



Insurance & Risk Management 101 for Nonprofits

A nonprofit organization purchases various types of insurance policies to cover the organization, its employees, and/or directors of the organization. Insurance premiums can be a significant expense for a nonprofit. The insurance claim process, if needed, can be difficult.

This alert will explain the basics of the insurance policies that are most commonly purchased by nonprofits – what they cover, when they are required, and what to do if there is a claim.¹

The Role of the Insurance Broker

The first step in understanding your insurance coverage is to find a good insurance broker. The broker acts as your agent and negotiates with the insurance company to ensure that the nonprofit organization has a policy that will protect it as necessary and that the nonprofit pays a fair price for the policy. A good insurance broker will explain policies to a nonprofit client, will seek to tailor policies to fit that particular client's needs, and will assist in any claim process. There is no substitute, however, to understanding your own insurance policies, making sure they

have the right coverages for your organization, and being your own advocate when needed.

Insurance Limits

A decision common to all policies is the limit needed by your nonprofit: \$500,000? \$1,000,000? More? It obviously depends on your size and exposures. A good broker will advise you on the limits you need.

There are three kinds of limits. First, there are limits per “occurrence,” meaning the amount the insurer will pay for any one distinct claim within the policy period. Second, there are “aggregate” limits, meaning the most the insurer will pay during the entire policy period, no matter the number of claims. Third, sometimes there are “sub-limits,” meaning the insurer will pay only up to that lower amount if the loss is for something specifically defined as having a sub-limit. (For example, a property policy will typically have a lower limit for any loss to “landscaping.”)

A nonprofit might enter into an agreement with the government, a landlord, a lender, or another entity that requires certain insurance and limits. For example, a landlord may require that your organization has a general liability policy with a \$1 million limit. Close

¹ This alert does not address employer – purchased insurance coverage for employees, such as health and long-term disability insurance.

attention should be paid to matching these insurance-related requirements with the type and amount of insurance actually purchased.

The Basic Parts of Any Policy

Insurers use standard forms issued by the Insurance Services Office, or ISO, or if they have their own forms, they are similar to the ISO form.

Most insurance policies can be organized in three parts. First, there is the policy “declarations,” or “deck” pages. This is the page or pages that show:

- the insurance company,
- the policyholder (in this case, the nonprofit),
- the policy number,
- the policy period (typically the twelve-month period which matches the nonprofit’s fiscal year),
- the premium that must be paid for the coverage, and
- The maximum dollar amount of coverage provided by the policy. This is where you will see any occurrence limits, aggregate limits or sub-limits.

The declarations page also usually references the insurance forms and endorsements by number. Those references are a guide to the exact policy forms and endorsements that set forth the policy terms and conditions.

Second, there is the main policy, which sets forth what is covered by the policy, any exclusions from coverage, any conditions that must be met for the policy to apply, the limits of the coverage, and definitions.

Third, there are usually various endorsements that amend and supersede the main policy form as well as any prior endorsements. These are usually added to the basic policy so that it is customized to meet the nonprofit’s specific needs and the state law requirements of the nonprofit’s state of operations. One should read the endorsements to get the full picture of coverage.

With that overview, there are up to five basic kinds of policies that many nonprofits purchase. Some insurers offer a “package” policy for nonprofits, which combines two or more of these policies.

Property Coverage

If a nonprofit owns its own building, or has business property (such as computers, furniture, etc.), then it should protect that property from loss or theft. This insurance for nonprofits is similar to homeowners’ or renters’ insurance for individuals. This kind of insurance is sometimes called “first-party” insurance because it is triggered by an event like a fire, flood, or theft (*i.e.*, there is no “third-party” lawsuit involved).

An “all risk” property policy protects all of your property in the event of loss from most kinds of “peril,” including fire, hurricane, tornado, and theft.

There are exclusions found in most policies. You should read each exclusion and think about whether it matters to your nonprofit. Many of the standard exclusions may be irrelevant to your nonprofit, such as one for boats. But for others, you may need to patch up the exclusion by way of an endorsement.

Common exclusions are for loss caused by mold, flood, terrorism, and earthquake. These coverages can all be restored by endorsement or special policies, although adding back some of these exclusions can be very expensive. For example, to add mold coverage back to your policy may be cost-prohibitive. Terrorism coverage is commonly restored by special endorsement.

Property policies also cover loss by theft. Many property policies for nonprofits also add coverage for any loss incurred by the nonprofit because of employee dishonesty, such as by embezzlement.

Usually automobiles are excluded. If your nonprofit owns automobiles, auto insurance can be added by endorsement, or otherwise a special auto policy is needed (covering both property and liability, as reviewed below).

