (EPL) coverage. The EPL form usually includes coverage for emotional distress and other bodily injury type allegations contained within the claim.

Since these two policies cover very different risks, the D&O policy should also include volunteers as "insureds." Most nonprofits use committees to perform many of the governance and management functions. The membership of the various committees often includes non-board member volunteers. For example, a Risk Management Committee can include board members, an insurance agent, an attorney and other volunteers. The committee and its members could be named in a claim alleging that the committee failed to purchase adequate insurance. A commercial general liability policy would not cover this claim since the occurrence does not include bodily injury or property damage. A D&O policy would probably respond (subject to policy provisions) to the allegation of a "wrongful act." Therefore, each organization should evaluate its own insurance needs and consider purchasing both D&O and commercial general liability (CGL) insurance policies.

Our state law protects us from suits against our directors and officers - isn't that enough?

In all but a handful of states - New Jersey and Virginia are examples - the doctrine of charitable immunity has been abolished. In states that do not recognize charitable immunity, nonprofits can and are held responsible for negligence stemming from foreseeable harm. During the past decade, nearly every state has adopted volunteer protection legislation. These laws provided limited immunity for certain volunteers - not nonprofits - under certain circumstances. The federal Volunteer Protection Act preempts state laws except when they specifically provide greater protection. The VPA and its state-based counterparts do not prohibit suits. Even if one of these laws allows your volunteers to escape liability, substantial funds are required to defend even a frivolous claim. D&O coverage typically covers the defense costs as they are incurred.

Twelve Buying Tips for Director and Officer Liability Insurance

1. Solicit competitive bids on your insurance program every three-to-five years. Competition is one way to determine whether youre paying a fair price. However, be careful that the policies offer comparable coverage - a lower premium often means less coverage or the insurer may be "low-balling" to sign you up. Future increases may be necessary.

2. Allow sufficient time for an underwriting review - particularly with a carrier unfamiliar with your nonprofit.

3. Fully complete the carriers application and attach all requested supporting information. The information requested generally includes your bylaws, board roster, and audited financial statements or IRS Form 990. Some carriers request a copy of your employee handbook. Present your nonprofit in the best light and emphasize any activities underway to minimize losses, such as training supervisors on employment practices. Do not view the application process as a burdensome paperwork requirement, but as an opportunity to protect your nonprofit and conserve scarce resources.

4. Identify an insurance adviser - a broker, agent, or consultant - with experience working with nonprofits. A specialist can be invaluable as you try to understand the D&O options available to your nonprofit.

5. Be accurate and truthful in answering questions on the application. Misstatements on the application may void coverage if discovered upon the filing of a claim.

6. Respond to the underwriters questions (usually conveyed through your insurance advisor) promptly.

7. Fully disclose your nonprofits prior losses and provide details on corrective action taken to avoid future losses.

8. Remember that coverage and pricing terms are negotiable. If any specific terms are unacceptable, propose alternatives. For example, if coverage for employment practices is excluded, inquire about purchasing coverage via endorsement. Or, if the policy indicates that the insurer has sole authority to appoint defense counsel, inquire about the possibility of a policy form that allows the insured to participate in the selection of counsel.

9. Review the extent of the "prior acts" coverage provided by the policy. Seek coverage for incidents dating back to the inception of the nonprofit. (A great deal if you can get it!) If the policy contains a retroactive date make sure that the date stays the same with each renewal or new policy.

10. Make certain that any prior incidents that might potentially give rise to a claim are reported on your application to a new carrier as well as to your existing carrier. Claims stemming from known incidents will be excluded under your new policy.

11. Request information on the carriers financial strength and status ("admitted" versus "surplus lines") and have your broker explain the ratings to you. Ask your broker about the carriers history on handling D&O claims against nonprofits. If youre considering an alternative market (i.e. a charitable risk pool, or risk retention group), or a sponsored insurance program, make similar inquiries.

12. Consider the benefit of various loss control programs offered by your D&O carrier. With an estimated 60 companies now offering nonprofit D&O coverage, a growing number are providing useful loss prevention services, such as access to toll free employment practices hot lines. Risk education services can greatly enhance a D&O insurance program. Ask about available services when you request a quotation.