AIS Liaison
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Avoiding legal landmines with D&O cover

Class actions against listed corporations may capture the spotlight when it comes to court cases targeting companies, but directors and managers at smaller businesses can't be complacent about potential legal landmines.

In an increasingly litigious environment, and as regulators hone their focus on corporate culture, there are many areas where directors and officers may find themselves financially exposed if they haven't taken steps to lock in protection.

Research in Australia and internationally suggests directors' and officers' insurance policies have a higher penetration among large-scale companies but are often overlooked at the smaller end of the market, particularly among micro-enterprises.

AIG in the UK found SME decision-makers often lack knowledge about where and how easily management liability might arise and also about the nature of the D&O product and what it covers, leaving themselves unnecessarily exposed.

SMEs can easily become the target of legal actions. Customers, suppliers and employees are just as aware of their rights whether the business is large or small, and Australian regulators are increasingly active across the financial services spectrum.

Often company owners and directors believe their individual risks will be covered through other parts of the enterprise's insurance package, when that is not necessarily the case.

Professional indemnity insurance covers activities of the business, whereas management liability policies, which include directors' and officers' cover, provide protection where third parties claim for losses due to mismanagement.


Court drama: small businesses are increasingly exposed to litigation

The managers and directors of an SME can individually face claims for actions alleging fraud or breach of fiduciary duty, intellectual property breaches, engaging in unfair competition, defamation and accusations of other illegal conduct.

A typical D&O policy will cover representation costs, such as when a person must attend an inquiry, legal expenses in defending a claim and compensation paid to resolve an issue.

The number of D&O claims pursued has increased in the past decade as the environment favours greater "activism" by customers. There are also rising demands for individuals to be held responsible for actions in a push for accountability standards that limit the potential to shelter behind a corporate entity.

A number of reviews and changes are currently underway that underline the regulatory focus on financial services culture and improving customer outcomes, and which potentially flag a more interventionist approach.

SMEs often put a strong focus on making sure insurance policies are in place for property, fire and business interruption. Directors' and officers' cover is also an important area to address and it's well worth reviewing the options with us.

If you make or sell it, you can be liable

Prams, sunglasses, motorcycles, squeaking pig toys and wine had something in common last year – they were all products recalled from the market after problems were discovered.

The cases mark just the tip of the iceberg, with recalls escalating over the past decade as suppliers look offshore, consumers become more aware and regulators are quick to take action.

Recall incidents rose to 612 in 2016 from 388 in 2006, the Australian Competition and Consumer Commission (ACCC) product safety website shows.

By mid-December, recalls last year had reached 573, with transport representing the largest category, followed by health and lifestyle goods, items for babies and kids and food and grocery products.

The database highlights that almost no area is unaffected, with categories also covering home and living, electronics and technology, outdoor, clothing and accessories, gas and industrial business and building.

High profile cases that attracted media attention included the 2015 Nanna's frozen mixed berries recall due to a potential Hepatitis A contamination. More recently, Takata airbag defects were discovered that could put vehicle passengers in danger from metallic projectile fragments.

Food Standards Australia New Zealand data shows that food recalls in the past few years have jumped above the decade average. Allergens are the most common reason, particularly due to the undeclared presence of a dairy product or peanuts.

But what about if you just sell the goods? Under Australian Consumer Law a supplier can be liable whether they make and market goods using their own brand, import the products or allow another party to market the items.

Potential costs can be high if something goes wrong, including the expense of withdrawing products, notifying consumers and fixing the problem, while social media has raised the reputational fallout risks.

The ACCC warns a recall can become even more costly and time-consuming if it's not completed successfully initially, highlighting the importance of having risk and response strategies in place.

A recall system should suit the specific products an enterprise supplies and consider the degree of risk they may pose to consumers. The purchase of product recall or product contamination insurance is a key part of the process, whether a business is large or small.

The regulator also recommends identifying ways of reaching customers, including by referring to databases, online registrations and warranty cards and says it is important to keep details of suppliers.

Available insurance can cover recall expenses, business interruption and loss of profits, while crisis management assistance is an option to help contain the impact.

Costs from a recall can quickly escalate and take a business into uncharted territory. It can be a stressful experience and it's worth talking with us to gain advice about the most suitable insurance protection. Call us anytime – we're your insurance broker and we're here to keep you out of trouble!

