



UNDERSTANDING DIRECTORS AND OFFICERS LIABILITY INSURANCE FOR NONPROFIT ORGANIZATIONS

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COVERAGE OVERVIEW AND POLICY ROADMAP

Nonprofit organizations and their management teams can face significant liability arising from financing their entities, making investment and allocation decisions, maintaining a workforce, complying with regulatory requirements, and countless other issues, making investment and allocation decisions, maintaining a workforce, complying with regulatory requirements, and countless other issues.

Particularly at a time of heightened federal government scrutiny of the nonprofit sector, it can be critical for entities and their directors and officers to understand the risk mitigation

D&O INSURANCE – WHAT IS IT?

- Directors and Officers (“D&O”) liability insurance protects organizations’ directors and officers against claims alleging they committed wrongful acts in their capacities as directors and officers.
 - Typically this will provide that the policy covers **Loss** arising from a **Claim** made during the **Policy Period** against an **Insured** for a **Wrongful Act**.
- Coverage helps address defense costs, judgments and other liabilities arising from litigation by donors, beneficiaries, vendors, employees, regulators and others.
- Protects D&Os’ personal assets and promotes organizations’ missions by helping to attract directors to serve.
- In the event of a Claim, Insurers appoint defense counsel and pay their fees, or reimburse the Insured for its incurred defense costs.

POLICY ROADMAP: HOW TO READ A POLICY

First – Declarations Page (Summary of Coverage Terms)

- Named Insured: The covered organization(s).
- Policy Period: The dates during which Claims may be submitted under the policy (usually one year).
- Limit of Liability: The maximum amount the insurer will pay if coverage applies.

Second – Insuring Agreement(s)

- In general, D&O coverage falls into three categories:
 - Side A: Coverage for D&Os for claims brought against them for which the organization does not provide indemnity

Example: If an organization is financially unable to indemnify its D&Os

Example: If an organization is prohibited by law from using its assets to make indemnity payments

Example: If an organization wrongfully refuses to provide indemnity that is owed to D&Os (in which case the insurer will provide coverage as a Side A claim and then seek recovery from the organization)

- Side B: Reimbursement to the organization for amounts spent to indemnify D&Os
- Side C: Coverage for the organization for claims brought against the organization itself

Example: Criminal prosecution alleging that an organization participated in wrongfully harboring migrants.

Example: A “whistleblower” claim under the False Claims Act alleging that the organization wrongfully recovered funds under a state or federal government program (absent restrictive policy phrasing to the contrary).

Third – Definitions

- To determine whether an Insuring Agreement is triggered, refer to the policy’s Definitions section.
- While general coverage principles are similar throughout the industry, each insurer defines key terms in a unique way, with potentially significant coverage differences.
 - Insured: The entity named as the Named Insured, its subsidiaries, and their D&Os and employees.

- **Claim:** A third party must initiate an action (including a lawsuit, complaint, or regulatory proceeding) or otherwise make a demand for relief against an Insured.
- **Wrongful Act:** The Claim must allege that an Insured actually committed some wrongdoing in the scope of his/her role as a D&O.
- **Loss:** An Insured must actually incur losses as a result of a Claim. This includes defense costs/attorneys' fees and other liabilities such as judgments and settlements.
- **Policy Period:** The Claim must have been made against the Insured after the policy starts (sometimes called the date of inception) and before it expires (typically a one-year period).

Fourth – Exclusions

- Even if an Insuring Agreement is triggered, an exclusion may preclude coverage for all or part of the submitted claim (see below).

Fifth – Endorsements

- Provisions added to the policy after the insurer's standard policy form often change, add or delete the policy's coverage terms and conditions.

Sixth – Self-Insured Retention

- If a matter is covered, the insured organization must pay or incur a certain amount of loss before the insurer will begin making payments.
- This is similar to a deductible applicable to other types of insurance.
- Side A Claims are not subject to a retention.

COMMON D&O INSURANCE CLAIMS FOR NONPROFIT ENTITIES

Governance Liability

- Donors may dispute directors' allocation and management decisions, claiming that such decisions were not made in the best interest of the organization and its mission.
- Claims premised on negligence, misrepresentations and mismanagement are broadly covered.

Indemnification

- If an organization must indemnify D&Os for their losses, the Side-B coverage is meant to reimburse the organization for its indemnification payments.

Regulatory Investigations and Proceedings

- Coverage often helps offset costs arising from a government investigation or regulatory proceeding, but the scope of coverage depends on a policy's definitions.
- Policies often do not cover civil or criminal fines or penalties, subject to certain policy-specific exceptions (to the extent insurable by law in a particular jurisdiction).
 - Defense costs associated with a claim seeking to impose fines or penalties might remain covered.
 - Example: Defense costs incurred in connection with a criminal prosecution alleging wrongful harboring of migrants.
 - Example: Defense costs arising from a Department of Justice enforcement action alleging discrimination in the administration of program services.
- Confirm whether the "Claim" definition includes investigations generally or whether a particular type of government allegation must exist to trigger the policy.
 - If a regulator issues a demand for documents or testimony, on its own this may not constitute a Claim for a Wrongful Act (as needed to trigger coverage).

