



Federal Deposit Insurance Corporation
550 17th Street, NW, Washington, D.C. 20429-9990

Financial Institution Letter
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Director and Officer Liability Insurance Policies, Exclusions, and Indemnification for Civil Money Penalties

Summary: The FDIC has recently noted an increase in exclusionary terms or provisions in director and officer liability insurance policies purchased by financial institutions. These exclusions may limit insurance coverage under certain circumstances, thereby increasing the potential personal exposure of board members and bank officers in civil lawsuits. The attached advisory discusses the importance of thoroughly reviewing and understanding the risks associated with coverage exclusions contained in director and officer liability insurance policies. Additionally, the FDIC is issuing a reminder that an insured depository institution or depository institution holding company may not purchase an insurance policy that would indemnify institution-affiliated parties (IAPs) for civil money penalties (CMPs) assessed against them. Even if the IAP agrees to reimburse the depository institution for the cost of such coverage, the purchase of the insurance policy by the depository institution is prohibited.

Statement of Applicability to Institutions With Total Assets Under \$1 Billion: This Financial Institution Letter applies to all FDIC-supervised banks and savings associations, including community institutions.

Distribution:

FDIC-Supervised Banks (Commercial and Savings)

Suggested Routing:

Board of Directors
Senior Executive Officers

Attachment:

Advisory Statement on Director and Officer Liability Insurance Policies, Exclusions, and Indemnification for Civil Money Penalties

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Highlights:

- The purchase of liability insurance is a legitimate business activity that protects directors and officers who prudently discharge their duties. Liability insurance also helps financial institutions attract and retain qualified personnel.
- Insurers are increasingly adding exclusionary language to insurance policies that directors and officers should clearly understand, as it has the potential to limit coverage and leave officers and directors personally responsible for claims not covered by those policies.
- Also, as such policies are considered, directors and officers should keep in mind that FDIC regulations prohibit an insured depository institution or depository institution holding company from purchasing insurance that would be used to pay or reimburse an IAP for the cost of any CMP assessed against such person in an administrative proceeding or civil action commenced by any federal banking agency. See 12 U.S.C. § 1828(k)(6) and 12 C.F.R. § 359.1(l)(2)(i).
- The regulations do not include an exception for cases in which the IAP reimburses the depository institution for the designated cost of the CMP coverage.

**Advisory Statement on
Director and Officer Liability Insurance Policies, Exclusions, and
Indemnification for Civil Money Penalties**

A basic principle underlying the use of director and officer (D&O) liability insurance is that financial institutions (as well as depositors and shareholders) are best served by knowledgeable directors and officers who make carefully considered strategic risk decisions on behalf of the institution. Appropriately structured D&O coverage can protect directors and officers that discharge their duties in a prudent manner and enable financial institutions to attract and retain qualified individuals to manage and oversee the operations of the institution.

In recent years, the FDIC has noted an increase in exclusionary terms or provisions contained in depository institutions' D&O insurance policies that may adversely affect the recruitment and retention of well-qualified individuals. When such exclusions apply, directors and officers may not have insurance coverage and may be personally liable for damages arising out of civil suits relating to their decisions and actions. In some cases, directors and officers may not be fully aware of the addition or significance of such exclusionary language.

The board of directors' choice of coverage in a D&O policy should be based on a well-informed analysis of costs and benefits, and an important consideration is the potential impact to directors and officers that could result from exclusions. The FDIC urges each board member and executive officer to fully understand the answers to the following questions regarding D&O insurance coverage, especially when considering renewals and amendments of existing policies:

- What protections do I want from my institution's D&O policy?
- What exclusions exist in my institution's D&O policy?
- Are any of the exclusions new, and if so, how do they change my coverage?
- What is my potential personal financial exposure arising from each policy exclusion?

D&O liability insurance is an important risk mitigation tool for financial institutions, and it is vital for directors and senior executives to fully understand the protections and limitations provided by such policies.

In obtaining D&O insurance, the board of directors should also keep in mind that FDIC regulations prohibit an insured depository institution or depository institution holding company from purchasing insurance that would be used to pay or reimburse an institution-affiliated party (IAP) for the cost of any civil money penalty (CMP) assessed against such person in an administrative proceeding or civil action commenced by any federal banking agency. *See* 12 U.S.C. § 1828(k)(6), and 12 C.F.R. § 359.1(1)(2)(i). The regulations do not include an exception for cases in which the IAP reimburses the depository institution for the designated cost of the CMP coverage.