Defective: Takata airbags are one of many products to have been recalled

Disturbing trend: employee fraud is on the rise

Staying ahead of fraudsters

It's important to trust your employees, but it's equally important to be prepared for the day when one of them lets you down.

Employee fraud is big business, and getting bigger all the time.

Between April and September 2016, 143 frauds took place in Australia, with a total value of $442 million, according to KPMG's fraud barometer. This compares with 116 frauds with a value of $381.1 million for the previous six-month period.

The most common perpetrators are 'business insiders', with employees and management accounting for more than half of all reported frauds.

Some 22% of frauds were facilitated through the use of technology, and male fraudsters are responsible for more than two-thirds of them.

Most perpetrators were aged 46–55, and more than one in every 12 frauds committed had gambling or drugs as a motivation.

Detection is taking too long – 40% of frauds in Australia take place over a five-year period before being discovered.

And if you think it's just the big firms at risk and SMEs are immune, think again.

In many ways SMEs are more open to fraud, as fewer formal structures tend to be in place giving more opportunities to potentially deceitful employees.

The impact can be devastating. KPMG's report puts the average value of each fraud at $3.1 million.

But here's the good news – insurance cover is available to give you peace of mind should the worst happen.

Fidelity insurance reimburses the insured for a loss directly resulting from dishonest acts of their employees.

The insurance covers a direct financial loss, not a consequential one, so in other words the loss should be of money or goods of the insured.

The dishonest act should be committed in the course of the worker's duties, and must be committed by an employee, with sufficient evidence to prove it.

Purchasing fidelity insurance makes sense, but it's equally important to ensure systems and processes are in place to reduce the likelihood of fraud taking place.

While it isn't nice to think the worst of people, especially those who have been close and valued colleagues for many years, the reality is that employee fraud happens, and often when we least expect it.

When the future of your business is at stake, it pays to put aside emotions and think practically.

Don't forget that policies have varying clauses and exclusions and coverage may differ.

So speak to us to make sure you get the cover you need.

Preparation is key to claims prevention

Taking action to prevent five of the most common small business claims is likely to be time well spent as a busy year lies ahead.

Identifying and tackling common issues offers easy opportunities to limit risks and to show a pro-active track record that can be rewarded when it comes to purchasing and renewing insurance.

Theft and burglary typically top the list of claims lodged by SMEs, highlighting the importance of installing good security systems – and making sure they are correctly used and understood by everyone in the business.

Beware: theft and burglary top the list of SME claims

Lighting that limits the chance for intruders to sneak into properties unseen provides a deterrent, while strong locks on windows and doors also eliminates easy opportunities for thieves.

Storm damage is another major source of claims for businesses, which face varying levels of risks according to their locations in cities and towns across the country.

Where applicable, trimming overhanging trees and clearing drains and gutters can reduce risks from falling branches and debris, while the threat from gale-force winds can also be limited by keeping an eye on weather forecasts and securing outdoor furniture and equipment ahead of storms.

Businesses should prepare for the possibility of extended power outages and consider how that may affect their operations and steps they can take. It's an area where business interruption cover really comes into play.

Accidental or malicious property damage represents the third most common source of claims, according to a recent review of business pack claims data.

As with burglary and theft, it's important to secure the premises and make sure there are no easy temptations for vandals and the risk of unexpected damage is reduced.

Machinery and equipment breakdown is another common problem area and can have a significant impact on expenses and profits.

A schedule for regular checks and maintenance will help keep equipment running smoothly and any minor problems should be attended to and worn parts replaced before bigger issues emerge.

Employees should be trained so equipment and machinery are used as intended, without operating at over-capacity or in unfavourable environmental conditions. Machinery vital to a business should be stored in ways that minimise the chance of problems.

Liability risks are often overlooked by SMEs, but round out the top five claims areas for small business. This type of claim can be complex and difficult.

Keeping walkways and floors dry and clear of tripping hazards can reduce the risks, while adequate lighting, particularly on stairs, helps prevent accidents. Access should be restricted to areas where hazardous equipment may be operating, while clear systems can ensure clients' property is handled with care.

Many risks can be averted, and considering steps to prevent common problems pays dividends. It is an effective part of a wider risk-management approach that you can discuss with us. As your insurance broker, it's our job to keep you and your business safe.

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