



Seeking cover under pressure

A guide to Investigations Costs cover

Over the past decade, Australia has seen a significant increase in the pace and scale of regulatory investigations and enforcement activity, as well as other high-profile inquiries and royal commissions into potential wrongdoing by institutions, companies and their directors and officers. Investigation Costs cover – most commonly available in Directors' and Officers' Liability (**D&O**) Policies and Professional Indemnity (**PI**) Policies – has increasingly been called upon to cover the substantial costs that can be incurred.

Despite the widespread availability of Investigation Costs cover, it is our experience that many policyholders remain unfamiliar with its scope and application. Furthermore, the practical complexities that are often faced in successfully pursuing claims for Investigation Costs can present additional challenges in the already highly-pressured and fast-paced environment created by a large-scale inquiry or investigation.

We routinely assist clients in their pursuit of Investigation Costs. We summarise below the key things that you need to know when 'seeking cover under pressure'.

Investigation Costs: what you need to know

The cover offered under D&O and PI Policies varies across the market - both between insurers and over time – including for Investigation Costs. While it is not possible to provide specific guidance that is applicable to every individual insurance policy, this type of cover generally has similar key features. On this basis, we set out below some of the key questions you should consider in pursuing a claim for Investigation Costs cover under your Policy.

WHEN IS INVESTIGATION COSTS COVER REQUIRED?

Under conventional D&O and PI Policies, cover is only enlivened when a 'Claim' is made – either against the Company (under PI Policies or under D&O Policies in limited circumstances, such as a Securities Claim), or against one or more of its directors, officers or employees. In this context, a Claim is generally defined to include *'any writ, summons, subpoena, complaint, application or other originating legal or arbitral proceedings'*, as well as any *'prosecution against an Insured Person'*.

In the setting of investigations and inquiries, however, formal proceedings or charges can take years to materialise (if they do at all), with an extensive lead-up period of compulsory notices, examinations and requests for information. The trigger for Investigation Costs cover is therefore different, being the commencement of an 'Investigation' (rather than a 'Claim').

An overview of how Investigation Costs cover sits within the broader landscape of policy coverage is set out in the following table:

WHO IS THE INVESTIGATION DIRECTED TOWARDS?

WHAT STAGE IS THE PROCEEDING AT?	Individuals	The Company
Formal proceedings or charges	<p>Formal proceedings or charges will typically fall within the definition of a 'Claim'.</p> <p>Under D&O Policies, if the director or officer is party to a Deed of Indemnity with the Company, or is otherwise protected under the Company's Constitution, then Side B cover will generally respond (subject to Policy terms).</p> <p>Practically speaking, the way this operates is that the insured individual - upon incurring costs or liabilities - calls upon the indemnity under their Deed of Indemnity with the Company. The Company indemnifies the individual, and then seeks reimbursement from the Insurer.</p> <p>If the Company is insolvent, or otherwise incapable of indemnifying the director or officer, Side A of the Company's D&O Policy will generally respond instead.</p> <p>PI Policies commonly cover employees, and in some cases, D&O Policies may also.</p>	<p>Under PI Policies, the Company may be covered for Defence Costs if the proceeding relates to alleged wrongdoing in the provision of professional services.</p> <p>Otherwise, under D&O Policies, Companies are not typically covered for claims made against them, except in limited situations. These include:</p> <ul style="list-style-type: none"> ■ where a D&O Policy includes Side C cover – but only in respect of a 'Securities Claim' made against the Company; or ■ subject to the terms of the Policy, where the Company and its directors or officers are both defendants to the same proceeding – especially where they retain the same legal representation – and the Company incurs Defence Costs that were also <i>necessarily incurred</i> for the benefit of the insured individuals (Joint Defence Costs).
Investigation phase	<p>Defence Costs incurred during the investigation phase of a proceeding are not generally covered under standard D&O or PI Policies, as there is no 'Claim' (as typically defined).</p> <p>However, if the Policy has Investigations Costs cover, then once a director, officer or employee is identified in writing by an authority as a subject of its investigation – or receives a notice compelling them to attend an examination – the Policy will generally respond to cover their costs in responding to that investigation.</p> <p>In most cases, Investigations Costs cover will not extend to informal or internal investigations carried out voluntarily (subject to any Pre-Investigation Costs cover). For example, where a regulatory authority requests a director's cooperation with an inquiry (but the director is not legally compelled to do so), then Investigation Costs cover will not usually be triggered.</p>	<p>Under PI Policies with Investigation Costs cover, Company Defence Costs may be available if the investigation relates to the Company's provision of professional services or activities.</p> <p>In most other contexts, however, the Company will need to resort to its D&O Policy, which will not typically respond to the Company's own costs and expenses (even with Investigation Costs cover).</p> <p>Joint Defence Costs may be available, however, where the Company's expenses were also necessarily incurred for the benefit of insured individuals.</p>

IS COVER AVAILABLE?

