LIABILITY INSURANCE FOCUSING D&O LIABILITY

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TYPES OF LIABILITY INSURANCES

There can be various types of liabilities that may arise under the law of tort/ civil law but the covered liabilities through insurance policies and frequently practiced are as under.

1. Public Liability
2. Product Liability
3. Professional Liability/ Indemnity
4. Cyber Liability
5. Employers Liability / Workmen Compensation
6. Commercial General / Umbrella Liability Insurance including Pollution Liability
7. Clinical Trial Liability Insurance
8. Directors & Officers Liability Insurance

BRIEF BACKGROUND OF LEGAL LIABILITY AND LIABILITY INSURANCE

- Liability means breach of duty of care

- Duty of care is the sense of responsibility or being negligent whether it is:
  a. performance any task/ services
  b. an advise,
  c. manufacturing and selling products or
  d. taking decisions.

- Duty of care arises by operation of common law (i.e. civil law) generally and through statutory law.

- Duty of care/ negligence is also called civil wrong (a french word for civil wrong) or tort which means:
  a. Wrongful act
  b. Causing injury or damage
  c. for which liability may be imposed by law if there is causal connection between the loss and breach of duty

BRIEF BACKGROUND OF LEGAL LIABILITY AND LIABILITY INSURANCE

- The doctrine of duty of care/ negligence arose in 1932 established by Lord Atkinin UK by introducing Neighbor principle.
- This principle was established through a case of Donoghue v Stevenson
- This case elaborates that reasonable care to be taken if you are well aware that you can or your products can injure the third party.
- You should treat your third party as protectively as you treat your neighbor as not to injure them.
- Key to determine duty then rests on foreseeability, proximity and fairness

BRIEF BACKGROUND OF LEGAL LIABILITY AND LIABILITY INSURANCE

- Steps/ Limbs in determining duty of care and creating legal liability

  a. Law determining duty of care
  b. Breach of duty of care
  c. Injury, loss or damage was caused
  d. Breach of duty caused injury, loss or damage

- The above were established through case laws (common law)

- Owing to the financial constraints on loosing party and to cover the cost of damages/ compensation, various liability insurance came into being.

PUBLIC LIABILITY INSURANCE

- It is also called occupiers liability

- Generally covers

  a. bodily injury also leading to death of the third parties and
  b. property damage
  arising out of the business operations of the policy holder.

Few Examples:

a. Unsafe/ defected premises
b. Injury or damage due to works in progress
c. Falling objects
d. Slipping/ tripping

PRODUCT LIABILITY INSURANCE

- It covers

  a. bodily injury also leading to death of the consumer/ third party

  b. property damage

  arising out of the use of the product

"Product" means any property after it has left the custody or control of the Insured which has been designed, specified, formulated, manufactured, constructed, installed, sold, supplied, distributed, treated, serviced, altered or repaired by or on behalf of the Insured.

Few Examples:

a. Use of towels leading to rashes
b. Pharmaceutical products/ confectionaries/ edible items causing injury or disease due to consumption
c. Faulty product design of electrical items causing damage say by way of short circuit
d. Faulty automobile parts leading to accidents causing injury or damage

PROFESSIONAL INDEMNITY INSURANCE

- It has two divisions
  - a. Financial Lines Professional Indemnity
  - b. Commercial Professional Indemnity

- It covers negligence, error and omission in performing professional services leading to
  - a. financial loss to the recipient of services
  - b. bodily injury also leading to death of the third parties and
  - c. property damage

Few Examples:

a. Financial experts giving erroneous advices or accountants doing faulty reporting
b. Designers/ Architects designing faulty structures
c. Lawyers giving faulty opinions and advices
d. Medical practitioners being negligent in providing medical services

