

Insurance law update

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CASE NOTE

Victorian Court of Appeal characterises role of executive directors

In the [recent decision](#) of *AIG Australia Limited v Jaques* [2014] VSCA 332, the Court of Appeal of the Supreme Court of Victoria discussed the definitions of non-executive and executive directors in the context of policy interpretation.

FACTS

AIG Australia Limited ('**AIG**') issued an Investment Management Insurance Policy ('**the policy**') to the Australian Property Custodian Holdings Limited ('**Holdings**'). Mr Jaques was a director of Holdings.

The policy insured all executive directors for losses up to \$5 million, in the aggregate. Relevantly, non-executive directors were entitled to a further \$1 million in cover.

Mr Jaques notified AIG of claims made against him for wrongful managerial acts and sought the additional \$1 million in cover on the basis that he was a non-executive director. Mr Jaques, who was a director of Holdings from 1 March 2001 until 6 July 2011, contended that he first became an executive director on 26 June 2007, when he was formally appointed by the board of Holdings.

Although AIG accepted that Mr Jaques was a non-executive director until 6 April 2004, it denied the claim in circumstances where the alleged wrongful managerial acts were said to have occurred on various dates in 2006, 2007, and 2008.

AT FIRST INSTANCE

In finding that Mr Jaques was a non-executive director at the time of his wrongful managerial acts, Dixon J made the following observations:

- » The policy definition of non-executive director was '*not helpful*'.
- » The essential characteristic of an executive director is their discharge of executive functions in the management and administration of a company. This is a question of fact, that is, there must be evidence that the company has delegated executive function to that director.
- » The trial judge found that there was no 'explicit act' of Holdings that evidenced a delegation of power to Mr Jaques to operate as an executive director until his appointment on 26 June 2007.

ON APPEAL

AIG appealed the decision at first instance alleging that the trial judge erred in failing to find that Mr Jaques ceased to be a non-executive director on 6 April 2004. In short, AIG submitted that:

- » Critical to this characterisation is whether the director represented themselves to the investing public, and whether they were regarded internally, as an executive director.
- » A proper interpretation of the policy required that a non-executive director should be defined by reference to all of the relevant facts.
- » Based on the facts, Mr Jaques did not fall within the definition of a non-executive director during the relevant period under the policy.

In support of its position, AIG pointed to the following evidence:

- » Directors' meeting minutes which referred to Mr Jaques as an executive director.
- » The Corporate Directory in a Product Disclosure Statement which referred to Mr Jaques as an executive director and which was signed by Mr Jaques in his capacity as an executive director.
- » Mr Jaques' functions did not change upon his appointment as an executive director on 26 June 2007.
- » Mr Jaques' apparent belief that he was an executive director in April 2004.
- » Correspondence from Mr Jaques to potential acquisitions was sent on Holdings letterhead and signed 'general manager', representing that he was a Holdings executive.

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The Court of Appeal unanimously dismissed AIG's appeal. In doing so, the Court of Appeal relevantly stated that:

- » The trial judge's definition of executive director was consistent both with authorities and the principle that a policy of insurance, as a commercial contract, should be given a businesslike interpretation.
- » In essence, the distinction between executive and non-executive directors is whether the director performs executive functions in the management and administration of the company.
- » The subjective views of investors, the board and the director themselves are of limited relevance in construing the terms of the policy.
- » In the absence of formal authority conferred upon a director by the company, a director should generally be treated as a non-executive director.
- » Mr Jacques was an employee whose duties were limited to the management of retirement villages, rather than the performance of the executive functions of Holdings.

IMPLICATIONS

This decision provides a useful illustration of the court's approach in determining whether a director is a non-executive director under a policy. In the absence of a substantive definition in the policy, this is a question of fact.

The substance of a director's functions is critical to this question. If a director does not perform the organisational activities of an executive director, the court will not characterise them as an executive director, for the purposes of a policy, merely because they have been held out as such to investors and the public.

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