Why would I need directors' & officers' liability insurance?

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Many people fail to realise that their personal property may be at risk from their conduct in a professional capacity. This article intends to give some examples of the nature of claims and the possible effect on the individuals to which a directors' & officers' (D&O) policy would respond.

Introduction

Broadly speaking, an officer or director of a company may be held personally liable for any decision, act or omission made in their professional capacity within the company. In this article, 'company' refers to any corporate body; be it a non-profit entity such as a trade association, regulator or voluntary organisation, or a privately owned, family-run or publicly listed entity. The claims can be made by any one or more of a number of potential plaintiffs such as: shareholders, investors or owners, trustees-in-bankruptcy, police or public prosecutors, tax authorities, or even the company's peers or competitors. Claims need not necessarily be limited to judicial actions. A threat of legal action or of a raid on premises to seize computers or documents will likely necessitate immediate defensive action and legal costs to protect the company's position or prevent further intrusion.

While most corporate bodies are protected through public limited liability and other insurances, the individuals within a company are often left unprotected, particularly where they have acted without proper authority or breached any part of the Companies Act or similar legislation. The risk is particularly apparent where a company trades in overseas territories.

Depending on the allegations involved, a company may be relieved of its obligation to indemnify directors or officers, at least until the allegation is proven to be false or the individuals are exonerated. Under such circumstances, the directors may be left to personally fund their own legal costs to defend a claim that arises from their conduct in a professional capacity. It is further likely that, in order to give their client the maximum possible opportunity of a successful defence, their lawyer is unlikely to want to join in with other defendants, especially where each party implicated is intent on passing blame to the others, resulting in multiple directors defending themselves individually. Costs can quickly escalate.

How does D&O cover differ from P&I cover?

To many readers of this article, this might not seem to be a significant risk. Your company, be it a shipowning company, a charterer or a ship manager, will most likely buy third-party liability protection and indemnity (P&I) insurance. Therefore, it may be easy to assume that all claims and costs incurred, even those arising as a result of actions taken by directors and officers of the company, will fall within the scope of P&I cover.

The Standard Syndicate

Why would I need directors' & officers' liability insurance? continued

Actually, this may not always be the case. There are many cases where the management team of a shipping company were alleged to have been responsible for losses caused to others. Suits have been brought for loss of life, loss of profits, unfair trade practices or making personal profit at the expense of the company itself. While the majority of claims are covered by P&I or asset (e.g. hull, cargo) insurances, allegations against individual directors may not be, if the alleged wrongdoing relates to activities within the office.

In certain jurisdictions, where multiple plaintiffs are affected, claims can involve a class action or representative actions. This is particularly true in the USA, Canada and Australia. Once again, defence costs can be significant, often running to hundreds of thousands of dollars.

As shipowners seek fresh capital from wider and more diverse sources in the current difficult economic climate, raising public debt or issuing public stock may lead to further exposure to potential liability.

Case studies

We have seen a class action lawsuit being instigated against a US-listed cargo carrier, resulting from the issuance of materially false statements to the Securities and Exchange Commission (SEC). The ensuing $500m asset write-down and the default of loan covenants following the financial correction were disastrous for the company's share price.

In other cases, shareholders have challenged the acquisition of vessels by a company on the basis that these transactions were allegedly the result of self-dealing by directors of the company and that the company entered these transactions on unfair terms.

Not uncommon also are claims by shareholders against directors in respect of alleged excessive payments of directors' fees and other remunerations.

D&O cover from The Standard Syndicate

The Standard Syndicate uses the same service philosophy as The Standard Club, with success built upon its in-depth knowledge of members' operations. The club management and underwriters visit new and existing members, and interact closely with them throughout the course of their membership, often over many years, and not only in the time of a casualty. In doing so, they ensure, wherever possible, that any claim situation is resolved efficiently and amicably to return the member to normal operations as quickly as possible.

The Standard Syndicate's D&O cover can be tailored for individual, specific, needs. We would welcome an opportunity to discuss this cover further with you.

Normal commercial exclusions will apply.