

You're a Board Member — Manage Your Personal Liability and Risk Exposure



You've been invited to serve as a director or officer on the board of a corporation or nonprofit. This is an exciting opportunity that also comes with potential liability exposures across several areas, including employment and fiduciary liability.

Nonprofits and corporations have unique risks. In general, larger companies mean greater risks, but the cost to defend and settle a lawsuit isn't relative. If a smaller nonprofit is accused of mishandling donations, it might bankrupt the entire organization. And while larger corporations have deeper pockets, the cost to defend a multilayered lawsuit out of pocket could mean the difference between sinking or swimming.

Wells Fargo recently settled a derivative lawsuit for \$240 million against its own directors and officers named in a 2016 bogus accounts scandal, according to a January 9, 2020 CNBC article. Insurance paid the settlement as part of the organization's directors and officers (D&O) policy — an otherwise hefty out-of-pocket expense for those personally named in the lawsuit.

Are you personally liable for a company loss?

The short answer is yes. As a board member, you could be held personally liable for the decisions and actions of the board, even in the case of impropriety on the part of other members. A lawsuit might name everyone at an organization, including board members, before a determination is made. This leaves you open to risk and exposes you to potential liability, especially if your board doesn't have appropriate insurance.

In the news — how liability is playing out

The Boy Scouts of America (BSA) is currently facing allegations of nearly 100,000 incidents of abuse. BSA is claiming insolvency, filing for bankruptcy and looking to liability insurance for coverage. But insurance companies are pushing back on the liability claims, saying they should not have to pay for the organization's preventable negligence, according to a November 2020 PropertyCasualty360 article.

The legal team for the alleged victims is seeking other sources of solvency to name in the lawsuit, including local BSA chapters. The litigation is still unfolding, and probably will be for some time, but it highlights the nuances of liability, prevention, good-faith efforts and key decision-makers with oversight into all those areas.

Limits and expectations of board members

As a board member, you're expected to take your duties seriously and make reasonably informed decisions. But you're not expected to guarantee results or prevent setbacks. The business judgment rule can protect directors and officers from the effects of honest mistakes, provided they were made in good faith.

You'll still need to provide evidence of good faith (such as meeting minutes, training and other reasonable care actions) when responding to accusations. You'll also need to mount a legal defense, even if you're ultimately found innocent, which can be costly if you're not covered by your organization.

Who's at risk? It's on a case-by-case basis

No organization is too small to create some form of D&O liability if its directors and officers have discretion over money and other governance issues. This can include condo boards, nonprofits, schools, churches, associations and for-profit corporations. There's a lot of liability spread across an ever-growing canvas of industries.

Small organizations — even without a lot of money, lawsuits can happen

As a practical matter, local groups such as churches, parent-teacher associations and recreational sports leagues may not have enough in assets to justify the cost of a lawsuit. But individual members of a board of directors might. It all

depends on the issue being litigated and the legal team involved.

Reach out to your insurance professional and lawyer to review your organization's various insurance policies, along with your own policies and exposures.

- Be clear on the insurance policies in play, and their exclusions and limits.
- Review the organization's activities, service base and risk factors (such as youth groups, elder care, developmentally disadvantaged). Depending on the organization, you could be held to a higher standard, regardless of organizational assets.

Public organizations and for-profit corporations — the risk grows

The risks can be high if you serve on a school board, municipal council, public health board or some other tax-supported public body. The risks also increase within for-profit corporations that answer to shareholders.

For example, shareholders could launch a lawsuit against the corporation if assets are sold off or a product line is terminated, and shareholders feel that decision unnecessarily devalued the stock value. Recent IPOs are also at risk for lawsuits and the trend is on the rise.

Nonprofits are at risk — the larger the service net, the greater the risk

The larger the organization you serve, the greater the financial risk — and the more protection you need. That maxim applies to all organizations, however benevolent their mission may be. If you join the board of a nonprofit cultural institution with a priceless art collection, you can expect scrutiny.

Additionally, if you sit on a board that oversees homeless issues in a large urban area, then your risk may increase due to multiple locations or inexperienced volunteer staff.

Even contracted help for a temporary job can be a liability. For example, if a drywall contractor hired to repair walls assaults a volunteer at the shelter, the organization can be held liable. The organization is expected to have a process for background checks and vetting vendors.

Public perception is a risk

Liability isn't always connected to financial loss. The loss of public reputation due to negative media exposure can be a loss — and an even harder one to recover from.

D&O liability — who insures the board?

Apart from their general liability, directors and officers also have potential liability from the organization they serve, as well as its shareholders, beneficiaries and other stakeholders. That's where D&O liability insurance comes in.

Here are a few things to ask your organization about D&O insurance for its board members:

- **Am I covered directly for any legal costs or damages I incur?** This is called side A coverage. It presumes that you would manage your own defense and could potentially offer more control over settlements.

