

Directors' and Officers' Liability Insurance

In partnership with the Institute of Directors
(IoD) in Ireland

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BACKGROUND

What is Directors & Officers (D&O) Insurance?

D&O is a form of insurance that protects directors, officers and others with managerial responsibility from legal and other costs that they may become personally liable to pay as a result of litigations by various parties.

The key point is being “personally liable” – too many directors rely entirely on company arranged D&O insurance without assessing the adequacy of this.

A Director is defined widely in the policy wording.

The Need for Cover (1)

- Companies allow Directors to benefit from limited liability in their business dealing but that limited liability protection can be lost if third parties can demonstrate that the director has not acted in a professional manner.
- There is extensive legislation under which Directors can be personally prosecuted or legally pursued such as Health & Safety Legislation, Competition Law etc.
- Directors can be the subject of Government or Quasi-Governmental investigations with their associated costs.

The Need for Cover (2)

- Who is exposed?
 - Anyone who is a director of a company, charity or any other institution run by a board or committee is at risk.
 - If a third party suffers financially as a result of the actions of the directors then they may bring legal action against those people. Limited liability will not apply.

The Need for Cover (3)

- Directors of small enterprises often believe they are less exposed to large claims against them than the directors of larger companies. It is sometimes easier to successfully prove the personal liability of directors and officers in smaller businesses than in larger ones.
- Many directors misunderstand the scope of their company's other insurance policies e.g. Employers' Liability and Public Liability insurance. These only apply to third party injury or damage to property.

The Legal position (1)

- An increase in legislation and regulation of companies has increased the potential for directors to be sued as individuals by shareholders, employees, creditors and competitors.
- The Companies Act 2014 consolidated and reformed the Companies Acts 1963 to 2013.
- It also increased the chance of the directors being personally prosecuted by a regulatory body such as the Health and Safety Authority (HSA) or the Competition Authority and investigations by the Office of the Director of Corporate Enforcement (ODCE).

The Legal position (2)

- Directors can be held personally liable for pollution and environmental damage. Much of Ireland's environmental legislation provides that a director may also be guilty of an offence.
- Potential claimants are increasingly aware of their rights, and can enter into a conditional fee agreements.
- Directors can be held liable for various offences under the Safety, Health and Welfare at Work Act 2005, where the director authorised or consented to the acts that constituted the offence.

The Legal position (3)

- Company directors can be held personally liable for breaches of competition law, even where the company has not been prosecuted, provided that the director authorised or consented to the breaches.
- If a company commits certain revenue offences, a director can be deemed guilty where the offence is shown to have been committed with the consent or connivance, or attributable to any recklessness, of the director in question.
- A director can be held liable for offences under the Data Protection Acts 1988 and 2003 where a company commits an offence with his consent or connivance.
- In certain limited circumstances, a director may be liable for acts of the employees of the company where a criminal offence has been committed by the company.



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WHO MIGHT BRING A CLAIM AND CLAIM EXAMPLES

Who might bring an action?

- Office of the Director of Corporate Enforcement
 - Reckless Trading
 - Director's Loans
 - Breaches of Company Law
 - Director Disqualification
- Competition Authorities
- Health and Safety Authority
- Employees (Employment Practices Liability)
- Shareholders
- Creditors
- Receivers, liquidators and administrators
- Customers and suppliers
- Past, present and potential Employees
- Vendors
- Competitors

Examples of claims involving Individual Directors

- Government Investigations
- Tax Investigations
- Shareholder Actions
- Corporate Manslaughter (UK)
- Insolvency issues
- Misrepresentation issues
- Health & Safety issues
- Breach of duty and conspiracy

Some Specific Claims Examples

- Following a takeover s/holders commenced an action against the directors alleging they were misled as to the terms of the deal.
- A creditor pursued 3 directors alleging that they continued to take materials on credit knowing the company could no longer meet its obligations.
- An allegation of slander was made by a customer of a retailer following alleged comments made by a director impacting reputation.



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How is a Director Indemnified

Indemnity from Company (1)

- The extent to which Irish companies can indemnify directors is limited. A company can only indemnify a director for:
 - Liability that does not involve negligence, default, breach of duty or breach of trust.
 - Costs incurred by a director in successfully defending a case against him.
- Where the constitution of a company or a contract seeks to indemnify a director in relation to matters restricted by the Companies Act 2014, the provisions will be void.

Indemnity from Company (2)

- A director may not be able to rely on financial assistance from their company if they are sued because
 - The company has no funds (directors are often sued when the company is insolvent)
 - It is not permitted by its Articles of Association.
 - It is not permitted legally e.g. under the Companies Acts
- If the directors and officers cannot receive indemnity from the company, and have no Directors' & Officers' Liability (D&O) insurance, then they will have to pay the loss settlement (and defence costs) out of their own pockets.
- Company Law makes it clear that a company is allowed to pay for a D&O policy in relation to any negligence, default, breach of duty or breach of trust.



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How does D&O insurance work?



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D&O Policy Cover

- D&O cover is designed to cover the personal liabilities of the individual directors; it is not designed to protect the company for claims made against it.
- Whilst the company purchases the policy it is for the benefit of the directors.

Operative Clause

- The policy will typically indemnify the directors for legal liability to pay damages, settlements and legal costs and defence costs arising from a wrongful act committed in their capacity as directors of the company.
- It does not cover all the directors personal liabilities only those that arise from them acting as directors of the company.



