

Directors' and Officers' Liability



Why are Company Directors Exposed?

- Company law imposes express liabilities
- Other laws impose liabilities directly or indirectly:
 - Securities laws
 - Occupational health and safety laws
 - Environmental protection laws
 - Criminal laws
 - Many other laws, rules and regulations, often across multiple jurisdictions
- High public profile
- High degree of responsibility
- Decision making power

Who Can Sue a Director

Any person or entity to whom a duty is owed, including:

- The Company
- Shareholders
- Employees
- Creditors
- Customers
- Intellectual property provider
- Franchisor / franchisee
- Public / Government / Regulators
- ...and many other third parties



Generic Industry Exposures

- Mining
 - Pollution
 - Occupational health and safety
 - Capital raising
- Forestry
 - Pollution
 - Occupational health and safety
- Import/Export
 - Foreign jurisdiction laws
- Manufacturing
 - Occupational health and safety
- Retail
 - Employment practices liability



Foreign Jurisdiction Risk

“In 2005 we required directors to improve disclosure in relation to approximately \$6 billion of fund raising out of a total of over \$15 billion.”

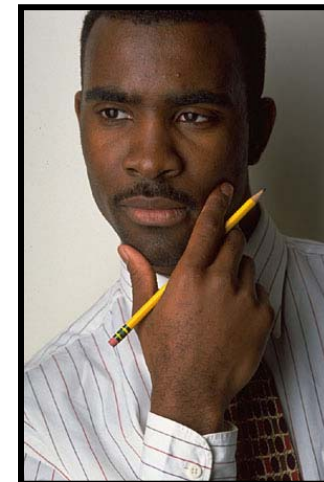
“63 out of 488 troubled companies we visited needed to appoint an administrator.”

“We banned 33 directors who acted dishonestly.”

Jeremy Cooper
Deputy Chairman – ASIC
June 2006

How Do You Know If You Need Insurance?

- You employ staff
- You have external shareholders
- You have non-executive directors
- You have raised debt or equity capital
- You have trade credit arrangements with your suppliers
- You manufacture products
- You import/export products
- You have a license to operate
- You have bought other entities
- You intend to sell your company



Claims Example



- Not-for-profit entity and all directors acting in a voluntary, unpaid capacity
- Victorian Branch collapsed in 1990 with AUD\$255 million of debt
- Collapse attributable to fraud of John Friedrich
- Commonwealth Bank sued to recover debt
- Chairman Max Eise held personally liable for AUD\$97 million (uninsured)

Other claim sources

....overstated profits claims

...oil spill

...manager charged with bullying

...hit by US law suits

...class action against directors



...disqualified then prosecuted

....fatal accident

...mum-to-be sues

...harassment and discrimination

...directors in dock

When a Company Won't Indemnify You:

- Not acting in good faith
- Not acting in best interest of the Company
- Acting unlawfully

The Australian Financial Review
www.afr.com • Wednesday 27 April 2005

9+

Insurers offer to pay legal costs up-front

Andrew Main and Steven Scott

The two biggest directors' and officers' (D&O) insurers in Australia have launched policies promising to pay directors' legal costs up-front following a landmark High Court case.

The two, AIG and Chubb, are targeting directors nervous about the implications of the recent cases in which insurers refused to cover executives' legal costs in ongoing cases because they thought the cases had no merit. But lawyers warn some insurers are likely to tighten the wording of policies.

Two recent High Court decisions muddied the waters on when insurers must pay D&O cover up-front. Former FAI Insurance chief operating officer Daniel Wilkie was able to force his insurer, GIO, to pay his court costs for three charges under the Corporations Act because an exclusion clause only applied if the executive was convicted of a dishonesty offence.

But policy wording differs between insurers. On the same day as the Wilkie decision, the High Court rescinded leave to appeal for former One.Tel executives Jodee Rich and Mark Silbermann, allowing their

insurer CGU to avoid paying court costs in a civil action brought by ASIC. While Rich and Silbermann lost on a separate issue, their policy was different to the GIO contract

"Some insurers are likely to tighten the wording."

held by Mr Wilkie, giving CGU the discretion to pay legal expenses.

AIG and Chubb said they would pay defence costs in similar cases as long as no dishonesty was proved. Other insurers, such as CGU, retain a discretion clause which allows

them to avoid paying legal costs.

Insurers argue they will only pay after the conclusion of the case once it is clear there is no dishonesty.

Jason Grant, regional manager Australasia for AIG's financial lines, said Mr Wilkie would have had his defence costs paid if he had held the new AIG policy. He said his company would not increase premiums as a result of the Wilkie case.

But Freehills partner Mark Darwin predicted that some insurers would alter their policies to allow themselves to refuse to cover legal costs. Mr Darwin said some insurers were trying to use the mere allega-

tion of dishonesty as grounds for refusing to cover legal costs.

"We'll have an unsatisfactory situation where claims managers of insurers will be able to exercise their discretion on the merits of a case without a full hearing of the evidence that the director has been dishonest," he said.

If they cannot afford to fund their own defence, executives might have to settle the case or enter a plea bargain, Mr Darwin said.

