

Directors' and Officers' liability exposures for Sporting Associations

With the current heightened regulatory environment and increasing investigations into companies, Directors and Officers (D&O) have a greater duty to protect against liability for wrongful acts committed in their capacity.

Jardine Lloyd Thompson Limited (JLT) has prepared the following paper to highlight the key exposures for president, management and senior members of sporting associations to individual liabilities arising from their conduct in those capacities.

Board Governance

There may be instances where the board do not act in a prudent manner or where individual board members are inadequately informed as to their responsibilities. Each board member has a standard to conduct themselves using the three basic duties of care, loyalty and obedience. The business judgement principle protects those board members who have acted with a good faith belief that their decision was in the best interests of the association.

The Plaintiff's top allegations in this area include:

1. Failure to identify and adequately deal with conflicts of interest
2. Failure to define responsibilities and roles
3. Mistakes or errors in judgement
4. Failure in disclosure of material facts
5. Issuing or endorsing false or misleading reports
6. Dissemination of false or misleading information
7. Permitting the organization to make improper guarantees
8. Fraudulent conduct, reports, financial statements or certificates
9. Violation of provisions of articles or by-laws
10. Improper self-dealing
11. Acquiescence in conduct of fellow directors engaged in improper self-dealing
12. Transactions with companies in which members are personally interested

Stakeholders

Although sporting associations have no publicly traded equity or debt they do have stakeholders who are at least partially dependent on the association's ability to perform efficiently. These fall into the following categories:

Customers

A sporting association will be a supplier under business to business and business to customer relationships. No doubt some of these arrangements are governed by contracts, which is a potential area for dispute. Whilst most of these claims are more Errors and Omissions (E&O) claims in their nature it is possible a claimant would name a director to bring attention to his action, and the D&O policy would provide defence costs coverage for such a dispute (provided there is not a contractual exclusion). Any management issues at a sporting association may have an effect on their ability to maintain their role in the supply chain. The lack of proper business continuity planning would be a management issue.

Competitors

A sporting association may be involved in contracts concerning image rights and intellectual property rights. The directors are ultimately responsible for the policy on patents and treatment of intellectual property rights and may well find themselves named in litigation. It is therefore important to either remove the copyright/patent exclusion or at least soften the preamble to exclude claims brought "for" a breach rather than "arising out of or in any way attributable to... "

Suppliers and Partners

A sporting association will owe a strict liability under contract and liability in tort to those companies which markets its events or allows products to be made under license. The decision of a sporting association to invest in or divest itself of partner companies that could attract a liability at board level.

General Liability

A sporting association will have liability emanating from its events and products, from its conduct as a corporate citizen, and from a health and safety angle with regard to its employees and the public at large. Whilst claims directly "for" property damage and bodily injury are necessarily excluded, the exclusion should not be absolute



in nature and should allow where directors are named for defence costs until final adjudication at appeal.

In terms of environmental pollution claims it may be government agencies that would seek to investigate or censure the management of the company.

Members

Directors and officers of membership associations are vulnerable to claims brought by members alleging harm to the interests of the member. Any policy exclusion for "Insured versus Insured" claims should be removed or softened by the addition of carve backs.

Donors

A non-profit association contributors may sue directors and officers alleging misuse of a restricted gift. Members could also be subject to litigation arising out of their acceptance of gifts or inappropriate inducements.

Human Resources

The Tillinghast Towers Perrin D&O survey shows that the largest group of claimants by the number of claims brought is employees. Typically these may be of the employment practice type, but may subsequently evolve, if things are not expediently dealt with, into whistle blower claims, which will alert the industry regulators and other stakeholders such as customers. We at JLT have seen a wrongful termination suit in the US develop into a formal investigation into price fixing, and subsequently a customer class action by virtue of the fact that the claimant possessed information, which he used to further his original employment suit.

Financial Operations

For any entity with exposure to the world of finance, default of loan repayments or exceeding of overdraft arrangements can lead to legal action against directors. Allegations of trading whilst technically insolvent, which is a criminal act in some countries, are likely to develop into claims against individual directors and officers under the D&O policy (unless there is an insolvency exclusion) because the company is unlikely to find the funds to indemnify the directors when the judgement is given against them.

For more information on any of the issues covered or for general enquiries about how JLT can assist Sporting Associations, please contact:

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Examples include:

- Allegation of Financial Mismanagement
- Inefficient administration resulting in losses
- Sale of assets for unreasonably low prices
- Wasting of assets
- Extension of credit where not warranted
- Failure to ascertain whether extension of credit is warranted

Investigations / Regulators

Whilst a sporting association does not operate in a formally regulated industry, they will still be subject to competition rules (DOJ, EC) proper tax and Accounting (IRS, Inland Revenue, SEC, BIS). They may find themselves subject to a formal investigation into the affairs of the company. Most D&O policies will now cover the cost of representation at such an investigation on behalf of the directors and recently we have seen this achieved without sublimit.

Attorney General and other government officials may bring suits alleging breach of state or government laws.

Reputation

Often the senior people in associations will be called for comment in the press. This may lead to allegations of libel, slander or reputational damage by members or third parties. A D&O policy will defend such actions and pay awards of damages if such comment was given in their capacity as senior member or president of the association.

Membership

Directors and Officers of membership associations are at risk of suits alleging harm to the interests of the member. There may be suits alleging discrimination against certain members or member groups or concerning member disputes over certification.

Event exposure

If the association's events generate significant income for the association then the leadership will be expected to allow for cancellation or abandonment and the resultant lost revenue. Failure to adequately prepare or insure for such eventualities may bring allegations of mismanagement from the members.

Safety

Sporting associations will have exposure to lawsuits alleging inadequate safety procedures for player and spectators. Also as a ruling body, any change in the rules or refereeing criteria may lead to bodily injury. D&O policies exclude direct claims for damages resulting from bodily injury but they can defend allegations of failure to supervise or implement the correct safety procedures.

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