



A Quick Guide for **Background Screening Firms to Consider When Selecting an Insurance Policy**

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A Quick Guide to Help Background Screening Firms Select The Right Insurance Policy To Meet Their Needs

Background screening is a highly litigious area of business and having the right insurance coverage in place will not only help you sleep better at night, but also help protect your business.

The number of lawsuits brought under the Fair Credit Reporting Act (FCRA) was the highest on record at the close of 2019. FCRA litigation increased by 8.7 percent year-over-year, with 4,163 claims filed through October 2019, according to data-tracking firm WebRecon LLC.

According to Good Jobs First, a 22-year old non-profit based in Washington DC focusing on government and

corporate accountability over the last decade, employers and background check companies have shelled out more than \$325 million to settle related litigation.

A good insurance policy can mean the difference between continued existence or bankruptcy, or at least the difference between a profitable year and a highly unprofitable year.

The purpose of this white paper is to help guide you towards selecting a better insurance policy.

Why is it important to have a good Errors & Omissions (E & O) insurance policy?

Mistakes happen. And we all know that screening companies can be sued even when it appears that they did not make any mistake whatsoever. An Errors and Omissions policy provides a critical “backstop” for a screening company. If the policy wording is “right,” it can cover all or nearly all damages, settlement amounts, and attorney fees in an actual or threatened lawsuit.

Error and Omissions, also called Miscellaneous Professional Liability is the most important line of coverage for screening companies. The definition is, “what you do as a Professional Service in return for a fee.” In the screening world, it is where you find coverage for The FCRA and similar State and Local laws. A very well written policie will also cover

Governmental fines, fee’s, penalties and investigations and give you a bodily injury carve-back for mental anguish and emotional and emotional distress. Your policy should be a stand-alone policy and not combined by endorsement in a General Liability Policy.

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How do you find a good E&O insurance policy?

Most insurance agents know little to nothing about the background screening industry. As a result, they typically have no idea what policy language may be useful and favorable to screening companies and what policy language may compromise coverage entirely. Accordingly, we believe it’s important for screening companies to seek out and work with agents that have familiarity with the screening industry.

We also believe it’s worthwhile for screening companies to work closely with their legal counsel on insurance policy language. For most screening companies, the insurance policy is the single most important contract that they have.

Michael Burke, Director of Background Screening, Rooney Insurance estimates that approximately 75-80% of the policies he reviews for background screening companies currently are lacking in important coverages. Burke said, “It is not that they are bad insurance agents, but they just do not understand the risks, laws, and government entities involved.” The agent needs to have indepth knowledge of the background screening industry to be able to ask the right questions to understand each client’s business and their specific needs. This helps the agent to be able to explain the risk to the underwriters so they provide the right coverage for the best premium.



What is the #1 policy item for screening companies to consider when evaluating the quality of an E&O Policy?

The exclusions (i.e., a description of the types of lawsuits that will not be covered by the insurance policy). Too many Errors & Omissions policies contain exclusions that preclude coverage for the most significant background screening claims. For example, many policies exclude coverage for Fair Credit Reporting Act (FCRA) claims, even though these claims are the most likely type that a screening company will face. Where the exclusions are problematic, a screening company is essentially paying good money for nothing.

In addition to paying close attention to the exclusions in the policy a background screening company also needs to look at the endorsements. When reading the endorsements, it is especially important that you look at the words that are in bold because these will have definitions. Admittedly, Insurance Policies are a bit more difficult to read than your typical novel, but nevertheless it is important that a background screening firm thoroughly read and understand what is in the policy being presented to them. It is a wise move to have legal counsel review it as well. Please note that the counsel that reviews the insurance policy should have specialized knowledge of the background screening industry so that they fully understand the risk your business may face. Do not make the mistake of simply having your in-house attorney or even external attorney that only has a general knowledge of the background screening industry review the policy you are considering. There is too much at stake to make this mistake.

Which common claim “exclusions” in an E&O policy should concern a screening company the most?

The following exclusions tend to be of most concern:

- (1) FCRA claim exclusion,
- (2) consumer protection claim exclusion,
- (3) privacy claim exclusion,
- (4) federal and state law violation exclusion.

These types of exclusions, in particular, signal a lack of meaningful coverage and should serve as a big red flag.

Recent cases have demonstrated how important it is to cover investigations, fines, fees, and penalties from the Consumer Financial Protect Bureau (CFPB) or the Federal Trade Commission.

Most E&O policies completely exclude bodily injury, however, it is crucial to have mental anguish and emotional distress covered in your policy.



Besides the exclusions, what other parts of an E & O insurance policy really matter?

Attorney Paler:

The Professional Services definition is especially important. It needs to be broad, not specific and needs to accurately describe what your business does. Getting the professional service description right is crucial because any lawsuit related to activities that fall outside of the professional service description likely will not be covered. For example, if a professional services description indicates that a background screening company will solely perform “pre-employment screening,” then lawsuits related to screening on active employees, prospective tenants, volunteers, and others may not be covered. - *continued on page 4*

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In addition to carefully reviewing the professional services description, it is very important to carefully scrutinize the deductible (i.e., how much the insured pays on a claim before coverage kicks in), the limits (i.e. the maximum amount of coverage), the insured's ability to select its own counsel, and whether attorney fees on a lawsuit will deplete the policy limits.

As mentioned earlier having the right Attorney is mission critical. Simply having an attorney who is knowledgeable of the FCRA is not enough. The attorney that reviews your policy really needs to have experience and knowledge of the background screening business.

