

Business Insurance

Private companies urged to buy D&O

By COLLEEN McCARTHY
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NEW YORK—Directors and officers of private companies rarely have D&O insurance but should consider the cost-effective coverage to minimize their risks, a lawyer says.

Directors and officers of private companies can face lawsuits by employees, vendors, customers, shareholders, investor groups and federal regulators. Other claims can arise as a result of mergers and acquisitions, bankruptcy or disputes between family members who share ownership of a company, Spiro Bantis, a partner at London Fischer L.L.P. in New York, said at the Fourth Annual Directors and Officers Insurance ExecuSummit in New York May 6-7.

It's a common misconception that private directors and officers do not need this level of protection, but directors and officers of private companies still are subject to liability for their decisions and actions, Mr. Bantis said.

Oftentimes, "shareholders in closely held private companies, who are not involved in the daily management of the company, assert claims that the directors and officers breached their duties to the shareholders by mismanaging the company's affairs, or by self-dealing to the detriment of the company, or by treating the minority shareholders unfairly in a buy-out or merger situation," he said.

Private company D&O insurance would cover claims that arise from alleged wrongdoing by directors and officers in their corporate capacities. Unlike its public company counterpart, coverage in a private company D&O policy is much broader and is generally considered all-risk because the protection extends to the employees and the organization itself, Mr. Bantis said.

Private company D&O policies generally cover claims other than bodily injury, defamation and property damage, he said.

Currently, one of the biggest factors influencing a company's decision to purchase a private D&O policy is the policy's employment practices liability component. However, less than half of all claims made against such policies relate to employment practices, Mr. Bantis said in citing an Advisen Ltd. study. After excluding employment liability claims, the remaining sources of claims that trigger private company D&O policies are customers with 43%, government/regulators at 29%, vendors at 17%, and shareholders with 11%, according to the survey.

"To rely on EPL coverage alone is short-sighted," Mr. Bantis said.

While D&O insurance for private companies is optional, companies should consider purchasing coverage to protect themselves, he said.

Many private D&O liability policies are written on a duty-to-defend basis, a term that generally is not available to public companies in D&O policies, he said. This feature can be valuable to a private organization because it would provide 100% reimbursement for defense costs where at least one allegation of a lawsuit, regardless of its merit, is potentially covered by the policy.

A private D&O policy can also cover subprime-related claims, "to the extent the company is in any way involved in the mortgage business, or to the extent it invested its assets in mortgage-related investments," he said.

Directors and officers of private companies are particularly vulnerable because "so often their personal wealth is tied to the company balance sheet and assets," Mr. Bantis said. "Any defense or settlement money related to a claim will likely come out of the company coffers."

While the purchase of private company D&O coverage is increasing, the market is still relatively small. It is estimated that only a minority of private companies, roughly 50,000 to 70,000, buy such coverage, with a total premium of about \$2 billion, he said.

While organizations should work with their broker to fully assess their risks, private company D&O insurance can be an effective risk management tool.

"It's basically sleeper insurance. When you weigh the cost of the premium against the exposure, it's not very expensive," Mr. Bantis said.