fact sheet

Directors' and Officers' Liability Insurance

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Preliminary

In the Wizard of Oz Dorothy is warned to be "careful what you wish for …". Those of you with ambitions to be appointed as Director of a company may do well to be mindful of that warning.

You will be well-advised to take out insurance to protect you against some of the risks.

This Fact Sheet gives you key points on Directors' and Officers' liability insurance.

The Companies Act 2006

Section 232 of the 2006 Act states that any provision which attempts to exempt a director of a company from any liability for negligence, default, breach of duty or breach of trust is void. Furthermore, any provision by which a company provides an indemnity to a director against liability for negligence, default, breach of duty or breach of trust is also void, subject to the following three exceptions.

1. Qualifying third party indemnity provision (QTPIP)

Section 234 allows a company to provide an indemnity to a director against liability for negligence, default, breach of duty and breach of trust incurred to third parties (i.e. not the company or an associated company). These are known as 'qualifying third party indemnity provisions'.

In order for a QTPIP to qualify as an exception to the Section 232 prohibition, the indemnity must exclude criminal and regulatory fines payable by the director. It must also exclude defence costs for criminal proceedings where the director is convicted, defence costs for civil proceedings brought by the company where judgement is given against the director and costs incurred in connection with an application for relief where the court refuses to grant such relief.

Section 236 of the 2006 Act requires that where a QTPIP is in force for one or more directors at any time during the financial year, this fact must be disclosed in the directors' report for that year. Section 237 also requires that a copy of the QTPIP or a written note of its terms must be available for inspection at the company's registered office and kept for at least one year from its expiry/termination.

2. Qualifying pension scheme indemnity provision (QPSIP)

Section 235 allows a company that is a trustee of an occupational pension scheme to indemnify a director against liability incurred in connection with the trustee company's activities. Such provisions are known as 'qualifying pension's scheme indemnity provisions'.

In order to qualify as an exception to the Sections 232 prohibition, the indemnity cannot cover liability for fines imposed in criminal proceedings, penalties payable to regulatory authorities or any liability incurred in unsuccessfully defending criminal proceedings.

The requirements regarding disclosure set out above apply equally to QPSIP's.

3. Directors' and officers' insurance

The types of claims that directors and officers may find themselves facing are very diverse and can include claims for breaches of health and safety legislation, misrepresentation, liability under the Equality Act 2012 and wrongful trading. Section 233 allows a company to purchase insurance for its directors to protect them from liability resulting from negligence, default, breach of duty or breach of trust by them.

Directors' and officers' liability insurance can be purchased as part of a company's insurance programme and the amount of cover required will depend upon the company itself. It is worth noting that a company doing business in the United States will need specialist advice. The contentious and compensatory nature of US society means that insurers are wary of providing cover.

What will the insurance cover?

Generally, directors' and officers' liability insurance will cover "losses" arising from "wrongful acts" although the wording will vary between insurers. Each term will be defined within the specific policy but generally a "wrongful act" will cover breach of duty or trust, negligence, error, misstatement, misleading statement, omission, libel, slander, breach of warranty of authority and wrongful trading. "Losses" will typically include defence costs, awards and damages that the director is liable to pay.

Who will the insurance cover?

Generally, a directors' and officers' insurance policy will cover any director (including non-executive, shadow and de facto directors) or officer (including company secretaries). This can often be extended to include managerial employees, spouses and estates.

What amount of cover can I expect?

The insurance policy is likely to have an overall limit per year set on an aggregate basis. This means there will be a specified amount of money available for the year and any claims will be deducted from this total amount. There may also be financial limits per claim.

Cover is on a "claims-made" basis

Directors' and officers' insurance policies are written on a "claims-made" basis. This means that the insurer at the time the claim is made will be the one responsible for covering a claim as opposed to the insurer who was on risk at the time the original wrongful act was committed.

What types of limitation or exclusions can I expect?

The exclusions and limitations of directors' and officers' insurance will vary according to the insurer and the policy but may include the following:

- **Fraud and dishonesty** – excludes claims where the person insured makes a wrongful gain through fraud or dishonesty. This will be a non-negotiable exclusion.

- **Prior notice** – excludes claims which have been notified under a previous policy because the insurance protects on a "claims-made" basis. Again, this will be a non-negotiable exclusion.

- **Insured v insured claims** - excludes claims bought by one director against another director.

- **Liabilities covered elsewhere** – for example, claims for property damage or personal injury which may be met by employer or public liability policies.

Conclusion

Any person, particularly a prospective non-executive Director should consult with an experienced insurance broker. The choice will be to take out a personal policy: the Institute of Directors has a standard policy. The alternative is a policy taken out by the relevant company.

Rob led the Everyman team effectively and efficiently. We found him to be understanding, patient and supportive and the fee model we agreed removed the need to worry about the cost of every conversation.

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