Many carriers will not offer defense outside the limits of the Professional Services definition and endorsements, however, there are carriers that will and you should definitely seek them out because this will give you a lot more coverage.



The rule of thumb in the industry is to get as much insurance as you can comfortably afford. Limits of 2 million and 5 million are probably good for medium companies. Once you get to the larger companies with revenues approaching, or in excess of 10 million, we see limits of 7.5 million, 10 million, 15 million and beyond.

What amount of deductible is reasonable for an E&O policy?

The deductible is the amount of money that an insured must pay before the insurance company begins footing the bill for a lawsuit. They can vary substantially from policy to policy. We have seen deductibles as low as \$1,000 and as high as \$150,000. This number matters. For example, if a company has a \$75,000, 100,000, or \$150,000, they will likely be handling single plaintiff cases without much help from the insurance company. If the deductible is only \$1,000, the company may be paying higher premiums than necessary. We tend to prefer a deductible in the \$10,000 to \$20,000 range for most of our clients.

Also, sometimes we will see a separate deductible for class actions. Ours typically run between \$2,500 and \$25,000. Most are 2,500 to \$10,000.

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Can you negotiate with insurance companies on the terms of an E & O policy?

Yes!!! This is the biggest misconception in the industry. Insurance policies are not one-size-fits-all, are not “standard,” and are not “off the shelf.” Often, screening companies can obtain a much better policy by negotiating. However, like most things in life, the insurance companies willingness to negotiate depends on many factors. One of the first items they will review is your loss runs. If a company has had several claims or a large claim, it will greatly reduce your ability to negotiate. The size of the company is also a factor they will look at and the controls they have in place to avoid litigation.

Once again, it is extremely important that the Agent and/or Broker understands the industry so they will know what questions to ask and areas to negotiate with the carrier on.

If the insurance company won't negotiate on issues that really matter, screening companies are well advised to consider other policy options.

How much E & O coverage is sufficient (i.e., what should “aggregate limits” be)?

According to Attorney Scott Paler the answer is the typical one you would expect from an attorney – *“It depends! It depends on the volume of checks that the screening company runs, whether the screening company has a large client base in high risk areas like California and New York, whether the screening company makes reporting judgment calls conservatively or aggressively, and the screening company's asset portfolio.”*

If an insurance company is providing coverage for a CRA, can the CRA still use its regular attorney to defend it in a lawsuit?

Most policies will state that insureds need to use “panel counsel” (i.e. law firms pre-selected and approved by the insurance company). The problem is that most “panel counsel” know little to nothing about background screening claims, require the screening companies to spend lots of time educating them, and take far too long to cogently assess the value of a case. Smart screening companies are pushing back on the “panel counsel” requirement and either seeking permission to select counsel of their choosing or getting their own counsel pre-approved.

It is always best to have “choice of counsel,” but for carriers that will not offer choice, which is the vast majority, many will agree to have a specific Attorney endorsed on the policy.

Would you expect an E & O insurance policy to cover emotional distress damages and does it matter?

Often, they do not cover emotional distress damages. This is a problem because in many single-plaintiff cases the emotional distress “damages” greatly exceed the amount of lost income or conventional monetary damages. It’s worthwhile for screening companies to seek out an acceptable policy that has a sufficient amount of emotional distress damage coverage. Its important to seek out a carrier that will provide this type of coverage.

Will an E & O policy that applies to a parent company or family of companies provide coverage for a CRA that is related?

Maybe, maybe not. A policy is a form of a contract. If the policy states that it covers ABC parent company, but makes no mention of XYZ subsidiary, then the insurance company may retain the ability to say that the policy does not cover a claim involving XYZ subsidiary. If a medium-size or large claim comes in, the insurance company may very well decline coverage. Accordingly, we think it’s important to make sure that the insurance policy identifies all covered entities by name and that the policy is written correctly. Ideally, you should seek out a carrier that provides you a “Description of Operations” document along with your application.



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In what situations have you seen an insurance company deny coverage for a background screening company?

Attorney Paler share that, “One situation sticks out the most on his mind. A few years ago a screening company found out at the worst possible time not only that it had been sued in an FCRA class action, but that its insurance policy excluded coverage for claims based on “federal or state law violations.” The combination of these two problems drove the company out of business.” Paler added, “We have been shouting from the roof tops for the industry to seek out better insurance coverage ever since.”

Michael Burke, a seasoned background screening profession shared that, “A number of companies have come to us after being denied coverage or fearing they might be. The only time we’ve seen an issue with one of our policies arise was when the plaintiff attorney mistakenly sued the CRA for Bodily Injury (3rd party death claim) when they should have sued alleging FCRA law violations instead. In this particular instance, we were able to find coverage in the General Liability policy that provided for our client’s defense. Had the plaintiff attorney sued correctly, our client’s E & O policy would have responded.”

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What types of insurance coverage should CRAs consider besides E & O coverage?

Background screening companies may wish to consider a variety of options.

Two types of policies that are gaining popularity in the industry and that are very worthy of serious consideration are:

- (1) data breach/cyber liability policies and
- (2) employment practices liability policies.

The point of this article is to provide background screening companies with a deeper understanding of the intricacies involved in selecting an insurance carrier, the various factors they should consider and to

emphasize the critical importance of fully understanding what is contained in the insurance policy you are purchasing. It is also absolutely essential that you select a carrier that has a deep knowledge of the background screening business and use an experience attorney that has expert knowledge of the industry as well.

****Disclaimer: Nothing in this article should be considered as legal advice. All readers should consult with competent legal counsel to analyze their specific situation before making any insurance related decisions.****

About the Contributors

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