- **Will the organization defend me and pay damages for me?** This is called side B coverage. Your defense is managed by the company or organization, but you have little to no control over the settlement of claims. It generally reimburses the company for expenses incurred defending its executives, directors and officers.
- **Does the organization have its own coverage?** This is called side C coverage. It responds to lawsuits against the company or organization, which can include its employees, board members and other staff. But this shared coverage could leave you personally exposed if the limits are too low. The coverage amount might be depleted by other board members or the organization's own defense before your defense is complete.

Your insurance professional and lawyer can advise you on purchasing your own D&O coverage.

Coordinated risk management — personal liability gaps

What protection do you need? The biggest hurdle is covering the gaps between your personal liability and the organization's liability. You can start by finding out what coverage your organization currently has in place.

Commercial general liability

Confirm whether executives and board members are insured under the organization's commercial general liability (CGL) insurance policy. A CGL policy covers your organization's liability for bodily injury or property damage to an unrelated third party, and directors and officers are typically covered. But the coverage is usually limited and may not be enough to support a lawsuit or catastrophic loss.

Talk to your insurance professional about how much coverage your organization's CGL would offer you. Get a copy of the policy so you can understand the coverage.

Hired and nonowned auto liability — coverage for personal vehicles

How many times have you run an errand for your organization or company? Hired and nonowned auto liability insurance covers these situations. CGL policies do not cover auto accidents.

Fleet coverage and traditional owned auto policies cover the vehicles owned by the company or organization. But many organizations don't own the vehicles used by their employees, volunteers and board members. There is a chance your organization would not be covered if it is held liable for injuries caused by someone driving their own car to run errands on its behalf.

The driver's personal auto insurance will respond first, but you and the organization may be exposed if there are catastrophic injuries and the coverage limits run out.

D&O liability

Sides A, B and C are stackable lines of coverage, meaning one coverage side should respond when the other does not. If your organization has side C coverage, you can seek out additional sides to stack on your own.

Think in terms of long-haul and worst-case scenarios when insuring yourself. If you depend solely on an organization-provided policy and that policy has slim limits, there may not be enough money left to mount a legal defense for

every board member once those limits are exhausted. You could be left with a big legal fee.

Either way, you might want to talk to your insurance agent about getting your own personal D&O policy as a secondary line. Your personal D&O coverage should respond once all limits are exhausted on the primary (the organization's) D&O policy.

Cyber liability

Cyber attacks are a growing risk, with no signs of slowing down. It's no longer sufficient to assume only big companies or banks are at risk.

The care of personally identifiable information (PII) is a liability that goes beyond storage of credit card or banking information. All data is of interest hackers, who can make big money off buying, selling and trading all types of PII on the dark web, including client, volunteer, benefactor, employee and business contact information.

It's all worth something to someone and you'd be surprised how little is needed to recreate entire identities. Your agency needs a plan and may even be legally required to have one, depending on the state you're in.

Many management liabilities — review your policy exclusions

Not long ago, it was enough for directors and officers to be covered under a CGL or a D&O policy. But laws and the insurance industry are changing. There are many other types of management liability insurance coverages you should consider.

- **Cyber liability** for data breaches due to the loss, exposure, theft and/or corruption of electronic info
- **Employment practices liability (EPL)**, which includes volunteers and employees, claims of discrimination, harassment, violence and abuse in the workplace
- **Environmental liability** for contamination of air, water or land caused by your organization
- **Product liability** for manufacturing defects that cause catastrophic injury
- **Sexual abuse or molestation** for incidents that occur at your organization or company
- **Crime or fidelity** for incidents involving theft by employees
- **Media liability** for publishing, marketing or trusted information sources for libel or slander

In the past, a D&O policy would typically cover claims alleging cyber, employment practices, abuse, environmental liability or (less often) product liability. But recently the trend is to exclude or restrict coverage with the expectation that the organization will purchase separate policies addressing those exposures.

Virtually every organization today has some level of exposure. It's likely board members do, too.

Due diligence and a risk management protection plan

With this potential for risk, what should you do when you get an invitation to serve as a director or officer?

- Schedule an appointment with your insurance professional and tell them about your plans to join the board.
- Gather as much information as you can from the organization's financial statements and claims history. Their willingness (or unwillingness) to provide them says a lot.
- Ask questions about their current insurance coverage such as commercial general liability, D&O liability, hired and nonowned auto, environmental liability, cyber liability, crime and fidelity, abuse and molestation liability and EPL.
- Ask to review their policies with your insurance professional so you can make an informed insurance strategy for your own personal liability.
- Ask if the organization has assessed its cyber, employment and environmental exposures.
- Review any written risk management plans for addressing exposure areas.
- Review your insurance options with your insurance professional annually as laws and exclusions change.

Coordinate with your insurance professional

It's an honor to be considered for a board membership. Transparency with information is part of that process and it's essential to your personal risk management exposure planning. If you're satisfied with the responses you get, you can feel confident about assuming a leadership position within a responsibly run organization. Talk to your insurance professional to help guide you on this exciting path of opportunity.

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