

The delicate science of compliance

BY MICHAEL LEA

For companies that do business internationally, a global directors' and officers' liability coverage may once have provided its risk managers with a neat solution. In today's more demanding environment, when businesses are keen to establish a presence in the world's emerging economies but corporate decisions are subject to much keener scrutiny, a global D&O policy is beginning to present more problems than solutions.

What is the reason? A combination of factors, with differing local jurisdictions and the idiosyncrasies of the law in a number of countries, is at the heart of many of them. In the Nordic regions, it is by no means the norm for companies to offer to indemnify their directors against alleged wrongful acts. So a D&O policy for

this region cannot be written with the assumption that indemnification will take place.

In France, insurers are not able to write D&O on its usual 'claims made' basis and must instead offer something akin to a 'losses occurring' coverage. In Italy, costs must be in addition to the limit of indemnity instead of being part of it, with a similar requirement imposed in Israel.

Changes to Romania's corporate law late last year made it compulsory for companies to purchase D&O insurance, including subsidiaries incorporated in Romania and firms with a non-Romanian parent, and other Eastern European countries are likely to follow its lead.

And in the five years since Sarbanes-Oxley was enacted in the US, there is a worldwide trend to codify what exactly a director's duties are, which in turn will increase the level of exposure to lawsuits, and determine the level and breadth of insurance deemed appropriate for directors to carry.

The heart of the matter

The debate on whether D&O policies comply with this mounting list of differing requirements has generated more heat than light. What's more, it has tended to obscure the main purpose of a D&O policy, which is to ensure that the cover is fully responsive to the needs of the company directors and senior management that it protects and addresses the duties imposed upon them by local law.

This remains the most vital issue – how does your company continue to attract and retain the best candidates in countries where they may suspect that a global D&O cover is no longer adequate? Take Brazil as an example. Since directors' duties were codified in 2004, individuals have become keenly aware of their potential exposures at law. So they will demand to know what level of indemnification

their company provides and how the D&O policy will respond in the event of a claim.

However, other issues have intervened, such as those of local regulation and admitted versus non-admitted carriers, which some have taken to be more important. They have certainly acted as obstacles to the concept of a global policy provided by a single insurer. In Latin America, China and India, the law maintains that the insured cannot have the benefit of payment from a non-admitted carrier in the region. Cover must either be reinsured through a local admitted carrier or provided by the local market. Brazil insists that a D&O policy cannot provide indemnification unless cover is provided by the local market and reinsured by the state-owned IRB Brasil Resseguros.

So a worldwide cover provided by a global carrier may involve having 10 or even 20 different policies, many of them tied in with local reinsurers. Only a handful of major insurers – AIG, ACE, Allianz, Chubb, Zurich and Lloyd's – have a comprehensive network of local companies worldwide that they can use as admitted carriers, without recourse to other insurers.

The issue of taxation can also be problematic. A global D&O policy providing indemnification for directors in Australia or Canada, for example, will provoke questions from the tax authorities on the proportion of the overall premium applicable to that country and the tax payable on it. Accurately quantifying the exposure in these countries may not be easy.

The right approach

The D&O market has devised some solutions to these problems of compliance. AIG last year launched its Passport product, under which local policies are tied in with the limit applying to the global policy. More recently, ►►

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Zurich has introduced a master insurance programme that assesses the company's D&O exposure in each territory that it operates in, writes locally compliant policies and administers tax for each jurisdiction.

Other approaches, such as the Global Liberalisation Endorsement used by US carriers and the Difference In Conditions Endorsement that adjusts the policy coverage to comply with lo-

cal law, provide less than satisfactory solutions as they don't adequately address the issues of admitted paper or premium tax.

The best approach is one steered by common sense, with companies deciding where in the world payments under a global policy might breach local jurisdiction and where the risk of non-compliance is greatest – and ensuring that local policies are issued in those countries.

However, we would caution against placing the need for compliance over that of meeting the needs of senior management. ■

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