CYBER LIABILITY INSURANCE

- Cyber is a buzz word these days
- It is an emerging insurance product in the domestic market
- Cyber is a Greek word i.e. cybernetics/ kubernetes which means a pilot or steersman. Its technical meaning is any thing related to or characteristics of a culture of computer, information technology or virtual reality.
- With the advent of AI and growing digitalization, cyber crimes and security compromises are on rise
- Hence a cyber liability insurance policy is devised to cover digital crimes and frauds.
- It covers

  a. Incident response costs
  b. Business Interruption losses
  c. Data and System recovery costs
  d. Cyber Extortion losses
  e. Privacy and Network Security Liability
  f. Media Liability
  g. Betterment Costs
  h. Cyber Crime
  i. Reward Expenses
  j. Telecommunication Fraud
  k. claim Preparation costs
  l. Hardware replacement
  m. Reputational Hard
  n. Ransomware and fines

EMPLOYERS LIABILITY/ WORKMEN COMPENSATION INSURANCE

- Workmen Compensation operates as per Workmen Compensation Act 1928 and subsequent amendments.
- It covers the death due to bodily injury and disease of the workmen while being in the course of employment.
- It has statutory limits for each province i.e. PKR 500,000 for Sindh, PKR 400,000 for Punjab and Federal Capital, PKR 300,000 for KPK, Gilgit Baltistan and PKR 200,000 for Baluchistan
- On the other hand Employers Liability is a legal liability leading to injury, death due to injury or illness while in the course of employment and due to work/ business operations of the employer.
- Few examples include:
  - a. Loss of hearing due to heavy sounds at work
  - b. Accidents while operating machines
  - c. Work stress related injuries (not very common but can be covered if proven)

COMMERCIAL GENERAL / UMBRELLA LIABILITY INSURANCE

- It is a combination of multiple liabilities specially the casualties excluding the liabilities covering for financial losses.

- This kind of insurance requirement generally is seen as part of contractual requirements from US based companies.

- Umbrella Liability is not a separate insurance or unique insurance cover but just an additional limit is given for big causalities breaching the given usual limit. It is back up limit for mega accidents

- The combination includes liabilities like

  a. Public Liability
  b. Product Liability
  c. Pollution Liability (Accidental and Sudden Pollution)
  d. Excess Automobile Liability for project sites only excluding road traffic act
  e. Advertising Liability
  f. Workmen Compensation / Employers Liability

CLINICAL TRIAL LIABILITY INSURANCE

- This policy is meant to cover injuries caused due to performing clinical trial i.e. testing medicines / pharmaceuticals products on humans or doing any kind of medical research on humans.

- What is clinical trial:

  a. It is investigation on human subjects, whether patients or non-patients and those want to be part of trial on voluntary basis.

  b. It tests and verifies the effects of pharma on humans

  c. identifying any adverse reactions

Few examples of claims:

a. Any kind of sickness like fever, vomiting etc. due to medicine
b. Heart issues
c. loss of sight or loss of hearing

No cover for any pre-existing diseases and medical expenses. Medical expenses are only covered if incurred consequent upon trial causing injury.

BASIS OF CLAIMS

- What is the basis of claims or claim pay out under all foregoing policies.

  a. Damages meaning the actual losses suffered by the claimant.

  b. Court awarded damages

  c. Court awarded compensatory damages

  d. Legal costs and expenses including claimant's costs and expenses for bringing the court case.

DIRECTORS AND OFFICERS LIABILITY INSURANCE

- How this insurance came into being

  a. With economies getting expanded and modernized thus becoming corporate economies, need arose to regulate the corporate sector.

  b. Corporates are mainly based on companies which are either public limited or private limited companies driving the overall economy

  c. With corporate interests of many stakeholders are tied up like employees, customers, shareholders/ investors, creditors, environmentalists etc.

  d. to protect and balance the interest of various stakeholders, those running the corporate owe fiduciary duty (arising from the concept of tort law) towards the stakeholders

DIRECTORS AND OFFICERS LIABILITY INSURANCE

- How this insurance came into being

  e. Therefore a body of regulations called Companies Act 2017 subsequently amended in 2022 was enacted to define duties of directors and consequences of the breach

  f. Section 204 of Companies Act 2017 describes such duties and compels the directors how to perform the duties and in case of breach due to negligence, lack of reasonable care etc. will have consequences to be imposed.

  g. In order to cover financial loss the company and stakeholders may suffer due to negligence of Directors in performing their duties, Directors and Officers Liability Insurance policy was introduced.