Workers Compensation

Workers compensation insurance is required for any nonprofit that has employees. In D.C., one employee triggers the requirement. Premiums are calculated by payroll and the type of work done. For example, premiums are generally higher for an employee engaged in manual labor than for an office worker, because the risk of injury is greater. Such insurance is not only required, but highly recommended. In the event of an injury to an employee while in the course of employment, workers comp will cover all medical costs. Moreover, the employee cannot sue the nonprofit for negligence in causing the injury. The terms of the coverage are spelled out by state law.

General Liability Insurance

General liability insurance is basically “lawsuit insurance.” There is coverage for any damages that your nonprofit is obligated to pay as a result of “bodily injury” or “property damage” to a third person. This includes both paying a lawyer to defend the suit as well as anything paid to settle the case. For example, if a guest to your business falls and is injured, then sues you, alleging the injury was caused by your negligence in failing to maintain safe premises, you are covered. The insurer will hire an attorney to defend your organization and also pay any settlement or court judgment.

General liability insurance also covers lawsuits brought as a result of “personal injury” that does not result in bodily injury, such as invasion of privacy or “advertising injury,” such as libel. Some policies also include coverage for suits alleging employment discrimination, harassment, and similar claims. If such coverage is excluded, it can be added by endorsement or through directors and officers coverage or a special employer’s liability policy.

There are standard exclusions in liability policies. Some of them are designed to prevent overlapping coverage provided by other policies. For example, general liability insurance does not cover damage to your own property, since that claim would be covered by your property insurance.

Other exclusions require a special endorsement to fix. For example, your general liability policy may exclude coverage for a liability caused by an automobile, since that would normally

be covered by an automobile policy. However, if your nonprofit does not own an auto, you may want to add an endorsement to the liability policy to add this coverage. Such an endorsement would cover any potential liability to your nonprofit if one of your employees or volunteers uses his or her auto in the course of performing work for the nonprofit. The endorsement covers liability caused by “non-owned and hired autos.” The coverage will protect your organization from liability if the employee or volunteer has an accident while on the job, and the nonprofit is sued by the other driver in the accident.

Premiums are generally much lower for nonprofits relative to other businesses. That is because in D.C. and most states, there is special statute that limits the ability of persons to sue a nonprofit, or any of its employees or volunteers, for mere negligence. In order to invoke the protections of the statute, however, it is required that the nonprofit maintain liability insurance at least equal to the statutory limits. In D.C. the nonprofit must maintain liability insurance at least equal to \$500,000.

In the nonprofit world, the general liability policy usually insures not only the nonprofit organization, but also as a “named insured,” all directors, officers, employees, and volunteers.

Directors & Officers Insurance

Almost all nonprofits have a board of directors and various officers. At the same time, the general liability policy is limited to liability arising from only certain occurrences – bodily injury, property damage, personal injury, or advertising injury. Therefore, for many

nonprofits, a directors and officers liability policy is a must.

A D&O policy more broadly covers liability arising from any kind of an alleged “wrongful act.” Most importantly, this insulates your directors and officers from personal liability relating to participation on your board or running the nonprofit.

The wrongful acts covered by a D & O policy include claims that the officer or director breached his or her fiduciary duty when carrying out his or her responsibilities. It also covers any claim that the officer or director discriminated against someone applying for benefits from the nonprofit. For example, if an individual applies for housing from the nonprofit and is denied, the individual may claim that the nonprofit engaged in illegal discrimination when denying the benefits. The D & O policy is designed to cover such claims.

In addition, nonprofit D & O policies may also cover employment discrimination claims. You should check with your broker to see if your D & O policy covers such claims or if you need additional insurance to protect your organization.

In the nonprofit world, the D&O policy should insure not only the directors and officers, but also the employees, volunteers and the nonprofit organization itself.

The combination of the general liability and D&O policy provide the broadest possible range of “lawsuit” protection for nonprofits and their directors, employees and volunteers.

Errors & Omissions Insurance

Some nonprofits may need to purchase errors and omissions insurance, a special type of liability insurance. General liability and D&O policies typically do not cover claims arising from a breach of duty in the delivery of “professional services.” Doctors and lawyers call this “malpractice” insurance. E&O insurance is commonly purchased by architects, engineers, licensed social worker and certain others who deliver specialized professional services. Also, some contracts require the organization to carry E&O insurance.

Risk Management Generally

The purchase and management of insurance falls into the broader field of “risk management.” Larger nonprofits sometimes employ full time risk managers. For smaller nonprofits, the risk management and insurance functions usually falls into the hands of the CFO or executive director.

