Your D&O Policy Looks Standard. Read It Anyway.

What D&O insurance actually is, why investors care about it, and what to look for before they carry it.

By Jacob J. Denham

Given the recent headlines in the public markets, expect more media attention on directors and officers, and the protections they actually have.

That isn't just a public-company conversation. Regardless of stage, size, or whether you're public or private, one question looms: When someone challenges how the company was run, who pays?

For most startups, the answer starts with D&O insurance. And for most founders, D&O is something an investor will eventually ask about.

What D&O Insurance Is

D&O stands for directors and officers: the board members and executives who run a company. D&O insurance pays to defend and resolve lawsuits over their business decisions (and only those; more on that below), so the costs don't come out of their own pockets.

It usually does that in two ways:

- **It reimburses the company.** Companies usually promise to pay their leaders' legal costs. D&O pays the company back.
- **It covers directors and officers when the company can't.** If the company is broke, or the law won't let it pay, D&O protects directors and officers directly. That keeps a lawsuit from reaching their personal savings.

What It Covers

D&O covers lawsuits over business decisions someone later claims were wrong. Common examples in new ventures:

- A shareholder who says they were misled about the company's finances.
- An early investor who says the board hid something important.
- A co-founder who isn't on the policy and says the equity split was misrepresented.

What It Won't Cover

D&O covers mistakes and disputed business decisions. It doesn't cover deliberate fraud, or personal bad behavior that has nothing to do with someone's role running the company.

Other suits, like employee lawsuits, injuries, or property damage, fall under different insurance policies.

Why Investors Want It

Their person is about to be on your board. Once their partner takes a board seat, that partner faces the same exposure as everyone else. Investors often require D&O before that happens.

It protects their money. Without insurance, defending your leaders comes out of the company's bank account, and that money doesn't come back.

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That's precious capital paying us lawyers instead of building the business.

It keeps an exit easy. When a company is sold, buyers commonly require years of extra coverage, called a "tail," for claims about decisions made before the sale. Insurers typically won't sell a tail unless D&O is already in place, so having it avoids a potentially massive roadblock.

It signals a serious founder. Investors read D&O as a sign that a founder has thought about governance.

What You Should Look For

I know how much founders love paperwork. But taking the time to read and understand your D&O policy offers a peace of mind that's hard to find in the land of new ventures.

Here's what to look for in any policy, before signing and at every renewal:

- **Enough coverage.** Legal fees usually count against the policy's maximum payout, so make sure the limit leaves room for both a defense and a settlement.
- **Protection for people first.** Leaders should be covered when the company can't pay.
- **The right people covered.** Current and former directors and officers, including an investor's board member.
- **No gaps.** Coverage for past business decisions, not just ones made after the policy starts.
- **The insider and big-shareholder exclusions.** Many policies won't cover claims brought by other policyholders, or by shareholders who own more than a certain percentage.

D&O can't prevent challenges to your decisions. It determines who's financially protected when they come.

Save this for the next time you're thinking about a D&O policy.

And if you're putting D&O in place, renewing it, or about to promise an investor you'll carry it, I'm happy to talk it through.

For More Information

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