DIRECTORS AND OFFICERS LIABILITY INSURANCE

- What is Directors & Officers Liability Insurance

  a. It is an insurance policy that provides cover for Directors and Officers wrongful act due to breach of the directors duties leading to financial loss to the Company provided the loss cannot be indemnified by the Company itself.

  b. This insurance has two elements.

    i. First it covers the D&Os for their wrongful act and pays on behalf of D&O individually.

    ii. It indemnifies the company/ the entity suffering loss due to the wrongful act of the directors and officers and pays on behalf of the company.

DIRECTORS AND OFFICERS LIABILITY INSURANCE

- What is Directors & Officers Liability Insurance

  c. It also pays for Securities claims i.e. claims related to issuance of shares and public offering, raising of capital etc.

  d. It also covers the claims related to wrongful employment practices like wrongful dismissal of employees, harassment etc., termination etc.

  e. It also covers the D&Os individually and the company for D&Os wrongful acts while serving as outside directorships on the directions or request of the company

DIRECTORS AND OFFICERS LIABILITY INSURANCE

- Extended covers under Directors and Officers Liability insurance

  a. Derivative claim costs

  b. Extended Reporting period

  c. Spouses, Domestic Partners, Estates and Legal Representatives

  d. Court Attendance Costs

  e. Emergency Defense Costs

  f. Occupational Health and Safety/Corporate Manslaughter

  g. Protection for Non-Executive Directors

DIRECTORS AND OFFICERS LIABILITY INSURANCE

- Extended covers under Directors and Officers Liability insurance

  h. Lifetime Cover for Retired Directors and Officers

  i. Tax Liability

  j. Bail Bond Costs and Prosecution Costs

  k. Crisis Management Expenses

  l. Future Offerings

  m. Advancement of Defense Costs with a condition of repayment to the Insurer if deemed not covered, subsequently.

  n. Cover for acts occurring prior to Merger and Acquisition transaction date but notified subsequently after the merger but during policy period. Cover for additional no. of days is available upon additional premium, terms and conditions.

  o. Cover is available if an entity becomes subsidiary of an existing insured company but for wrongful acts occurred and discovered after the subsidiary transaction

DIRECTORS AND OFFICERS LIABILITY INSURANCE

- What are directors duties?

  a. directors owe their duties to the company itself and need to prioritse the interest of shareholders including other stakeholders but they don’t owe duty to shareholders personally.

  b. The duties are codified in Companies Act 2017 and in UK Company’s Act 2006

  c. Following are the duties

    i. the duty to act within powers of the constitution/ Articles of Association
    ii. the duty to promote the success of the company
    iii. the duty to exercise independent judgment
    iv. the duty to exercise reasonable care, skill and diligence
    v. the duty to avoid conflicts of interest
    vi. the duty not to accept benefits from third parties
    vii. the duty to declare interest in proposed transactions or arrangement with the company

DIRECTORS AND OFFICERS LIABILITY INSURANCE

- What is Articles of Association (Company’s Constitution) and how is it linked with D&O Liability Insurance Policy

  a. It is the document which describes the powers of directors and shareholders

  b. It is a contractual agreement between the company and its shareholders

  c. Besides describing the purpose of forming the company, it describes how directors are supposed to act and manage the company.

  d. By enforcing the contractual rights through AOA, shareholders can bring legal action against the company for breach of directors duties.

  e. The enforcement of AOA in the court of law, can invoke D&O Liability Insurance for claim payments if proved and found payable.