IS THE INVESTIGATION OR INQUIRY COVERED UNDER THE POLICY?

For cover to arise, there will generally need to be an 'Investigation' as defined under the Policy. A typical definition of this term includes all forms of '*examinations, investigations, conferences, interviews, depositions, hearings, or enquiries*' that are conducted by an '*official body*', such as a regulator, governmental body or agency, or parliamentary or royal commission. An official body can also include agencies such as the Australian Federal Police.

Generally speaking, an Investigation needs to be 'formal' or 'official' to attract cover. Internal investigations, routine inspections or compliance examinations, or the voluntary provision of information or documents to a regulator (even in response to a request from a regulator for assistance), will typically fall outside the scope of cover. A key trigger is generally the fact that the Insured has been compelled to participate in some way.

In some cases, cover may be available for Investigation Costs that are incurred during the 'pre-investigation' stage. If available, this may include cover for internal investigations that you have been requested (but not compelled) by a regulator to undertake, after you have notified an actual or suspected breach of duty. However, in our experience, this cover is non-standard and generally offered as an extension. Such cover may also be subject to separate conditions and sub-limits of liability.

COSTS INCURRED BY THE COMPANY

Under D&O Policies, it is very rare that a Company has any cover for the costs it incurs in responding to an investigation into its own affairs.

In most cases, the D&O Policy only provides cover for costs and liabilities that are incurred by: (i) directors and officers, or sometimes employees; or (ii) the Company where it is liable to reimburse those persons (such as under Deeds of Indemnity entered into between the Company and an Insured Person, or under the terms of the Company's Constitution).

In addition, however, if the Company and its directors or officers are both 'persons of interest' in the same investigation, or defendants to the same proceeding, the Company may be able to recover for the legal costs and expenses that it incurs for work carried out for the benefit of the insured individuals (especially where both parties have retained the same legal representation). It is generally a requirement that the relevant work was necessarily incurred in the defence of the director or officer (in the sense that it would not have been incurred 'but for' the involvement of the insured individual).

Unlike D&O Policies, PI Policies that provide Investigation Costs cover will cover Investigation Costs incurred by the insured Company or entity if the investigation relates to the Company or entity's provision of professional services or activities.

IS COVER TRIGGERED AT THIS STAGE IN THE INVESTIGATION?

Generally speaking, Investigation Costs cover will not be available until one or more of the following events takes place:

- the Investigation compels the attendance of a director, officer or insured employee at an examination;
- a director, officer or insured employee is identified in writing by the body conducting the Investigation as a 'target'; or
- an allegation of a breach of legal duty is made against a director, officer or insured employee.

This position may be different if your policy has additional Pre-Investigation Costs cover (although such cover is often subject to separate conditions and sub-limits of liability).

QUICK TIP

With complex investigations, it can take Insurers some time to determine indemnity, consent to the retainer of legal representation and agree upon the hourly rates that it will reimburse. In these fast-moving investigations, you may need to begin incurring costs before the Insurer has communicated its position on these issues. It is important to maintain a dialogue with the Insurer in these circumstances. Where an Insured incurs costs without the Insurer's consent, there may be some protection afforded by s 54 of the *Insurance Contracts Act 1985* (Cth) such that the Insurer can only deny indemnity to the extent that it is prejudiced by this omission.

HAS THE INSURER BEEN PROPERLY NOTIFIED AND UPDATED?

Standard D&O and PI Policies are issued on a 'claims made and notified' basis, meaning that the relevant policy period is the one in which the claim or investigation of the Insured is first notified. For this reason, it is important that you notify the Insurer promptly upon receipt of a Claim or Investigation (or upon becoming aware of circumstances that might give rise to a Claim or Investigation).

Following notification, it is also important that you regularly update the Insurer on any material developments in the Investigation.

