



WHY DO BUSINESSES NEED DIRECTORS AND OFFICERS LIABILITY?

Stories of wrongdoing and bad judgment by corporate managers have become familiar headlines. AIG's troubles almost brought down the world economy. General Motors was in such bad shape that the federal government took it over in order to save it. The collapse of Lehman Brothers in September 2008 ushered in the Great Recession. These stories became big news because they were exceptional; most companies do not fail in such a spectacular fashion. However, corporate managers are human and can make mistakes, and some mistakes can cause significant losses for the company, its shareholders, employees and vendors. When this happens, the right insurance coverage can make the difference between survival or corporate and personal bankruptcy.

Most businesses carry commercial general liability insurance that covers legal liability for bodily injury, property damage, and personal and advertising injury suffered by others. However, this insurance probably will not cover claims against corporate officers for their errors in running the company. These claims usually center around losses such as falling stock prices or loss of capital. While real, these losses do not involve physical injury to or loss of use of tangible property. In these claims, people lose money but their property is intact. CGL insurance will not apply in these cases.

Directors and officers liability insurance covers a business's legal liability for "wrongful acts" of its directors and officers acting within their capacity for the business. A typical policy defines "wrongful act" as errors; misstatements; misleading statements; acts; omissions; neglect; or breaches of duty. To be covered, these acts must be actually or allegedly committed or attempted by an individual in her capacity as a director or officer of the insured business.

Directors and officers face lawsuits from many sources, including the entity they work for, shareholders, employees, government entities, competitors, vendors, and consumer groups or groups that represent segments of the population. Leaders of all types of organizations are vulnerable, though the source of a legal claim will vary by the type of entity. Most claims against public companies come from shareholders, while employees file most of the claims against non-profit organizations and half the claims against private companies. Customers and competitors are also frequent sources of suits against private companies.

D&O insurance covers many types of claims, including:

- A lawsuit by one shareholder against the majority owners, claiming that the company lost money because the majority paid themselves too much.
- Shareholders allege that management breached its fiduciary duty to them while executing a merger with another company
- A key employee leaves one company and joins a competitor as a director. His former employer sues him and the competitor, claiming that he violated his contract and used confidential company information with his new employer.
- Shareholders file suit, claiming that the company misrepresented the quality of a potential new product when it sought funding for its production.

- A shareholder sues the president of a company for failing to promptly notify shareholders of a major pending transaction.
- Shareholders who think the company should have sued a deadbeat partner file their own suit.
- Members of a private company's board of directors are sued for allegedly using their positions for personal gain.
- The government sues a company for alleged anti-trust activities.

Even if courts dismiss these lawsuits, the legal defense costs can be significant; D&O insurance covers these costs. All organizations and their leadership should work with professional insurance agents to identify companies that can provide the coverage they need at a reasonable cost. Businesses face many different risks today. Overlooking D&O insurance to address those risks may be a costly mistake.