DIRECTORS AND OFFICERS LIABILITY INSURANCE

- Few Important Concepts

  a. Claims made policy

  b. Retroactive Date / Continuity Date

  c. Discovery of claim

  d. Importance of Territorial Scope from Foreign Members/ Shareholders perspective

  e. Importance of applicable law and jurisdiction from Foreign Members/ Shareholders perspective

  f. Can legal liability be determined without court's intervention?

  g. Basis of claim and actual claim payouts

DIRECTORS AND OFFICERS LIABILITY INSURANCE

- Few Important Concepts

  h. Wrongful Act

  i. Who is Director and Officer

  j. Outside Directorship

DIRECTORS AND OFFICERS LIABILITY INSURANCE

- Major exclusions

  a. Major Shareholders Exclusions

  b. Insured v Insured Exclusion

  c. Political Risks Exclusion

  d. Professional Indemnity Exclusion (how can D&Os negligence is difference from Professional Negligence and thus excluded)

  e. Fraud, illegal profits, bribery exclusion

  f. Known wrongful acts, prior and pending litigation

DIRECTORS AND OFFICERS LIABILITY INSURANCE

- Major exclusions

  g. Claims for bodily injury and property damage

  h. Claims brought in USA, Canada and Australia

  i. Claims occurred before Continuity/ Retroactive Dates

  j. Breach of SECP's provisions

  k. Nuclear Risks Exclusion

  l. Sanction Limitation Exclusion

DIRECTORS AND OFFICERS LIABILITY INSURANCE

- Important Conditions

  a. Non-admission of liability by the Insured

  b. Costs and expenses to be incurred with prior written consent of the Insurer

  c. Timely notification of claim except for regulatory prohibition however notification should still be made as soon as practically possible.

  d. The duty to defend is of Insured, Insurer has the right to participate in proceedings and investigations in order to direct whether D&O Liability Insurance Policy will invoke or not

  e. Insured to cooperate with Insurer in providing all information and to assist in claim investigation

  f. Related and Series of claims to be considered single claim. Commonalities to be determined.

DIRECTORS AND OFFICERS LIABILITY INSURANCE

- Important Underwriting Information

  a. Proposal form: detailing brief about the company

  b. Claim history for 5 years atleast

  c. Profiles of D&Os, their experience etc.

  d. 3 years financials

  e. Company profile

  f. Whether there is any US exposure, if so complete details.

  g. If subsidiaries and outside directorships exist, complete details of the entities and level of shareholding etc. are required.

DIRECTORS AND OFFICERS LIABILITY INSURANCE

Possible claim scenarios

A. Breach of Fiduciary Duty

SITUATION: A shareholder who invested over four million dollars in a land management company files a complaint against the company and its directors and officers alleging breach of fiduciary duty, conspiracy and fraud. In particular, it is alleged that the company (insured) failed to make quarterly distributions, wrongfully transferred funds out of certain properties and participated in sham transactions to the detriment of all shareholders.

OUTCOME: Settlement and defense exceeded $1,200,000

DIRECTORS AND OFFICERS LIABILITY INSURANCE

Possible claim scenarios

B. Non-Entity EPL

SITUATION: Plaintiff agreed to help form and work for a company as its Chief Operating Officer. He alleges that his employment was terminated without cause. Further,
it is alleged that the company hindered his attempt to find new employment by telling third parties that the plaintiff is prohibited from using trade secrets and intellectual property that allegedly belongs to the company. A complaint was filed against the company and a D&O which included causes of action for breach of contract, and unfair and deceptive trade practices.

OUTCOME: Defense costs and settlement for the individually named defendant exceeded $180,000.

DIRECTORS AND OFFICERS LIABILITY INSURANCE

Possible claim scenarios

C. Creditor Claim

SITUATION: Plaintiff filed a complaint against individual D&Os of a company alleging that its CEO, CFO, & COO conspired to use the plaintiff's services to furnish, install and repair the company's equipment knowing that it was insolvent and was planning to file for bankruptcy protection. Causes of action included: (1) fraud, misrepresentation and non-disclosure; (2) deceptive trade practices; and (3) civil conspiracy.

OUTCOME: Total settlement and defense of the individually named defendants exceeded $100,000.

DIRECTORS AND OFFICERS LIABILITY INSURANCE

Possible claim scenarios

D. Class Action Complaint

SITUATION: Plaintiffs represents a class of non-insider stockholders who invested in the company. Plaintiffs allege that certain directors and officers failed to disclose material facts and provided them with inaccurate and misleading information. It is alleged that the materials did not disclose the high turnover of management and that the company's website had not yet been developed. The company later went bankrupt. The complaint included causes of action for: (1) common law fraud; (2) negligent misrepresentation; and (3) breach of fiduciary duties.

