

Excess vs. umbrella limits

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Many nonprofit organizations seek to increase the amount of their liability insurance protection for a variety of reasons, such as when —

- The organization expands, perhaps by internal growth or merger, so that the former liability insurance limits no longer fit the organization's new liability exposures.
- A newsworthy jury verdict or appellate court decision alerts the organization's senior management or board to the need for broader or higher limits of liability insurance.
- A major change in the organization's leadership (e.g., board chair or CEO) brings in top management that is more conservative, less willing to tolerate uncertainties associated with potentially ruinous liability losses.

When the concerned leaders of these organizations ask for increased liability coverage from their current liability carriers, those carriers that are willing to cooperate often offer these organizations either *excess liability* insurance or *umbrella liability* insurance above their existing primary liability insurance.

Traditionally, there have been clear, significant differences between excess liability and umbrella liability insurance — differences that managers responsible for managing a nonprofit's insurance have had to understand to be sure that their organizations were protected by adequate liability insurance. Recently, however, these once sharp distinctions have become blurred. Insurers have introduced liability policy forms that combine the distinguishing features of excess liability and umbrella liability policies, sometimes renaming these new policies in the process. Consequently, it is no longer safe to judge a liability policy by its title, watching for the key words "excess" and "umbrella." Now, the responsible nonprofit executive often must read several liability policies in their entirety to understand their liability protection.

To make reading these policies more manageable, this fact sheet first describes the traditional distinctions between excess and umbrella liability insurance and then touches upon the differences in some of the newer hybrid forms.

The Traditional Distinctions

For the past several decades and until quite recently, it has been the case that:

- Excess liability insurance (1) overlays a specific liability insurance policy that an organization already owns by increasing the per person and per accident or per occurrence limits of liability in that particular policy; (2) incorporates all the provisions of the specific underlying policy, such as its insuring agreements, definitions, exclusions, and limitations (or "follows form" with the underlying policy); but (3) does not have any effect on any other liability insurance policies that the insured organization may have.
- Umbrella liability insurance, in contrast, (1) overlays most of the major policies in an organization's liability insurance program, increasing the limits of liability in each of the liability policies in that organization's program; (2) typically offers broader coverage, with few exclusions or limitations and more liberal definitions than the underlying liability policies in the organization's program, and (3) "drops down" to provide first-dollar liability coverage (above any "self-insured retention" or other deductible) in many (but not all) areas of potential liability for which the organization has no other, more specific, liability coverage.

To illustrate these traditional differences between excess insurance and umbrella insurance arrangements, let us consider first some excess liability insurance and then substitute umbrella insurance. (Only the largest nonprofit organizations carry both excess and umbrella liability policies; most nonprofits rely on one or the other.) Start by supposing that a nonprofit's liability insurance program rests on four underlying primary policies:

- Commercial General Liability (CGL) policy with a \$2 million per occurrence limit
- Automobile liability insurance with a \$1 million per occurrence limit
- Professional liability insurance with a \$3 million per occurrence limit
- A Directors' and Officers' (D&O) liability policy with a \$1.5 million per claim limit

Suppose, as one alternative, that this nonprofit's program also includes, as a traditional excess liability policy, a CGL policy with a \$3 million per occurrence limit. Under this excess-insurance alternative, its liability insurance program consists of:

- CGL insurance of \$5 (\$2 + \$3) million per occurrence
- Automobile liability insurance of \$1 million per occurrence
- Professional liability insurance of \$3 million per occurrence
- Directors' and Officers' (D&O) liability insurance of \$1.5 million per claim

Now as the second alternative, assume that this organization does not buy excess CGL coverage with a \$3 million per occurrence limit but, instead, purchases a traditional umbrella liability policy with the same \$3 million per occurrence limits. Each of the original primary insurance limits then increases by \$3 million, so that this nonprofit's liability insurance program, under the umbrella insurance alternative, consists of:

- CGL insurance of \$5 (\$2 + \$3) million per occurrence
- Automobile liability

insurance of \$4 (\$1 + \$3) million per occurrence

- Professional liability

insurance of \$6 (\$3 + \$3) million per occurrence

- Directors' and Officers (D&O) liability insurance of \$4.5 (\$1.5 + \$3) million per claim

The traditional umbrella insurance clearly costs — and typically is worth — more than the excess coverage for three reasons. First, the traditional umbrella coverage increases the automobile, professional liability, and D&O coverage limits, but the excess coverage does not. Second, the broadly written umbrella coverage provides insurance for many of the "following-form" exclusions and limitations that the excess coverage imports from the underlying primary policies. Third, traditional umbrella liability insurance provides (subject to any self-insured retentions or other deductibles) first-dollar coverage of exposures the more specific liability policies never address. Umbrella liability policy costs more than excess liability insurance but, for virtually any organization with the range of exposures that characterize its particular rating class, the umbrella provides more protection than the excess insurance policy. At least, that's generally true for the traditional excess and umbrella liability insurance arrangements.

Some Ongoing Changes

But traditions are changing. Some insurance policies with "excess " in their titles now increase policy limits for several underlying policies, not just the traditional single policy. Some policies that are still called "umbrellas" have no "drop down" feature like those that used to fill in many coverage gaps within and between primary policies. Furthermore, some newly named "umbrellas" are almost indistinguishable from traditional excess liability policies.

In short, one can no longer confidently judge many new liability policies by their titles. One has no choice but to read them, or read at least the insurer's very detailed descriptions of these often long and complex documents. The traditional distinctions between excess and umbrella coverages still matter — which primary limits are being increased, what are the exclusions and other coverage limitations, what is happening with coverage gaps within and between the primary policies — but these distinctions are not as clear as they once were, and they may emerge in surprising places and ways. Change is in progress, and change usually brings progress that ultimately benefits consumers of all goods and services. In the meantime, nonprofit buyers of increased limits of liability insurance beware. Stay alert — read carefully!