

# INSURANCE PROTECTION

# FOR TRUSTEES?

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## KEY POINTS

1. Trustee fiduciary professionals should confirm that vicarious liability coverage is included in their E&O policy acting in their **trustee** capacity.
2. Force placed policy (or lender-placed) **does not** include general liability insurance coverage.
3. A fiduciary bond will not cover the cost of a defense in a lawsuit nor will it pay the settlement to the plaintiff without seeking reimbursement from the fiduciary.

**F**iduciaries, like trustees, often assume that they have appropriate insurance coverage to cover them in the event of a lawsuit. Sometimes, however, that assumption is wrong particularly when a trustee is being sued for the errors of others. The article below examines how Errors and Omissions Insurance can help protect the trustee and their firm against some of the most common insurance claim situations and its limitations.

### Cyber Liability Claims

Trustees are increasingly having to defend themselves from claims of cyber liability and data breach. The loss can occur from a variety of actions such as a debtor stealing a laptop, hacking a network or intentionally misplacing hard copy data files. When this happens, a party may look to the trustee alleging that the trustee failed to adequately protect against the loss of sensitive data.

Without Errors and Omissions Insurance, the costs can mount quickly post-breach as the trustee may incur:

- forensic costs to determine the scope and source of the breach; and
- legal expenses to determine reasonable and/or statutorily required responses.

These initial responses also typically require notification be sent to any former employee or client of a company that their personal data may have been breached. Further, an offer for credit or identity monitoring will need to be presented to the same parties.

Even if a trustee takes these steps, third parties still may suffer damages and may look to the trustee to compensate them based on allegations of invasion of privacy and actual losses due to the breach. And even if no liability is found significant defense costs likely will be incurred.

### Vicarious Liability for the Negligence of Subcontractors

Trustees utilize sub-contractors for many of the vital services during the bankruptcy process. These professionals include appraisers, auctioneers, attorneys, property appraisers, etc. The trustee, however, can be held vicariously liable for any errors or omissions caused by these professional actions.

Trustees, of course, need to ensure they are performing adequate due diligence regarding the reputation, conduct, and state licensure of these contracted professionals. As part of this due diligence it is important to remember that these profes-

sionals are eligible for their own errors and omissions policies. An imperative question for the trustee to consider is whether there are certificates of insurance that show that E&O coverage is in place, active and with an adequate limit in case of a professional liability allegation.

**If not, the trustee will need to ensure that they have their own or their firm has errors and omissions coverage that covers this vicarious liability.**

### Failure to Use Proper Diligence Investigating Debtors Assets

A creditor may allege that they were paid either the wrong amounts and/or in the wrong priority. There is also the possibility that a trustee may unintentionally fail to discover a debtor asset.

Any of these scenarios can trigger an error and omission claim against the trustee. These actions are not the typical duties of a CPA or attorney and are often specifically **excluded** or do not have affirmative coverage from lawyers and accountants professional policies.

Again, the cost to defend allegations even if proven untrue can escalate quickly. The only true solution is for a trustee to obtain a trustee specific errors and omissions policy.

### Your Firm's Liability Policy May Not Cover Actions Taken As Trustee

A trustee may think that they do not need E&O coverage because their firm's professional liability policy provides coverage for all claims. A significant point to consider is whether the vicarious liability coverage includes action taken in their **trustee** capacity. The fact is that there are many insurance policies that cover their actions *only* as an attorney or CPA. Without proper coverage, it could be left to the court to determine in what capacity the professional acted in and whether there is a claim denial by the insurance carrier if these allegations are litigated.

A related misconception is the notion that a fiduciary's bond would respond to help mitigate the cost of a settlement or defense in the absence of necessary insurance coverage. The reality is the fiduciary and/or their firm will have to reimburse the bond company for costs incurred in settlement and directly pay for their defense and settlement of a drawn-out lawsuit.

**KEY POINT:** A fiduciary bond will not cover the cost of a defense in a lawsuit nor will it pay the settlement to the plaintiff without seeking reimbursement from the fiduciary.

This is important to note as we have been told by trustee colleagues that they did not need to obtain either property or

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### About the Authors

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includes experience in legal research and financial management, employee benefit management and human resources.

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liability coverage because “they were protected by their blanket bond.” This is a mistake that could cost a fiduciary their position.

### What an E&O Policy WILL NOT COVER

While E&O coverage is a powerful tool, it is not a panacea against all problems. An E&O policy will NOT directly cover the **absence of other insurance coverages** (e.g., property or liability insurance coverage). The intention of the E&O policy is not to replace a coverage that should have been obtained by a fiduciary. Evidence of other coverages would have to exist for the E&O coverage to respond as it was intended to.

For a practical example, let’s assume a slip and fall lawsuit has just been filed against the estate involving a fiduciary held property. A first thought might be:

“The E&O policy will cover any liability.”

A second thought might be:

“The bank has force placed insurance. Their insurance company and legal counsel will handle this. No need to worry.”

Unfortunately, both assumptions are incorrect.

An E&O claim for not obtaining general liability insurance will not be honored as it is the fiduciary’s duty to properly identify the existing liability of any asset they manage in a case. Should the fiduciary be a named party in a slip & fall lawsuit and not have obtained general liability coverage, renewing their professional E&O policy will become problematic if not impossible.

Likewise, a force placed policy (or lender-placed) **does not** include general liability insurance coverage. This policy would only cover claims against their interest in the structure. If none of the claims in the lawsuit fall into that category the fiduciary and their firm would have to pay for the defense and any settlement or judgment. Suddenly, the lawsuit that was assumed to be “no problem” is a financial nightmare.

The fiduciary could have avoided this scenario by obtaining a general liability policy. These policies are simple and relatively inexpensive.

- **What is it?** General Liability Insurance, also called Commercial Liability Insurance, is a policy that covers third-party lawsuits over bodily injuries and property damage. A “third party” can be anyone other than the insured’s employee (e.g., a customer, client or a business partner).
- **What does it cover?** General liability covers the cost of investigating claims and defending against third-party lawsuits. It pays attorney fees, court costs, witness fees, settlements, and court-ordered judgments. The policy may also cover an injured party’s immediate medical expenses and the cost of repairing or replacing their damaged property.

Using the slip and fall example above, if the debtor or customer sustains bodily injuries, they may sue for medical expenses. If and when this happens, a claim may be made on the general liability policy to cover litigation costs.

In short, trustees are targets for lawsuits. The cost of obtaining the proper insurance coverage is far less than facing the consequences of not having coverage and it is worth the time to make sure that you have the correct insurance coverage in place. 🏠



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February 23-24, 2018

Room Rate: \$229, All Suite hotel

Sessions Begin Friday

### 2018 Annual Convention

The Ritz Carlton, Amelia Island

August 16-18, 2018

Room Rate: \$239

Sessions Begin Thursday

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