Browne Jacobson

D&O: Australian Courts consider the meaning of ‘personal advantage'

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The Federal Court of Australia grapples with the meaning of "personal advantage" in the context of an exclusion clause within a D&O policy.

In Hakea Holdings Pty Ltd v McGrath (No 2) [2022] FCA 995 the Federal Court of Australia recently had to consider the meaning of ‘any personal profit or advantage’ contained in an exclusion clause within a directors and officers (D&O) insurance policy.

Mr McGrath was the sole director and shareholder of Denham Constructions Pty Ltd (Denham). He was also a director of Hakea Holdings Pty Ltd (Hakea). Denham contracted with Hakea to design a care facility. The project was beset with delays due to Denham’s significant financial difficulties, which were never communicated to Hakea. Mr McGrath continued to represent that the project would be completed on time. Denham’s solvency issues eventually came to light and the company was wound up.

Hakea had taken out a D&O policy with Neon Underwriting Limited (Neon) which contained an exclusion for losses in connection with a claim in any way involving or in connection with a director gaining "any personal profit or advantage … to which he or she was not or is not legally entitled". The court at first instance had found that, in not disclosing the financial difficulties, Mr McGrath had gained an advantage by the construction contract continuing to remain in place.

Hakea appealed arguing that the "advantage" must be capable of being the subject of legal entitlement, such as money, ownership of property or a contractual right. The continuation of the contract could not have been an advantage to Mr McGrath as he was not a party to the contract. Hakea also argued that the first instance judge had ignored the words "to which he or she was not or is not legally entitled". In response, Neon argued that the clause was broadly worded and the advantage was the buildings contract, together with its associated revenue stream, remaining on foot when it would otherwise have been terminated by Hakea.

On appeal, the Federal Court judges found that the first instance judge had not erred in his findings. There was no need to confine the words "any personal … advantage" more narrowly than their ordinary and natural meaning. The words were capable of applying to any matter which makes the individual better off or improves their circumstances and it was sufficiently broad to encompass the avoidance of a negative commercial event, such as the risk of the cancellation of a contract. Keeping the contract on foot enabled Denham to earn a revenue stream that supplemented funds under Mr McGrath’s control which he used to pay his personal expenses. The judges found that a director obtaining a personal advantage in this way by breaching his duties as a director gained an advantage to which he was not legally entitled.

Another issue before the Federal Court was whether the claim had been properly notified within the policy period. On this issue, the judges found against insurers. It was sufficient that the claim had been sent to an active email address and it would be uncommercial to require that the email was opened and read in order to consider the claim had been properly notified.

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