



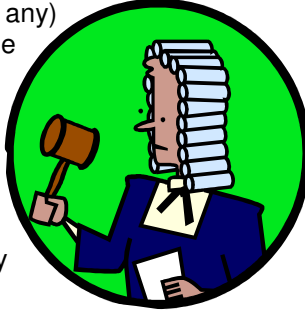
HEIDTMAN & CO.

LAWYERS

DEEDS OF INDEMNITY, INSURANCE AND ACCESS

Directors can be, and often are, held personally liable for losses suffered by various parties as a consequence of their acts or omissions as a company director.

It can also be the case that former directors are forced to defend claims with little (if any) help from the company they once served, and with limited access to company documents.



For these reasons (amongst others which are discussed below) it is important that directors have in place a well drafted Deed of Indemnity, Insurance and Access to give them security in such circumstances.

The advantage of a Deed of Indemnity, Insurance and Access can also extend to key company officers; but in this Fact Sheet the issue is considered only from the perspective of a director for reasons of simplicity and space.

Liability of Directors

Who Is a Director?

The *Corporations Act 2001* (Cth) (the “**Act**”) provides that directors include:

- * persons appointed as directors;
- * persons appointed as alternate directors, when acting in that capacity; (regardless of the name given to their position);
- * persons not so appointed but who act in the position of a director; and
- * persons on and in accordance with whose instructions or wishes the directors are accustomed to acting.

In What Circumstances Can Directors Be Liable?

Directors can be held personally liable for damages suffered by the company as a result of a breach by the director of their duties to exercise reasonable care and diligence, to act in good faith in the best interests of the company, and to act for a proper purpose.

Directors can also be personally liable, both to the company and to company creditors, for losses suffered by creditors as a result of a breach of the duty to prevent insolvent trading.

Furthermore, directors can be held personally liable to compensate third parties for losses, or for penalties, resulting from a breach by the company of certain statutes, some of which impose absolute liability (i.e. directors can be liable without ever having knowledge of the act or omission), and for losses resulting from other acts or omissions by the director (e.g. breach of warranty of authority).

Directors may also have to bear the legal costs of defending any claims brought against them.

Prohibitions on Indemnity

Section 199A of the Act prohibits a company from indemnifying its directors against:

- * liabilities owed to the company or to a related body corporate;
- * liabilities for pecuniary penalty orders or compensation orders (e.g. compensation to creditors for losses suffered as a result of the director breaching the duty to prevent insolvent trading by the company); and
- * liabilities owed to third parties which did not arise out of conduct in good faith.

Section 199A also prohibits a company from indemnifying its

directors against legal costs incurred in defending claims in certain circumstances, such as:

- * proceedings in which the director is found to have a liability for which they could not be indemnified (as above);
- * criminal proceedings in which the director is found guilty; and
- * proceedings brought by ASIC or a liquidator for orders where grounds for making the order are established.

A company may indemnify a director for all other liabilities and costs incurred while acting as a director of the company.

The Value of a Well-Drafted Deed

Indemnity and Insurance

Many company constitutions set out rights of indemnity for directors, and often also include provision for Directors’ and Officers’ insurance.

Directors’ and Officers’ insurance can be important because an indemnity will provide little comfort if the company has insufficient funds to meet a claim by a director for indemnity.

However, a director should not rely solely on the constitution for their right to indemnity and/or insurance. A company’s constitution usually does not bind the company with respect to past directors, and a company can change its constitution. Furthermore, any rights of indemnity or insurance provided for in a constitution may be less extensive than permitted by law.

For these reasons, directors should ensure their company indemnifies them and insures them, to the full extent permitted by law - in accordance with the terms of a properly prepared Deed of Indemnity, Insurance and Access.

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Settlement of Claims

There are many issues which must be considered when negotiating a deed of indemnity. One such issue is settlement of claims.

Most Deeds of Indemnity, Insurance and Access allow a company (or its insurer) to settle a claim on a director's behalf - which they will often do with the foremost intention of reducing the amount payable. However, in settling a claim, a company may not always be acting in the director's best interests. For example, settlement may involve an admission of guilt which may harm a director's future prospects - but the director may not feel that any wrong has been committed.

Accordingly, in our Deed of Indemnity, Insurance and Access, we have included a clause which provides that, whilst a company retains the right to settle a claim on the director's behalf, it may do so only after it has gone through a process which includes:

- * giving notice to the director that a settlement is intended, together with details of that settlement;
- * giving the director an opportunity to dispute any admissions or statements which will be made as part of the settlement; and
- * a dispute resolution procedure in the event the director does not wish the settlement to proceed.

Having said this, the terms and conditions of a deed of indemnity are a matter of agreement between a director and the company.

Storage and Access

It is often not enough that a director be provided with an appropriate indemnity and insurance cover. It is also important that a director have a contractual entitlement to access company documents to ensure an adequate defence can be conducted if necessary, as it may not always be in the company's best interests to see a director succeed in defending an action; for example, if a successful defence by the director would see the company itself become liable, or if access to company documents would enable a



director to prove entitlement to be indemnified out of company assets.

Whilst the *Act* does require companies to keep certain kinds of documents, and also to allow directors access to company documents in certain circumstances, it does not go far enough to protect the interests of directors in certain areas.

Storage: The *Act* requires companies to store certain kinds of company documents, including:

- * company minutes;
- * company registers; and
- * financial records and certain declarations of directors.

However, there are other kinds of company documents, possibly vital to a director's defence, that a company is not required to store (e.g. internal memoranda and communications). Directors should ensure that the company is contractually obliged to keep all company documents that may be important to a defence, not only the ones required by statute.

We recommend that the parties consider whether the Deed of Indemnity, Insurance and Access should require a company to retain, in a secure and readily accessible fashion, a full set of "Board Papers", being all written communications to which a director is entitled to have access during the time they are a director of the company, including notices, board papers, minutes, board committee and sub-committee papers, and all documents referred to therein.

We also recommend that the parties consider whether the Deed of Indemnity, Insurance and Access should extend the protection afforded to directors by not only requiring the company to hold the "Board Papers" for the statutory period of six years within which claims may be brought, after the director ceases to be a director, but also for any period during which legal proceedings are taking place. This is important if a claim begins close to the end of the six year period, in which case the director or their advisors may not have sufficient time to access the documents before the company is entitled to have them destroyed. It may also be difficult to determine which documents will be relevant to

an action until relatively late in the proceedings.

Access: Directors should also be assured they will have sufficient access to those documents if and when required.

The *Act* provides directors with the right to access the "books" of a company whilst a director, and for a period of seven years after ceasing to be a director, for the purpose of pursuing or defending legal proceedings. "Books" are defined generally to include a register and any other record, information or document. The types of company documents that a director is entitled to access are far broader than those a company is required to store.

Even if the statutory definition of "books" is broad enough to cover the documents to which a director may require access, we recommend that the parties consider whether the Deed of Indemnity, Insurance and Access should extend the statutory rights of access by providing that:

- * the company allow a reasonable number of the director's advisors access to company documents; and
- * the director (or their advisors) be entitled to access all "Board Papers" retained by the company for such period as the company still has them, not just for the statutory period after the person ceased to be a director.



Conclusion

The rights of indemnity and access for directors contained in company constitutions and in the *Act* may not provide directors with the degree of protection they now require, and it may be appropriate to put in place a well-drafted Deed of Indemnity, Insurance and Access to supplement these rights. We have experience in advising on, negotiating and drafting these types of deeds.

Please contact us if you would like to discuss any aspect of this important issue for directors and officers.

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