

UPDATE

When are directors indemnified by a Company's Articles of Association?

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The Grand Court of the Cayman Islands has considered whether a director can rely on exoneration and indemnification provisions in a company's Articles of Association when there was no written contract between the company and the director incorporating those provisions into the terms of the director's appointment.

While the Grand Court accepted that in the specific facts of the case, the director was entitled to rely on the exoneration and indemnification provisions in the Articles, the judgment emphasises the desirability of avoiding uncertainty by expressly incorporating exoneration and indemnification provisions into the director's contractual terms.

Introduction

It is common practice for a company registered in the Cayman Islands to indemnify its directors against personal liability for any liability or loss they may suffer while acting as a director. While a company's Articles of Association (**Articles**) constitute a contract between the company and its shareholders, they do not automatically also constitute a binding contract between the company and its directors, even if they contain protective terms the directors would wish to rely on. Consequently, a separate written directors' service agreement is often entered into between the director and the company which may incorporate the provisions of the Articles into the director's appointment or include equivalent, exoneration and indemnification provisions.

In *Goodman v Cummings and DMS Governance Limited – Tangerine Investment Management Limited*¹, the Grand Court of the Cayman Islands confirmed that where the facts support such a finding, a director may rely on exoneration and indemnification provisions in the company's Articles even where they were not incorporated into a separate written director's service contract with the company.

The Facts

At the relevant time, Ms Cummings was employed by DMS Governance Limited (**DMS**), and was appointed as a director of Tangerine Investment Management Limited (**Tangerine**) in 2011. Tangerine acted as investment manager for funds established by Axiom for the purposes of providing loans to English law firms. Axiom collapsed in October 2012. Ms Cummings resigned as a director of Tangerine in October 2012. The Plaintiff, Mr

¹ Unreported, Cayman Grand Court FSD, 13 September 2018.

Goodman, acquired from Tangerine the right to bring certain claims, including breach of common law and fiduciary director duties claims against Ms Cummings, and a claim against DMS that it was vicariously liable for Ms Cummings' acts as a director of Tangerine.

Ms Cummings and DMS denied the allegations made against them and Ms Cummings asserted that she was entitled to rely upon the terms of various indemnity provisions in Tangerine's Articles which gave her defences to the Plaintiff's claims as well as separate rights of action against Tangerine. Ms Cummings did not have a separate written director's service contract with Tangerine. Her case was that her appointment was made expressly on the basis that the protections afforded by the Articles, including the indemnity provisions, were incorporated into the terms of her appointment as a director of Tangerine and that she was accordingly entitled to the benefit of them.

The Plaintiff disputed Ms Cummings' entitlement to rely on the indemnity provisions in the Articles.

The Issues before the Court

The parties agreed to deal with the central issues by way of preliminary determination at trial. The key issues, and the Grand Court's findings in relation to them, were as follows:

1. Were the Articles (and so the indemnity provisions in them) incorporated into Ms Cummings' appointment as a director of Tangerine?

Ms Cummings submitted evidence to show that when first approached to be a director of Tangerine – before its incorporation – she notified Tangerine's attorneys that she *assume[d] that the director(s) will be indemnified under the Memorandum and Articles of Association of the Company...* That assumption was not challenged in subsequent correspondence. Ms Cummings submitted that the indemnity provisions in the Articles had been incorporated into her director's contract with Tangerine.

The Plaintiff argued that the Articles did not form part of Ms Cummings' contract with Tangerine as a company's articles are not automatically incorporated into the contract between a director and the company.

The Court held that while the company's articles do not automatically form part of a director's contract with the company, Ms Cummings' unchallenged reference to her expectation that she would be entitled to the protection of the indemnity provisions in the Articles brought them into her contract with Tangerine. The Court said that where a director is employed by a company but does not have a separate engagement contract with it, it will not be difficult – a *comparatively low bar* – to satisfy the Court that the indemnity provisions in the Articles were incorporated into the director's contract with the company. The Court found that it was clear from the evidence that Ms Cummings only accepted her appointment as a director of Tangerine on the basis that she would have the protection of the indemnity provisions in the Articles while acting as a director.

2. Did the indemnity provisions in the Articles extend to former, rather than just current, directors?

Ms Cummings had resigned as a director of Tangerine by the time she had reason to rely on the indemnity provisions in the Articles. The Plaintiff argued that only current, and not former, directors, were entitled to rely on the indemnity provisions in the Articles because they were expressly limited to "*the directors, for the time being, of the Company*" and the Articles defined "*Directors*" as "*the directors for the time being of the Company*": both definitions necessarily excluded former directors of Tangerine. Ms Cummings argued that former directors were still "*Indemnified Persons*" under the Articles in respect of any civil action which arose in relation to her conduct as a director and that any other interpretation of the indemnity provisions would be bizarre and plainly not what was intended.

The Court held that it would resist any interpretation of the Articles which would lead to an odd or unreasonable outcome unless there was clear wording to support it. There was no such clear wording in the Articles. The Court also accepted that the Plaintiff's interpretation would effectively render the indemnity provision worthless in practical terms which cannot have been intended. The Court held that the phrase "*for the*

time being" must refer to the director's period of tenure whether past or current, so the indemnity provisions included former directors.

3. If Ms Cummings *was* entitled to rely on the indemnification provision in the Articles, was she also entitled to demand pre-payment of her legal fees involved in defending the Plaintiff's claim?

Article 154 required that "*Expenses incurred in defending any civil...action... for which indemnification is required pursuant to these Articles shall be paid by the Company*" and that the Company should pay those sums "*in advance of the final disposition of such action...*". The Plaintiff argued that even if the indemnification provisions were incorporated into Ms Cumming's contract with Tangerine, the pre-payment right only arose in relation to claims pursuant to these Articles so did not apply to claims to an indemnity pursuant to an implied contract which only incorporated the Articles.

The Court rejected this narrow interpretation of the indemnity provisions in the Articles – were the Articles intended to be so narrow, they could have been drafted to achieve that outcome. The Court also rejected the Plaintiff's argument that as the indemnity was only intended to ensure that Ms Cummings *shall never be called upon to pay* legal fees, it was a "hold harmless" clause rather than a true indemnity clause and so only gave rise to a claim for damages in the case of a breach rather than a claim to a debt. The Court held that the clause was intended to be an indemnity rather than a "hold harmless" clause, and Ms Cummings was entitled to rely on it.

Conclusion

Ms Cummings succeeded in her claim to be able to rely on the indemnity provisions in the Articles principally because she had made clear in the pre appointment correspondence that that was what she was expecting, and, inferentially, that she would not have accepted the appointment without that protection. The conventional view has always been that a director should be able to rely on the protective provisions in the articles on the basis that they were impliedly incorporated into the director's contract: this decision confirms that in appropriate factual circumstances, the Court will support that view, but each case will have to be considered on its own facts. Rather than running the risk of litigation, it will always be safer to expressly include indemnification and exoneration provisions in a bespoke director's service agreement to mirror the equivalent provisions in a company's Articles.

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