OUTCOME: Settled for over $1 million and defense costs exceeding another $1.4 million

DIRECTORS AND OFFICERS LIABILITY INSURANCE

Possible claim scenarios

D. Class Action Complaint

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DIRECTORS AND OFFICERS LIABILITY INSURANCE

Possible claim scenarios

E. Shareholder

SITUATION: The plaintiff alleges that certain directors have exerted complete domination and control over the company and used the company as a vehicle for their own business purposes at the expense of the company and minority shareholders. Specifically, the plaintiff alleges that certain directors helped to renegotiate a service contract and booked all of the revenue during one quarter instead of over the three year life of the contract. The plaintiff also contends that this service contract received steep discounts and would cause other customers to request similar discounts resulting in lost revenue to the company.

OUTCOME: The defense and settlement of this case exceeded $500,000

DIRECTORS AND OFFICERS LIABILITY INSURANCE

Possible claim scenarios

E. Shareholder Derivative Action

SITUATION: A shareholder derivative action is taken against a company for breach of fiduciary duties on behalf of the directors. The plaintiffs contend that the defendants have failed to provide them with certain information, such as shareholder listings, financial data and other corporate records. They also allege that certain directors borrowed money from the company without the Board's approval and subsequently these loans were forgiven.

OUTCOME: Total defense costs and settlement exceeded $500,000

DIRECTORS AND OFFICERS LIABILITY INSURANCE

Possible claim scenarios

F. Foreclosure/Unfair Competition

SITUATION: A shareholder commenced a derivative action against the president of a company which develops and markets chemical compounds, after all its assets were sold. The company entered into an agreement to allow a corporation to test and evaluate its compounds. The corporation subsequently received various patents for the compounds; however, it refused to enter into a licensing agreement with the company. The plaintiff concludes that the company can assert causes of action against the corporation for: breach of contract; breach of fiduciary duty; misappropriation of trade secrets; unfair competition; fraudulent concealment; and intentional misrepresentation. The plaintiff also alleges the company series B shareholders did not approve certain loans. Subsequently, after the company defaulted on the loans, the president decided to execute a foreclosure sale of the company's assets and he advised the shareholders that he is resigning. The plaintiff alleges that the president did not promptly advise the shareholders of the foreclosure sale and he breached his fiduciary duties when failed to have the Company commence litigation against the corporation that was retained to test its compounds. The complaint is comprised of four causes of action, including: (1) negligence, (2) breach of fiduciary duty; (3) concealment; and (4) unfair competition.

OUTCOME: Total defense costs and settlement exceeded $750,000.

DIRECTORS AND OFFICERS LIABILITY INSURANCE

Possible claim scenarios

G. Loan Default

SITUATION: A diversified sports product company received a lawsuit against the President, CEO, and Chairman of the Board for not honoring a promissory note. The plaintiff alleges that it lent $1 million to the company. The company allegedly agreed to pay the funds back within a month pursuant to the promissory note. Despite requests for return of the money, plus interest, the company has not returned the funds to the plaintiff.

OUTCOME: Total defense costs and settlement exceed $250,000.

DIRECTORS AND OFFICERS LIABILITY INSURANCE

Few real case laws on D&Os

a. Re Pure Zanzibar Ltd [2023]

b. Re Noble Vintners Ltd [2019]

c. ClientEarth v Shell plc [2023]

d. Regal (Hastings) Ltd v Gulliver [1942]

e. Howard Smith Ltd v Ampol Petroleum Ltd [1974]

DIRECTORS AND OFFICERS LIABILITY INSURANCE

Is it easy to bring the claim against D&Os and thus invoke the D&O Liability Insurance Policy?

Anwer is No, but why?

DIRECTORS AND OFFICERS LIABILITY INSURANCE

Does this insurance have a commercial viability for both Insurers and Insured

Anwer is Yes, then how if D&O claims are difficult to invoke?

THANK YOU