

Why Private, For-profit Companies Should Purchase Directors, Officers & Company Liability Insurance

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It is a fact of doing business in the United States: Lawsuits happen. Regardless of whether the action has any merit, lawsuits are expensive to deal with, damaging to reputations and draining to a business and its executive team. Small to mid-sized private companies can specifically attest—litigation is never an inconsequential matter. Any business, regardless of the industry sector they are in, can become embroiled in a dispute.

Directors, Officers & Company (“D&O”) Liability Insurance, for privately-held companies can be a lifesaver if an unexpected lawsuit or dispute arises. When a business and its management team are placed in an adversary’s cross-hairs over an alleged business dispute, a D&O policy will respond right off the bat. This response includes providing legal defense by skilled legal counsel who will guide and advocate for the D&Os through the process. In addition, when coverage applies, the D&O policy would fund the settlement of a lawsuit, or pay a judgment if the case were to go to trial.

Originally, D&O coverage was designed to protect only the individual directors and officers from lawsuits brought by outside shareholders who are not involved in the management of the company. However, D&O products have evolved and expanded considerably over the past 20 years. A contemporary private company D&O policy can provide coverage for the entity, as well as the individual D&Os, against a wide range of allegations and claims, from not only shareholders, but also clients, competitors, vendors, creditors, and regulators.

Shareholders, Investors, Partners and Members:

- Merger / Acquisitions
- Financial performance
- Executive compensation
- Stock or other offerings
- Conflict of interest
- Bankruptcy
- Inadequate / Inaccurate disclosure
- Financial reporting

Customers, clients and consumer groups:

- Extension, refusal of credit
- Debt collection
- Deceptive trade practices
- Contract dispute
- Restraint of trade
- Dishonesty
- Cost, quality of product or service
- Lender liability

Other third party claims against Directors and Officers (including competitors):

- Anti-trust
- IP Infringement
- Business interference
- Competitor disputes
- Prospective company acquisition
- Company defamation
- Tax issues
- Regulatory / other government issues

A disturbing fact for members serving on the company's Board of Directors is that D&Os can, and usually do, get personally named in a lawsuit asserted against the company. As defendants to a suit, the claim seeks personal liability against the D&Os to fund a judgment. The more closely held a company is, the fewer owners/D&Os there are to sue. Therefore, the exposure to the personal assets of those principals is even more pronounced. D&Os know that, in most states, a corporation is required to indemnify its D&Os for personal liability, if such liability arose from the execution of their corporate duties. If the corporation is on financially sound footing, the D&Os personal assets, such as their home, cars, furniture, kids' college tuition and savings accounts, will usually be protected via the Company. However, situations often arise where the Company cannot or will not defend a D or O, compelling them to defend themselves. Such cases can be when the Company is not on solid financial footing, when they become insolvent, or are prevented by law. As troubling as it may sound, in tough financial times, or under unique statutory restrictions, the D&Os could unfortunately find themselves paying for their own defense and/or settlement of a lawsuit out of their own pockets.

When a lawsuit hits, the financial advantages of having D&O coverage is readily apparent. What isn't evident from reviewing policies is something we've witnessed over the course of watching many D&O claims unfold. When serious accusations of wrongdoing are leveled at a member(s) of management and there's no D&O coverage to fall back on to fund the claim, the financial burden of a dispute can tear a management team apart. For example, suppose you are the officer who is the target of certain allegations. How quickly do you think your colleagues will rally around you when your alleged error or omission is the cause of significant financial hardship to the company? Without D&O insurance in place to shoulder the financial and legal burden of a claim, infighting can erupt rather quickly when the Company's financial resources are placed in peril. When accusations fly, and salaries and bonuses might be affected, such situations often change the way people behave toward one another. As opposed to circling the wagons, executives may play the blame game. In contrast, if D&O insurance is in place, there may not be such a panic, and finger pointing may not be as fierce or important. Accordingly, it is believed that one of the great hidden benefits of D&O insurance is that it tends to diffuse internal turmoil, and helps maintain management cohesiveness during what is surely a trying time. When D&O insurance is in place and coverage has been accepted, the management team will be able to easily maintain a "stick together" attitude and an "us against them" mentality.

To summarize, we believe D&O insurance is imperative to carry for private companies and their principals, regardless of industry. D&O coverage acts as a solid backstop to mitigate and/or solve what could be the devastating financial impact of unforeseen business litigation. Litigation can happen at any time from within or from outside any organization. In a society as litigious as ours, not having D&O insurance creates a serious exposure to the business itself, as well as every member of a company's management team personally. Make sure your private company customers, no matter what size or industry, carefully consider the purchase of D&O insurance to ensure the company, as well as their personal assets, are protected.

About Socius Insurance Services, Inc.

Founded in 1997, Socius Insurance Services, Inc. is a property/casualty and management liability wholesale broker based in San Francisco, with regional offices in Los Angeles, CA; Elgin, IL; Birmingham, AL; New York, NY; Philadelphia, PA, and Tampa and Miami, FL. Socius specializes in D&O, E&O, EPL, property & casualty and umbrella coverages.



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