Trustee Liability Insurance - Do You Get What You Paid For?

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Rathbone Brothers PLC & Anor v Novae Corporate Underwriting Limited & Ors [2014] EWCA Civ 1464

In this case, which will be of interest to all professional trustees and their employers, the English Court of Appeal examined the insurance and indemnity arrangements in place for a Jersey trust company business, and in particular:

(a) The extent to which the trust company's insurance policy covered its employees and consultants who were acting as personal trustees (Coverage Dispute);

(b) The extent to which an indemnity given to an employee or consultant had to be exhausted before the insurance policy could be required to pay out (Excess Clause Dispute); and

(c) The extent to which, if the insurance policy had to pay out first, the insurance company could recoup that payment from the trust company by being subrogated to any right of indemnity the employee/consultant had against his employer (Subrogation Dispute).

Facts

This case concerned the insurance cover that might be available to a trustee who was being sued by certain beneficiaries for breach of trust arising from alleged poor investment decisions. One of the trustees was Paul Egerton-Vernon (PEV), who was an employee of, and subsequently a consultant to, Rathbones Trust Company Jersey Limited (RTCJL). PEV was therefore being sued personally.

PEV had the benefit of an indemnity from both RTCJL and its parent company, Rathbone Brothers plc (PLC) (Indemnity). This provided that they would indemnify him, and be jointly and severally

liable, for liabilities arising from the performance of his services, excluding liabilities arising from fraud or wilful misconduct. There was a limit of £40 million in respect of each event giving rise to any liabilities.

For the relevant year of account, PLC had purchased £50 million of professional indemnity insurance (PII) on behalf of the Rathbones group (including RTCJL), including annual civil liability, Directors and Officers' and financial crime insurance. The Group's trust-related activities, including the provision of professional trustees by RTCJL, were fully set out in the renewal submission.

Coverage Dispute

The arguments

The various excess insurers disputed that there was coverage under the PII policy, alleging that:

(a) PEV was not "a paid employee … working under the direct control or supervision of an insured company", and was therefore not an "insured person" for the purposes of the policy; and

(b) The personal trustee services provided by PEV did not fall within the "professional services" covered by the civil liability policy, which were defined as "the financial services declared in the submission performed by or on behalf of an insured company pursuant to an agreement with a third party: (i) for compensation; or (ii) in conjunction with services for compensation"

Among other things, the insurers argued that:

- When PEV was acting as a personal trustee, he was not under the "direct supervision and control" of RTCJL as he had to exercise his own judgment and take personal responsibility for his actions and RTCJL could not direct how he should carry out his duties;
- In any event, after PEV became a consultant he could no longer be described as a "paid employee";
- The provision of personal trustee services by PEV was neither "by or on behalf of" RTCJL, nor was PEV acting pursuant to "an agreement with a third party" because, it was argued, the only agreements envisaged in the clause were those to which the insured company itself was a party; whereas in this case PEV was acting pursuant to an agreement he had entered personally.

The Court of Appeal Decision

The Court of Appeal rejected the excess insurers' arguments, holding that:

- It would be an extraordinary limitation on the cover provided by the policy if, when exercising

their role as trustees, paid employees were not covered. The provision of trustee services was fully disclosed in the submission to insurers, was a major part of the business, and was one of the principal reasons for seeking professional indemnity insurance of this kind. There could be no doubt that the insurers were undertaking to cover liabilities resulting from the exercise of these functions, notwithstanding that the employer could not directly control their exercise, and the concept of "control or supervision" should be construed accordingly.