Insurers will generally issue requests for information (**RFIs**) and require the provision of written answers and/or documentary evidence before they agree to indemnify you

or advance Investigation Costs. Sometimes the extent of the information sought by the Insurer can be contentious, but this is often resolved by way of a dialogue with the Insurer or its representatives. Providing prompt and adequate responses to these RFIs can help policyholders to secure indemnity sooner.

QUICK TIP

Depending on the nature of any RFIs issued by the Insurer, and the Insurer's position on indemnity, your responses may risk waiving legal professional privilege. Especially in circumstances where the Insurer has not admitted indemnity, you may want to consider withholding certain items or negotiating an appropriate confidentiality regime with the Insurer in an effort to reduce this risk.

IS COVER EXCLUDED?

Cover under D&O and PI Policies invariably contains exclusions. A common feature of these exclusions is the nature of the alleged conduct, with exclusions typically applying to certain types of serious wrongdoing (if admitted or established by final adjudication). Routine exclusions to be aware of in the context of Investigations Costs cover include:

- **Dishonest or fraudulent conduct:** As a general rule, Policies exclude from the Insurer's liability costs arising from dishonest or fraudulent conduct (once this has been admitted or determined by the courts in a final, non-appealable decision). Unless there is an admission of wrongdoing, this exclusion will generally not apply during the Investigation phase. It is worth bearing in mind, however, that Investigation Costs advanced to directors or officers may need to be repaid if dishonest or fraudulent conduct is ultimately established.
- **Prior circumstances:** Cover is also commonly excluded in circumstances where a policyholder had knowledge of an Investigation, or of matters that could give rise to an Investigation, before taking out the relevant policy and failed to notify the insurer.

KEY TAKEAWAY

You should carefully examine your Policy wording and consider whether any exclusions may apply. Even if serious misconduct is alleged, directors, officers and insured employees are usually entitled to representation costs to defend themselves and seek to prove their innocence. You should, however, be mindful that such monies may need to be repaid if the allegations are ultimately established.

WHICH COSTS ARE COVERED?

D&O and PI Policies typically require that Investigation Costs are 'reasonable' and incurred with the Insurer's prior written consent. Usually, however, this consent cannot unreasonably be withheld and, with proper consultation, the Insurer will need to indemnify you for all reasonable fees, costs and expenses.

PRIOR CONSENT AND REASONABLE COSTS

Your Policy is likely to require you to obtain your Insurer's consent before incurring Defence Costs (including Investigation Costs), and to limit your recovery to 'reasonable costs'. What is 'reasonable' in the circumstances is frequently a point of contention between policyholders and Insurers.

In our experience, Insurers often seek to rely upon their own Litigation Management or Defence Costs Guidelines in determining what they regard as reasonable, including with respect to:

- charge-out rates for solicitors and counsel at different levels of seniority; and
- categories of costs and disbursements (eg, research tasks, internal discussions and the number of lawyers present at a hearing or in a meeting).

There is often scope for negotiation with your Insurer on the application of these Guidelines. You should be aware of the importance of balancing any consideration of the Guidelines with ensuring that you have access to the best possible representation in relation to the Investigation and any subsequent proceeding.

KEY TAKEAWAY

The meaning of 'reasonable costs' is generally not defined in insurance policies and Insurers' Guidelines are unlikely to have legal force. For this reason, there is generally scope for negotiation on these matters and these issues are usually resolved by way of dialogue with the Insurer.

ASSOCIATED COSTS

Many D&O and PI Policies also cover 'associated costs' incurred in relation to Investigations. These can include reasonable legal costs incurred to:

- commence legal proceedings to overturn orders that disqualify a director, officer or insured employee from their job;
- challenge the power of an investigative body; or
- hire a public relations firm to mitigate any negative media arising from an Investigation.

You should carefully review your Policies to determine if any associated costs cover is available.

HOW CAN WE HELP?

We can assist you by:

- advising on the scope of your Investigations Costs cover and the application of any Policy exclusions;
- assisting you with notifying your Insurer, providing timely updates on the claim and responding to information requests;
- helping you to develop your claim strategy to maximise recoveries and advancement of costs, as early as possible;
- assisting you with Insurer engagement to help progress the claim and avoid potential disputes over which costs are covered; and
- representing you in relation to any coverage disputes that arise.

Who to speak to



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