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How to Read an Insurance Policy

(This document was adapted from *Coverage, Claims & Consequences: An Insurance Handbook for Nonprofits*, available at www.nonprofitrisk.org.)

An insurance policy is a contract that defines the obligations of both the insured and the insurer. Most insurance policies contain terms that are hard to understand and policies are often written in a confusing manner. Taking the time to understand your policies is well worth the effort. Besides providing coverage, policies also assign certain responsibilities to the insured. Your failure to meet these obligations may impair the coverage your nonprofit relies on for protection.

Every insurance policy has five parts: *declarations*, *insuring agreements*, *definitions*, *exclusions* and *conditions*. Many policies contain a sixth part: *endorsements*. Use these sections as guideposts in reviewing the policies. Examine each part to identify its key provisions and requirements.

Declarations

The Declarations or *dec* page is usually the first page of the policy. It summarizes key information specific to the policy. The dec page shows the insured's name and address, the policy dates, a brief description of the business, coverages provided, coverage limits, premiums, and the forms applicable to the policy. The declarations section also contains various schedules that identify the location(s) of the insured's operations (including values or limits), the various assigned rating classifications, the rates and rating basis, and any special property covered (cameras, fine arts, construction equipment). If the policy is on a *claims-made* liability form, the dec page will identify it as such, and will show the retroactive date.

Insuring agreements

The insuring agreements specify what the insurance company has agreed to pay for or to provide in exchange for the premium. Often a policy contains a section clearly marked *insuring agreements*, although there may be additional agreements buried in the policy. Also, the policy may call an insuring agreement a *coverage* and many policies include more than one coverage. For example, a commercial general liability policy may provide Coverage A - Bodily Injury and Property Damage, Coverage B - Personal and Advertising Injury, and Coverage C - Medical Payments. Some policies, such as commercial general liability, contain separate

insurance agreements for each coverage area. Policies also call insuring agreements *supplemental, additional, or extended coverages*.

An insurance policy begins by declaring what it covers and then proceeds to restrict, limit, and exclude coverages. For example, under a directors' and officers' liability policy, the insuring agreement may state that "the company will pay on behalf of the insured all loss that the insured becomes legally obligated to pay due to a claim first made against the insured during the policy period because of a wrongful act." As you read the policy, you must research the definitions of insured, loss, claim, policy period, and wrongful act to determine if the policy will cover the incident and for whom. You cannot simply read the insuring agreements to understand the coverage. Read the entire policy and refer back to the various insuring agreements and other provisions to understand the coverages and limitations.

Definitions

Insurance policies contain many common words that have special meaning within the context of insurance. The policy identifies these words usually by bold print or quotation marks. Most policies contain a section entitled *definitions* where they explain the special meaning of the designated words. Since definitions may restrict or limit coverage, it is essential that policyholders read definitions carefully and seek clarification whenever a definition is unclear.

Exclusions

Every insurance policy has exclusions or policy provisions that eliminate coverage for specified exposures. *Exclusions* serve as a way to clarify the coverages granted by the policy. Most policies have a section entitled Exclusions. However, an exclusionary provision can be anywhere in the policy. Furthermore, an exclusion may also contain a broadening provision. In the commercial general liability policy, the *Aircraft, Auto, or Watercraft Exclusions* eliminate coverage for the ownership, maintenance, use, or entrustment of these vehicles or vessels. However, the exclusion has five exceptions where the policy covers watercraft, such as while ashore on the insured's premises and for certain nonowned watercraft. Or under a directors' and officers' liability policy a contractual exclusion may also be a broadening provision when it indicates that the exclusion does not apply to an employment practices claim. Always read the policy carefully and note the provisions that apply to your operations.

Conditions

Conditions within an insurance policy qualify the various promises made by the insurance company. The insurer does not promise to cover all losses. The company will impose certain requirements or conditions on the insured, such as premium payment or duties to follow after a loss. Another example is that the insurer promises to pay and provide other services only if the insured event occurs and if the insured has fulfilled its contractual obligations. Review the policy to identify the conditions that the organization must follow. Failure to meet your obligations can void the policy or otherwise restrict coverage.

Endorsements

Most policies also contain *endorsements*. Endorsements are policy forms that modify the main coverage form. Endorsements can add coverage (adding employment practices liability) or they can modify the coverage by revising a definition (providing coverage for nonmonetary claims). Lastly, an endorsement can restrict or exclude coverage, such as an endorsement that excludes claims from pending and prior litigation.

Steps in Reviewing an Insurance Policy

Review the organization's insurance policies upon receipt. Before buying any new coverage, an organization can request and review sample policies. However, many people find it difficult to fully understand the scope of coverages without considering a specific loss. One approach is to identify the risks or types of losses an organization expects to experience — an office fire, windstorm, injury (suffered by an employee, volunteer or client), auto accident, theft, or other risks. Then, determine if the policies will cover these expected losses. Ask your insurance advisor to assist with the review process. Here are the steps:

1. Check for accuracy. Insurance companies are notorious for issuing incorrect policies. The policy may contain spelling errors, the wrong named insured, incorrect additional insureds, the wrong forms, or not include a purchased coverage. Refer any errors to the appropriate insurance agent or broker immediately. Remember that this is a contract. If an organization does not address an error, it can become a problem if a loss related to the error occurs.
2. Review the rating classifications and other schedules. Check to see what rating classifications the company assigned to your organization. The company calculates the premium charge based on certain rating classifications. There can be substantial differences in the rates among the classifications. One insurance company assigned a *circus* rating classification to a workers' compensation policy for a nonprofit sports organization. The circus rates were much higher than the appropriate classification of *outside sales* and did not reflect the insured's exposures. Ask your insurance advisor to explain any classifications that do not seem to describe the organization's operations.
3. Read the policy and answer these questions.
 - Does the insuring agreement cover each expected claim?
 - Is there any exclusion or other provision that eliminates or restricts coverage?
 - Are there any exclusion exceptions that restore coverage?
 - What policy conditions must the organization comply with?
 - Are the people or operations affected by the conditions aware of them? For example, if the policy requires that a burglar alarm always be operational, have you informed the office manager, maintenance staff, or other appropriate personnel?
 - If the loss is covered, is there a deductible? How much is it?
 - How much will the policy pay for each loss?

An insurance contract is a complex contract with conflicting and confusing provisions. You must read the *entire* contract to fully understand the coverages, the insurance company's responsibilities, and your obligations. Some insurance advisors recommend that buyers review the endorsements first to identify those sections of the main policy form altered by the endorsements. This makes the process of reading the main form easier by alerting the reader in advance to sections deleted or altered via endorsement.

During litigation based on disputes over whether coverage applies, the courts have scrutinized a wide range of policies. Unfortunately, various courts have rendered conflicting interpretations. In contrast, most losses do not involve complex policy interpretations — the insurance company and insured quickly agree that the policy covers the loss. However, you must know your duties and responsibilities to qualify for coverage. Take the time to understand your policies. Your insurance advisor (agent, broker or consultant) can help you with this task. The staff at the Nonprofit Risk Management Center is also available to help you. Contact us at (202) 785-3891 with your general questions about insurance or your specific questions about the coverage you have purchased to protect your nonprofit.