5 Cornerstones of Well-Rounded Professional Liability Coverage

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The economy is beginning to show signs of life; but, for many in the community banking industry, the light at the end of the tunnel remains a mere flicker. The Federal Deposit Insurance Corporation (FDIC) has indicated that it will continue its aggressive efforts in 2011 to initiate litigation against the directors and officers of the more than 330 financial institutions that have failed since the financial crisis began in 2008. Shareholder claims are also on the rise, adding to the plethora of risks that have led to a difficult environment for independent, locally-owned and -operated institutions to provide the financial lifeblood for many communities across the country.

According to the Independent Community Bankers of America, community banks comprise 97 percent of all banks in the United States and hold more than half of all small business outstanding loans. These institutions represent a vital force in our society, but many may not be aware of the potential exposures they face in today's marketplace. Unlike the corporate banking world, community banks typically do not have the luxury of in-house counsel and risk management departments. Rather, they rely on their agents and brokers to provide guidance on insurance coverage that will assist them in limiting their liability

General liability policies often do not cover certain exposures that could lead to devastating judgments and financial ruin. And while no one policy provides a one-size-fits-all solution, brokers should be aware of the following five cornerstones of well-rounded coverage for community banks:

1. Directors & Officers (D&O) Liability. D&O liability policies provide coverage for individuals against lawsuits arising from their roles as directors or officers for alleged acts of improper establishment of corporate policy. In addition, they often provide coverage for directors and officers with respect to employment policy or actions taken with regard to specified employees, shareholder disputes as well as failure to comply with Securities and Exchange Commission rules and other federal regulations that apply to corporations. A D&O policy is essential for community banks where local citizens often serve on the board of directors. A policy that fails to offer broad coverage will handicap a bank in attracting and retaining leadership, who will be wary of exposing themselves to personal liability. In the absence of D&O liability coverage, community banks also may incur damages and litigation expenses which can run into the millions.

Only a handful of lawsuits have been brought forth to date. However, according to the FDIC, the agency has given the green light to future legal action against more than 130 directors and officers of failed banks that it has taken over. The FDIC is also enhancing its employee count and financial resources to target fraudsters. With a Congressional Oversight Panel finding that community banks will become even more vulnerable in the coming years as "underwater" commercial real estate loans come due, the need for a thorough review of D&O coverage becomes even more imperative.

2. Bankers' Professional Liability (BPL). Community banks also may face allegations of negligently representing the quality of its investments or offering poor financial advice especially during periods of economic slowdowns. These claims often can be prolonged, costly and time-consuming to defend. A BPL liability policy can provide coverage against claims arising from allegations of wrongful acts, errors or omissions in the performance of professional services by the community bank and its employees. This coverage can often be expanded to include lender liability, trust services or vicarious liability for services that a community bank may provide through a third party.

3. Employment Practices Liability (EPL). We live in an increasingly litigious society, and in bad economic cycles, losses increase as individuals seek new ways to be recompensed for perceived harm. Liability for employment practices is a growing concern among community banks, which are seeing an increase in harassment, hostile work environment and other employment-related claims. These lawsuits, often viewed as nuisance litigation, can disrupt the day-to-day business life of a community bank. EPL coverage can ease the burdens associated with these issues by providing coverage to entities, directors, officers and employees for wrongful employment practices and ensure that costs for legal and administrative proceedings are covered.

4. Fiduciary Liability. Community banks should also protect themselves from financial liability due to the administration of pension and welfare plans. Fiduciary liability coverage can offer banks protection against the unique exposures when managing and administering these plans, including Employee Retirement Income Security Act violations or losses incurred as a result of alleged errors, omissions or breach of fiduciary duties.

5. Information Risk and Network Security Liability. It's among every bank's worst nightmare; an employee's laptop is stolen out of his car, potentially compromising sensitive personal and financial information of thousands of its customers. Not only can such a scenario threaten an institution's reputation in the community, it can also be extremely costly. Notifying customers and complying with federal and state privacy laws in the event of a data breach are both time consuming and expensive.
As more community banks move forward into the 21st century and develop services to appeal to today's tech-savvy consumers, there is a greater need to address information risk and network security liability. Brokers should encourage their community bank

customers to consider coverage that will address breach of data by outsiders and employees, the theft or loss of removable media such as laptops and PDAs, and injury resulting from the unauthorized use or disclosure of private information in the bank's custody.

Working with your community banking customers to review or round out their coverage will provide a sound insurance program during these challenging times and allow these institutions to focus on what matters most – driving small business growth and keeping local communities vibrant for years to come.

4 Things to Keep in Mind When Evaluating Coverage

When evaluating coverage for your community banking clients, it is important to keep the following in mind:

1. **Know who is covered.** Make sure all directors and officers – appointed or elected – are covered under the community bank's D&O policy. In addition, all employees should be covered under an EPL policy. Banks also must consider whether or not independent contractors or temporary workers should be included in the coverage.

2. **Understand how policies are triggered.** Unlike general liability coverage, professional liability policies are "claims-made," meaning that they are triggered when a lawsuit or written demand for monetary relief is filed, as opposed to when an act occurred. Brokers must be aware of this critical distinction and be able to explain it to their community banking customers.

3. **Be familiar with an insurer's claim reputation.** An insurer's ability to effectively and efficiently handle claims is critical. Does the company have community banking experience, and is it willing to meet directly with the insureds prior to a claim, renewal or inception of a policy? Will the company work closely with underwriters to ensure that both parties understand the interpretation of the policy language? Consistent and seamless 24/7 support can go a long way in ensuring the best possible outcome for your customers.

4. **Conduct a thorough review in conjunction with other policies.** Professional liability policies for community banks have become increasingly complex in recent years. It is important for brokers to not only educate themselves about these coverages, but also conduct a thorough review of these policies in conjunction with a bank's other coverages – property/casualty, general liability, etc. – to identify any gaps that may leave the door open to potential risks.

About The Author

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