- In any event, the Court of Appeal found that the supervision requirement was satisfied: the role of personal trustee is highly regulated under Jersey law and RTCJL exercised detailed supervision over PEV's activities in accordance with the Code of Practice whose purpose is to ensure that trustees comply with the rules laid down by the Jersey Financial Services Commission.
- As regards the position once PEV became a consultant, the Court of Appeal held that although he did not fall within the common law concept of employee he was nevertheless a "paid employee" for the purposes of the insurance policy because he was not remunerated on a sale or commission basis but was employed to act for the company, was subject to its control or supervision, and was remunerated by salary. The Court of Appeal further noted that this was a perfectly normal commercial use of the term and that the Jersey Regulations describe a trust company business employee as "a person employed either under a contract of service or a contract for services by the registered person to assist in the provision of trust company business".
- As to whether PEV's personal trustee services were provided "by or on behalf of Rathbones", the Court of Appeal held that this concept should be construed so as to achieve commercial common sense, and that it was quite natural to speak of someone who is performing services at the request of an employer as doing so "on his behalf". The provision of personal trustees is commonplace in Jersey and was a significant part of the business which was identified in the submission to insurers. It was the justifiable understanding that such functions would be covered by the policy, and it would require very clear words to exclude them.
- There was no reason to limit the policy to cover only agreements to which the insured company itself was a party. Here, the service was provided for the benefit of RTCJL and on its behalf. RTCJL was potentially liable if there was negligence by PEV, and would in any event wish to protect the person acting for their benefit. It was therefore perfectly sensible for the policy to apply in such a situation.

Excess Clause Dispute

The arguments

Clause 5.14 of the PII policy provided that: "Insurance provided by this policy applies excess over insurance and indemnification available from any other source".

The insurers submitted that this allowed them to refuse to pay out on the policy until PEV had exhausted his claims under the Indemnity. Alternatively, they claimed that there were certain Directors and Officers policies (D&O) which also provided cover and had to be exhausted first.

The Court of Appeal Decision

The Court of Appeal rejected the insurers' arguments:

- The Court of Appeal held that employers frequently give indemnities to directors and employees for liability arising out of negligent conduct. A major reason for taking out such insurance is to protect against the risks of incurring liability as a consequence of such negligence. It would have frustrated the purpose of professional indemnity insurance to interpret the policy so as to exclude the insurers from liability in the very circumstances where that insurance is most likely to be needed. It would therefore require very clear language (which was not present here) to treat the indemnity granted by the insured company to be the primary source of cover ahead of the insurance for which the insured company has paid.
- As regards the D&O policy: there was a "professional services" exclusion which plainly covered the liability in this case, and as the liability itself was therefore not covered by this policy there was also no coverage for defence costs under the D&O policy.

Subrogation Dispute

An insurer who has fully indemnified an insured against a loss covered by a contract of insurance between them may ordinarily enforce, in the insurer's own name, any right of recourse available to the insured. This is known as a right of subrogation, and it can be excluded either:

(a) where there is a waiver in the insurance policy itself, or

(b) where the terms of an underlying contract between the insured and the third party (against whom there would otherwise be a right of recourse) the strip subrogation right of any substance and thus preclude its exercise.

In this case, the Court of Appeal found that there was no express waiver in the policy with respect to the Indemnity. However, the majority of the Court of Appeal found that the Court should imply a term that the insurers would not seek to be subrogated to PEV's rights under the Indemnity, as it could not have been the intention of the parties that the insurers should be able to enforce rights of indemnity against a co-insured (PLC) where that co-insured was indemnifying the very same risk as the insurers. To hold otherwise would be to deny PLC the very benefit which the policy was intended to confer, and defeat the purpose for which they had paid the premiums.

In any event, the Court of Appeal also held unanimously that one could readily imply a term into the Indemnity contract to the effect that it was intended to provide supplemental protection only

once the claim against the insurance company had been exhausted. In this way, any right of subrogation would be stripped of substance as the Indemnity could not have been enforced once the insurance policy had fully paid out.

Comments

Given that the insurance arrangements of Channel Island trust businesses are often governed by English law, the English Court of Appeal's decision will be welcomed by those acting as professional trustees or directors of corporate trustees, and their employers, who no doubt will view the decision as reflecting the commercial reality and purpose behind insurance and indemnity arrangements of this kind. The Court of Appeal was prepared to look to the intention of the parties and where necessary imply terms in order to avoid a commercially absurd result.

However, the case also serves as a reminder that, particularly where an underlying claim is of high value (as was the case here), insurers may seek to have the policy construed strictly and in accordance only with the words used in the contractual documentation. As was noted by the Court of Appeal, where experienced commercial parties have addressed an issue in a particular way in the contractual documents, the court should be very slow to conclude that they were not intending to do so. It therefore of course remains important to ensure that the wording of contracts of insurance and/or indemnity is clear and is tailored to the specific liabilities sought to be covered, as standard policy wordings may not adequately address all of the intricacies involved in the actual provision of trust services.

Regulatory information can be found under Legal Notice

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