- Definitions of “Claim” usually require a demand for monetary or non-monetary relief. Some insurers do not consider demands for documents or testimony as demands for relief against an Insured.
 - Consider requesting a policy endorsement providing that pre-Claim inquiry costs are also covered.
 - Example: A federal agency contract audit or investigation might not constitute a “Claim” absent a cognizable demand for relief.
- Even if a demand for relief is acknowledged, the Claim remains uncovered if the basis for the demand lacks an alleged Wrongful Act.
 - As with any D&O Claim, the Wrongful Act must have occurred in a person’s capacity as a director or officer to trigger coverage.
 - Example: If Congress, a regulator or a grand jury issues a subpoena seeking information regarding services provided in connection with immigration or asylum programs, coverage may not be available if there is no allegation of a Wrongful Act (even if the subpoena is acknowledged as a Claim).
 - Consider requesting a policy endorsement providing that certain regulatory notices can trigger coverage for defense costs as Claims if they are issued to an insured individual and seek relief without alleging that he/she committed a Wrongful Act.
 - Coverage disputes are common for notices, such as civil investigative demands, in which there is no demand for relief, or no Wrongful Act. Even if the regulator’s action or correspondence does not constitute a Claim, certain policies still cover costs associated with responding to an informal inquiry.

Employment Issues

- Depending on the policy’s definitions and exclusions, employment issues including retaliation and discrimination might be covered.
- Some policies exclude employment coverage altogether, with such issues covered only under a separate Employment Practices Liability policy.

TYPICAL EXCLUSIONS

Contractual Liabilities

- Insurance is not provided as a replacement for performing a contractual obligation.

Insured v. Insured Claims

- Insurers will avoid covering disputes among multiple directors of the same entity, or between the organization and any of its directors.
- This exclusion is typically subject to several exceptions. Confirm scope and impact of the exclusion before engaging directors or accepting a director role.

Fraud, Deliberate Dishonesty & Personal Profit

- Insurers will provide coverage for defense costs incurred in connection with allegations of fraud, deliberate dishonesty and gaining of personal profit unless/until a final, non-appealable adjudication establishes that the conduct actually occurred.
- Once such an adjudication exists, coverage ceases and the insurer is entitled to recover amounts paid in connection with defending against the fraud allegation.

ERISA

- Losses arising from violations of the Employee Retirement Income Security Act do not fall within D&O coverage. Refer to a Fiduciary Liability policy instead.
- Organizations involved in managing a pension or similar fund should ensure appropriate coverage is arranged and should not rely on a D&O policy for related exposures.

Bodily Injury and Property Damage

- Look to a General Liability or similar policy for these types of issues.

Prior Notice

- If a Claim is submitted and accepted under one D&O policy, the Claim is generally excluded from coverage under any other D&O policy (including any renewal of the policy under which the Claim was submitted).

Prior and Pending Litigation

- Policies identify a specific “prior and pending” date. There is no coverage for litigation that exists before that date, or for later litigation premised on acts involved in the earlier litigation.

CONSULT ADVISORS

Attorneys

- A D&O policy is a legal agreement governed by jurisdiction-specific rules and industry practices. Discuss the scope and intended operation of any policy with an experienced attorney.
- Consider legal advice on structuring insurance claims to maximize the likelihood of identifying multiple recovery theories to access several types of policies.

Brokers

- Engage a broker who specializes in D&O coverage. These policies differ significantly from other types of coverage, so relevant experience and industry relationships are key for a broker to be effective.
- Brokers with D&O expertise (and experience placing policies for nonprofit entities in particular) can help assess an organization’s risks, provide benchmarking to identify an appropriate amount of coverage and arrange for policy phrasing providing the broadest available protection.
- While brokers can facilitate requests for policy endorsements that broaden the scope of coverage, policies for nonprofit organizations tend to be relatively inexpensive and subject to low policy limits, limiting policyholders’ negotiating leverage with insurers.

CONSIDER ADDITIONAL TYPES OF INSURANCE

- D&O coverage is separate from Fiduciary, Professional, Employment Practices and Cyber coverages. If a claim is covered under one type of insurance, it is probably excluded under any other type of insurance.
- **Fiduciary Liability Insurance (FLI):** Coverage for claims arising from benefit plan management and fiduciary duty breaches.
 - Example: If individuals involved in an organization's management are also involved in managing employees' benefit plans, FLI will cover employees' allegations of breach of fiduciary duty in managing a plan. D&O coverage will not.
- **Professional Liability/Errors and Omissions Insurance (E&O):** Coverage for claims arising from performing or failing to perform professional services.
 - Example: If an organization performs services for clients, claims by clients arising from those services will be excluded under a D&O policy's exclusion for professional services, but likely covered under an E&O policy.
- **Employment Practices Liability Insurance (EPLI):** Coverage for claims arising from an organization's employment-related activities.
 - Example: If a D&O policy generally excludes employment-related issues including claims alleging discrimination, harassment or retaliation, an EPLI policy can provide the necessary coverage.
- **Cyber Insurance:** Coverage for losses arising from cyber attacks, data breaches and other network security events.
 - Example: Even if a D&O policy covers claims alleging managers failed to adequately protect an organization's networks, cyber insurance will likely cover the costs of actually recovering from a network security event such as data recovery and associated expenses.

This guide is meant to provide general information only, not legal advice. If you have any questions about this guide, please contact NYLPI via <https://bit.ly/ClearinghouseIntake> or the Lawyers Alliance Legal Resource Call Hotline at (212) 219-1800 x224 or ResourceCall@lawyersalliance.org. For information about our organizations, visit www.nylpi.org and www.lawyersalliance.org.



ABOUT THE NONPROFIT RESILIENCY NETWORK

The [Nonprofit Resiliency Network](#) strengthens and protects the nonprofit sector by providing informational resources, relationship-building, practical training, and legal advice and representation to nonprofits and CBOs dealing with the changing landscape at a time when nonprofits are needed more than ever. It will foster collaboration, build capacity, and distribute essential resources and legal advice to build resilient nonprofits.



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