

India - Is there a need for INDIVIDUAL / PERSONAL D&O LIABILITY INSURANCE POLICY?



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Holding corporate directors and officers accountable for business failures is becoming an increasingly global phenomenon. India is no exception to this. With ever-increasing complexities of business and changing economic and legal landscape, demands are mounting on directors for better compliance on governance and effective delivery on performance. While the impact on the responsibilities and liabilities resulting from various legislations including the Companies Act 2013 is well known, matters seem to be getting more complicated in certain areas as evidenced by some of the recent actions of the government and judicial pronouncements. Let us look at a few of them as listed below:

Disqualification of directors: The Ministry of Corporate Affairs, in the month of October 2017, disqualified around 200000 directors, under Section 164(2)(a) of the Companies Act, 2013. The disqualification of directors and the consequent suspension of their DIN has raised multiple legal questions including the following:

- Retrospective application of Section 164
- Disqualification made from an earlier date
- No opportunity of being heard granted to the disqualified director
- Rights of third party companies affected for no default of theirs and without hearing
- No remedy to the disqualified directors
- Vicarious liability provisions cannot be invoked without action against the principal offender

For a detailed understanding of the above, please read the article "India: The Recent Tale Of Disqualification Of Directors And Myriad Legal Issues" written by Mr. Ankur Khandelwal of Khaitan & Co. available on the following link

<http://www.mondaq.com/india/x/645716/Corporate+Governance/The+Recent+Tale+of+Disqualification+of+Directors+and+Myriad+Legal+Issues>

Invoking Personal Guarantees of Directors: Ministry of Finance, Government of India has recently alerted all banks to take steps to invoke personal guarantees in case of borrower company defaults. With the result, banks are beginning to initiate steps to invoke personal guarantees of defaulting firms even when they face bankruptcy proceedings under Insolvency and Bankruptcy Code, 2016. This move is already facing legal challenges from the promoters who are opposed to parting with their assets, as many legal experts feel that a lender cannot invoke guarantees after a case is admitted to National Company Law Tribunal (NCLT). There is no final word yet on this subject.

Lifting the Corporate Veil: On 22 November 2017, the Supreme Court of

India restrained the independent directors and promoters of Jaiprakash Associates Limited (the parent company of Jaypee Infratech) and their family members from transferring any personal assets or property without the court's permission in order to safeguard homebuyers' interests in Jaypee Infratech. It was inclined to lift the corporate veil of the bankrupt Jaypee Infratech's holding company, going to the extent of barring the promoter and other directors from alienating assets.

Presumption of innocence is a legal right and one is considered innocent unless proven guilty- *ei incumbit probatio qui dicit, non qui negat* (the burden of proof is on the one who declares, not on one who denies).

Assuming that the impacted directors were not dishonest with any ulterior motives and / or were not a party to alleged misdoings, what is the insurance protection available to them in the above mentioned cases? It is unlikely that the above situations including the action for enforcement of rights of directors are covered, except perhaps the third one, under normal Directors & Officers liability insurance (D&O) policies, unless a very wide bespoke coverage was granted. It may be noted here that coverage is not available in respect of fraudulent and dishonest acts, as D&O policies are normally subject to unscrupulous conduct exclusion which triggers upon admission of wrongdoing by the insured person or final adjudication which establishes that the unscrupulous conduct did in fact occur.

Be that as it may, in situations like the above, it is necessary for the directors to defend themselves whether it is for revival of their DIN numbers, unfreezing of the order about alienating their assets and protection of their personal properties. This process may entail heavy legal costs. That the legal costs are on the rise is well known and these costs may prove to be a financial burden for the directors.

Directors may go unprotected because of deficit in the required coverage even when a policy is in force and directors may go unprotected when the companies they work for do not buy/ renew the insurance cover or go bankrupt. As regards dissolution of a company, it is pertinent to note here that all the rights of a director under the Companies Act, 2013, cease to have any validity when the Registrar of Companies (RoC) strikes off a company. However, this does not relieve the director from any liabilities. Sec 248(7) of the Companies Act 2013 reads as under:

The liability, if any, of every director, manager or other officer who was exercising any power of management, and of every member of the company dissolved under sub-section (5), shall continue and may be enforced as if the company had not been dissolved.

Then, how do we address this insurance protection gap?

D&O insurance affords protection to directors and officers against liability arising from actions connected to their corporate responsibilities. The policy provides indemnity to the directors and officers in respect of:

- Legal costs in defending proceedings brought against them alleging wrongful acts.
- Any damages awarded to the claimants against the Directors and Officers, including out of court settlements.

As regards addressing the gaps in coverage and unmet needs, one option is to explore the possibility of getting an Individual or Personal D&O liability insurance policy. Individual or Personal Directorship liability policy can be issued in the name of individual director. Unlike normal D&O policies where buyer is the company and beneficiaries are the directors and officers, here buyer and beneficiary of the policy is one and the same.

This Individual or Personal D&O liability insurance policy is not available in India at present.

In the markets it is currently issued, it is issued as a policy with Drop down coverage. Coverage here applies on an excess basis over existing D&O liability insurance coverage that the employer already obtained.

Broad contours/ benefits of this policy can be as under:

- Policy is issued in the name of the director seeking cover.
- Coverage is available on a floater basis to all the board positions that an individual director holds in various companies.
- Acts as additional layer of support, in the event limit, under the primary D&O policy bought by employer, is exhausted.
- Acts as additional layer of support, in the event coverage is restricted in the primary policy bought by employer.
- Acts as additional layer of support in the event the primary D&O policy insurer is unable to pay for reasons other than coverage issues, e.g. Insolvency.
- Provision for at least defence costs by carving back coverage in certain exclusions.
- Immensely useful for independent directors.
- Purchase of the policy is a personal choice and an individual decision.

The entire purchase process here is initiated and driven by the individual director.

While there is no doubt that an individual D&O policy does address some of the gaps in coverage, it does pose challenges, as practical difficulties abound for insurers to gather and review required information for underwriting the policy. In India, a person can be a director in not more than twenty companies at the same time and the maximum number of public companies in which a person can be appointed as a director shall not exceed ten. Instead of calling for financials of various entities on which one is a director, taking a cue from some of the countries in which this kind of policy is available, insurers may consider seeking relevant information in the proposal from along with the DIN to evaluate granting cover. For operationalising the policy in a simple way, the options for limit of indemnity can be 2 or 3 like ₹ 1 Cr., ₹ 5 Cr and any other higher amount. Other terms and conditions may be worked out after appropriate deliberation.

Since Individual or Personal D&O liability insurance policy is currently not available in the Indian market, insurance companies may look at developing this policy to address the gaps in coverage and also unmet needs in this segment. For the sake of organisational convenience, effective delivery and wider reach, insurance companies planning to issue this policy may seek cooperation from a professional body like Institute of Directors (IOD).

Business is all about taking risks and managing them effectively. This includes well considered risk transfer by way of appropriate insurance. It is absolutely necessary for directors to always exercise due diligence in running their business ensuring compliance with all laws in letter and spirit and seek protection available like indemnity provisions in the letter of appointment and also D&O insurance policy protection. A D&O insurance policy is not a substitute for sound management and corporate governance. It is not a panacea for all ills. But, a good policy helps in as much as it reduces the apprehensions and addresses the concerns of the directors instilling in them confidence to concentrate on their work to discharge their managerial responsibilities properly and fruitfully. ■

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