Consultant with Clayton Utz Nancy Milne advises executives to carefully assess each policy clause to ensure they are covered.

How does D&O Insurance Work?

Insured Persons

Company
Reimbursement

Entity Cover

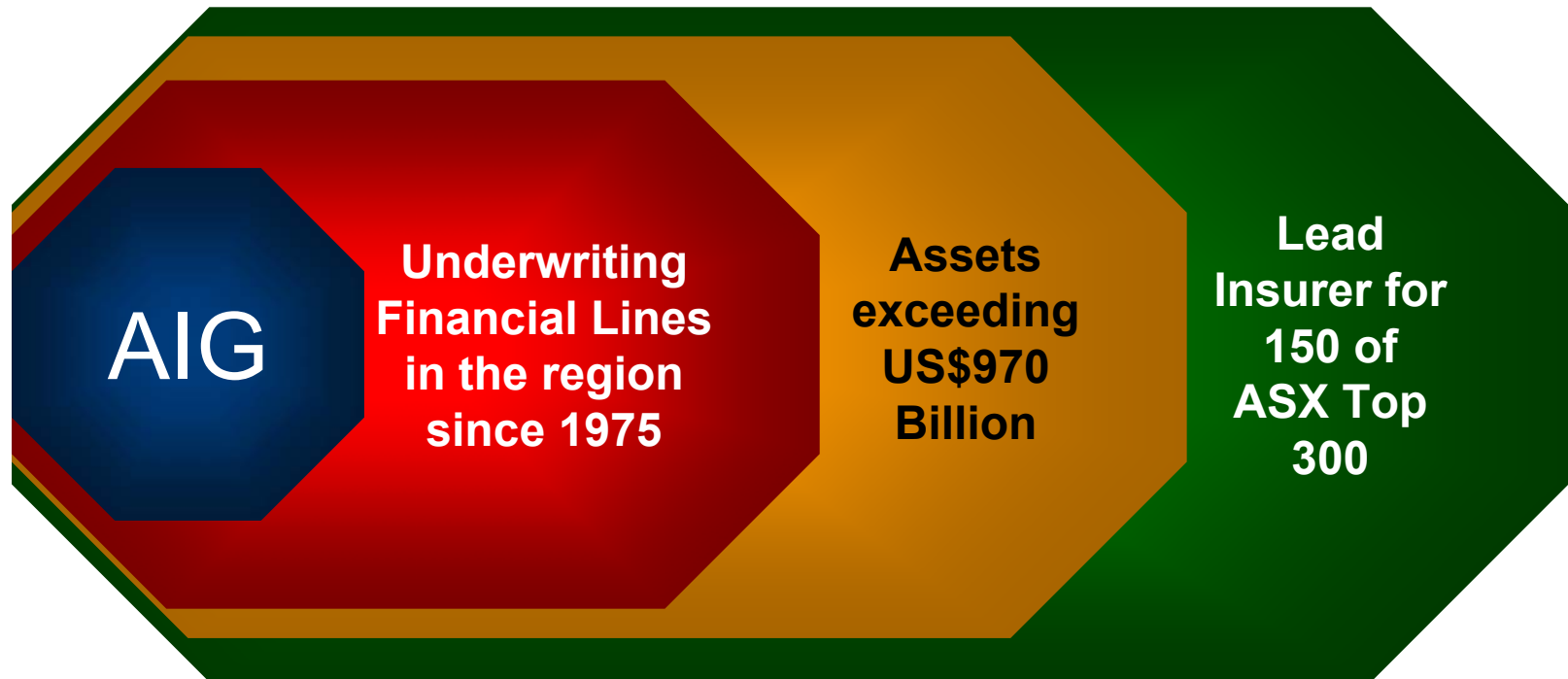
How risk is assessed by Insurers

- Size (turnover / assets / staff)
- Industry exposures
- Shareholder exposures
- Financials
- Equity or debt raisings
- Press articles and local knowledge
- Stock exchange listings



(Governance is difficult to assess with any reliability or consistency, but is definitely a factor in claims)

Why AIG?



Conclusions

1. Directors and Officers are subject to a great many duties under common law, statute and contract
2. They owe these duties to a large number of entities and people, including the company itself, shareholders, employees, regulators, creditors and others
3. Litigation involves personal and sometimes criminal liability and can threaten your assets, livelihood and reputation.

Why wouldn't you obtain insurance?



Confucius say:-

Needing insurance is like needing a parachute. If it isn't there the first time, chances are you won't be needing it again.



Thank you

Any Questions?

The data contained in this presentation is for general informational purposes only and is not intended to be advice for specific circumstances. Users should make their own enquiries and obtain independent advice specific to their circumstances prior to entering into any transaction based on this information. The description of coverage contained in this presentation is a summary only and potential insured's should review the policy in its entirety prior to entering into any transaction. The coverage and any claims made are subject to terms and conditions outlined and certain restrictions, limitations and exclusions contained in the policy of insurance. In the event of any conflict between the descriptions of coverage in this presentation and the policy of insurance, the provisions contained in the policy of insurance will govern.