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Who is Protected?

- Past, present and future Directors
- Employees – usually only in an Employment Practices Liability (EPL) incident or where they hold supervisory or management positions
- Management Committee Member
- Lawful Spouses of a Director
- Estate, heir or legal representatives of deceased Insured or legal representatives of an Insured in the event of incapacity, insolvency or bankruptcy.

Two Cover Sections

The policy is divided into two sections:

- Section 1 indemnifies the directors for their personal liability where the Company is not able or permitted to indemnify them
- Section 2 indemnifies the Company where they are able and permitted to indemnify directors and officers for claims against them.

The typical policy does not indemnify the Company for claims against it – only for losses they incur in indemnifying the director or officer.

Claims Made

D&O policies are always written on a 'claims made' basis. This means that they cover claims made:

- Against the directors or officers during the policy year, regardless of when the alleged wrongful act occurred;
- After the policy year, arising from circumstances first advised to the insurer during the policy year.

Therefore any claim notified during the period of cover which relates to any alleged wrongful act, that act is deemed to have occurred during the period of insurance.



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Wrongful Act

A wrongful act is usually defined as:

'Any actual or alleged breach of duty, breach of trust, neglect, error, misstatement, misleading statement, omission, breach of warranty or authority or other act by the directors, officers or employees in their respective capacities as a director or officer of the company'.

Claims and Definition of Loss (1)

Claims covered include any:

- Suits or proceedings brought by any person or organisation against the insured for monetary damages or other relief, including non-pecuniary relief
- Written demand from any person or organisation that it is the intention of the person or organisation to hold the insured responsible for the results of any specified wrongful act
- Criminal prosecution brought against the insured
- Administrative or regulatory proceeding or official investigation regarding any specified wrongful act of the insured.

Claims and Definition of Loss (2)

Loss means damages, judgments, settlements and defence costs. However, loss does not include:

- Criminal fines or penalties imposed by law
- Non-compensatory damages including punitive or exemplary damages (other than damages awarded for libel and slander)
- Taxes
- Any amount for which the insured is not legally liable or matters which may be considered uninsurable under the law pursuant to which the policy shall be construed.

Limit of Indemnity

- The limit of indemnity is stipulated in the schedule of the policy and is often in the aggregate for the policy period. This means that it applies to all claims made in the policy year.
- It is also usually costs inclusive.
- Directors should pay close attention to the limit of indemnity. Limits of indemnity should be bespoke to each company's specific risk profile.

Investigation Costs

Most D&O policies extend to indemnify directors for their legal representation costs in the event of an official investigation into the company. This cover is often subject to a sub-limit. In summary, the following are covered:

- The costs of representation and defence in civil or criminal proceedings
- The costs of their representation if required at any inquiry into the affairs of their company.
- As regulation increases, this has become a more valuable extension.

Extensions/ Endorsements

Extensions and endorsements to policies include:

- Employees and Employment Practices Liability
- **Individual Director Policies**
- Outside Board cover
- **Pollution**
- **Retired Directors Run-off**
- Retention Reimbursement/ Waiver
- Brexit Extension
- Entity Cover
- Allocation Endorsements
- Acquisitions
- Discovery Period



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Individual Director Policies

- It is possible to arrange cover with specialist D&O insurers on an 'individual' basis for a particular director that will cover all directorships held by them in distinct companies.
- Such individual cover is a contract between the director and the insurer and does not involve any company in which they hold office. For this reason, there is no company reimbursement cover.

Pollution

- Limited cover is provided for defence costs incurred by a director or officer in defending themselves against criminal or regulatory environmental proceedings.
- Many policies also indemnify settlement and defence costs in respect of claims by shareholders alleging loss of share value by reason of pollution.

Retired Directors Run-Off

- Policies cover actions against retired directors. This extension extends the cover for the retired directors for a specified 'discovery period' in the event that the company cancels their D&O cover.
- Discovery periods commence from the date the policy is lapsed (provided alternative insurance is not arranged).
- Common discovery periods are six or ten years, although some policies do provide lifetime run-off cover. They provide cover for wrongful acts discovered during (but committed prior to) the discovery period.
- The cover is usually provided automatically without additional premium.

Exclusions

The policy is subject to various exclusions, including:

- Insured vs. Insured
- Major Shareholder Exclusion
- Bodily Injury and Property Damage
- Professional Services
- Dishonest Acts
- Criminal Fines and Penalties
- Prior or Pending Litigation
- Circumstances Advised
- North American Claims
- Prospectus Liability



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Conclusion and Wrap Up

What are the key questions Directors should ask?

- What is the policy limit of indemnity?
- Assuming it is an aggregate limit, how many directors are covered and the size and complexity of the company?
- To what extent can a company indemnify a director and does it have the financial resources to do so?
- Legal advice should be sought on this?
- Claims reporting and extended reporting periods – what are they?
- Request a copy of the policy wording and have it checked independently.

Summary

- All Directors should be asking questions re D&O insurance arranged for their benefit.
- Your personal assets are at risk.
- Do not depend on Company arranged policies without checking the detail.
- Seek independent advice.
- Do this annually as policy terms and conditions can change year to year.



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Thank you for your time

QUESTIONS