

# Government proposes new liabilities for directors. What protection will D&O insurance provide?

On 15 July 2013 the Department for Business Innovation and Skills released a Discussion Paper setting out proposals to enhance transparency and increase trust in UK businesses ("Transparency & Trust: Enhancing the Transparency of UK Company Ownership and Increasing Trust in UK Business").

The proposals are intended to give effect to commitments made at the UK-chaired G8 Summit held in June 2013, and include:

- Requiring companies to obtain and hold information on who owns and controls them, including by implementing a central registry of company beneficial ownership information;
- Prohibiting bearer shares and reviewing the use of nominee directors;
- Amending directors' duties in key sectors such as banking in order to promote the financial stability of firms;
- Giving sectoral regulators powers to disqualify directors, expanding the factors courts can take into account when disqualifying directors, and increasing the time limits for bringing disqualification proceedings in insolvent company cases from the current 2 years to 5;
- Giving courts the power to make directors personally liable to compensate creditors if a director is disqualified for misconduct in connection with a company's insolvency.

The final proposal listed above would add significantly to the circumstances in which directors might find themselves personally liable if a company fails. One question arising from the proposals, therefore, is whether this new potential liability for creditors' losses is likely to be covered by the company's Directors' & Officers' ("D&O") insurance.

A key category of claims that D&O insurance is intended to cover is claims that arise in the event of the company's

insolvency, including claims that may be pursued by liquidators or other persons. Furthermore, D&O Policies typically cover directors for liability arising from "Wrongful Acts" – a term that is generally defined widely so as to include essentially any breach of duty by a director.

Directors may therefore anticipate they should be protected by their company's D&O insurance in the event the government implements its proposals and the director finds him or herself the target of a claim to compensate creditors. However, current market wordings for D&O policies provide potential pitfalls in this scenario, meaning this may well not be the case.

D&O policies are written on a "claims made" basis, meaning that only claims or potential claims notified to the insurers during the policy period are covered. The new form of liability proposed by the government would only arise as part of disqualification proceedings brought against the director after the company has failed. By that time the company in question will already be insolvent, and is unlikely still to have any D&O insurance policy in place under which a disqualification proceeding or associated claim for creditor compensation could be notified.

It is possible that after it is clear the company is entering an insolvency procedure the director may be able to take advantage of provisions in the policy allowing him or her to notify a creditor compensation claim as a potential claim to which the policy should respond. The policy may allow this, but much will depend on how soon a demand for compensation is made against the director and whether this occurs before the policy expires. If at policy expiry the

possibility of a claim remains only a remote – and speculative – possibility then the policy may not permit the potential claim to be notified before it expires. This problem will be exacerbated if the government extends the time limit which applies to when disqualification proceedings may be brought from the current 2 years to 5, as it proposes to do.

D&O insurance often contains run-off cover for former directors, sometimes for up to 6 years from the date they ceased to be a director. This run-off cover could help, but the pitfall here is that directors who have been disqualified are typically excluded. Former directors are usually granted run-off cover for breaches of duty they may have committed before they ceased to be directors, but this run-

off cover often does not extend to directors who have been disqualified from acting as directors. Directors facing a claim to compensate creditors as part of disqualification proceedings may find that they are unable to avail themselves of this run-off cover in the very situation in which they need it (although up to the date that the director is disqualified the run-off cover may at least cover the costs of defending a creditor compensation claim).

Directors concerned about the Government's proposals to expand their personal liabilities would be well advised to review their D&O policy wordings carefully, or face the risk of having to bear substantial compensatory awards themselves if the new proposals come into effect.

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