Risk management has three parts to it. First, a nonprofit should start with an internal risk assessment. What is every kind of loss that you could experience (and why), both to your own property and also from any lawsuits? Do you have guests and invitees to your premises? Do you drive others? Do you work with children? Do you have volunteers? Is your premises safe? There is potential liability as a result of each and every interaction you have with any person or company.

At least annually, the executive director and others should engage in a process of considering and identifying potential

risks that could cause a loss to the organization.

The second step is risk mitigation. This involves taking measures to eliminate or reduce the risk of any mishaps or events that could lead to loss. Do you have an emergency evacuation plan? Do you have fire extinguishers? Do you have a process for reporting any workplace or other injuries? Good risk mitigation involves making a written record that you have engaged in such risk mitigation measures. Your employee manual is itself a form of risk mitigation because it sets forth your rules and expectations for employees – for example, that workplace harassment will not be tolerated and may result in termination.

The third and final part of risk management is insurance. There is no such thing as a risk-free operation. Insurance is the last line of protection. It reaches those losses that could not be avoided despite having engaged in responsible risk assessment and risk mitigation. If one goes through the first two steps of the broader risk management process, one will better understand the final step of insurance – what and why certain coverages are needed. Some nonprofits hire outside risk managers to supply this service.

Insurance Certificates and Additional Insureds

Governments and those with whom you do business may require a certificate of insurance. This is to prove that you have certain insurance policies in place, with coverage and limits sufficient to meet their requirements. You should have copies on hand of this standard-form insurance certificate to supply to those

who require it. You can ask your broker to supply them.

From time to time, those with whom you contract or do business may require you to add them to your general liability policy (or other policy) as an “additional insured.” Usually, this is for a limited time. For example, you might sign an agreement with a university to provide housing and educational classes to children in your program during the college’s spring break week. The agreement may require you to name the university as an additional insured on your general liability program for the week the program is taking place. Typically, this can be done at no extra cost. You will need assistance from your broker or insurer.

As a general matter, it is better not to add any other entities to your liability policy if you don’t have to do so because it increases the likelihood that a claim will be filed against your policy. But as a practical matter, because of the demands of the other party, you may not have a choice, and the business need will justify your doing so.

At the same time, it is important to ask for certificates of insurance from people you hire to do work for you. For example, if you hire a contractor to make some alterations to your work space, make sure you get a certificate of insurance showing that the contractor has workers comp and general liability insurance. This will protect your organization in case someone is injured as a result of the contractor’s negligence. In addition, if the contractor does not have workers comp insurance, you may end up having to add his or her

employees to your policy for the period that they were working on your project.

Indemnifications

From time to time, you may be asked to indemnify another organization or person. Whenever you indemnify someone else, you are, in effect, becoming their insurer because you are promising to reimburse them for any loss they suffer under the circumstances described in the indemnification.

If possible, it is best to avoid signing an agreement requiring you to indemnify or “hold harmless” another company. At times, however, this may be required as a condition for doing business with another company.

For example, if you are holding an event at a theater, their “standard” agreement may contain an indemnification clause which provides that you will indemnify the theater for any loss they may suffer as a result of your use of the theater. You may have to agree to this if you want to rent the theater.

If your business need outweighs the downside of signing such an indemnity, perhaps the language can be negotiated to level the playing field. Is the indemnification mutual? That is, if you indemnify them for liability caused by your negligence, they should indemnify you for liability caused by *their* negligence. The worst indemnity clauses are the ones that attempt to impose an indemnity obligation on you not only for liability caused by your negligence, but also liability stemming from their own negligence or the negligence of others beyond your

May 2010

control. Avoiding unfair indemnity clauses is important risk mitigation.

Conclusion

Depending on your nonprofit, there may be specialized insurance policies or endorsements to consider. You should consult legal counsel or a good broker who specializes in nonprofits.

You should also meet with your broker regularly and keep them informed of any significant changes in your operations. This will allow them to ensure that you have the proper insurance policies in place.

Finally, if anything happens that could give rise to a claim, such as an accident on your premises or your organization is threatened with a law suit, you should contact your broker immediately. It is

important to give your insurance carrier timely notice of any potential claim or the carrier may refuse to pay your claim promptly.

Additional Resources

For more information about risk management and insurance, contact:

Nonprofit Risk Management Center:
<http://www.nonprofitrisk.org/>

Nonprofit Risk Management Toolkit:
<http://www.lexisnexis.com/risk/nonprofit/toolkit/index.html>

The Institute of Risk Management:
<http://www.theirm.org/>

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