

[GCG MEMORANDUM CIRCULAR NO. 2012-10 (RE-ISSUED)[1], December 05, 2012]

DIRECTORS' AND OFFICERS' LIABILITY INSURANCE (DOLI)

I. UNDERLYING STATE POLICY AND PRINCIPLES

1. GOGCs as Significant Tools for Economic Development

Section 2 (*Declaration of Policy*) of Republic Act No. 10149, officially designated as the "GOCC Governance Act of 2011" (R.A No. 10149), embodies the State's recognition of the potential of GOCCs to be "significant tools for economic development," and declares "the policy of the State to actively exercise its ownership rights in GOCCs and to promote growth by ensuring that operations are consistent with national development policies and programs."

2. GOCC Governing Boards Primarily Tasked with Control and Supervision of GOCCs

Towards achieving that State policy, Section 2 of the Act further mandates *inter alia* that "the State shall ensure that . . . [t]he [G]overning [B]oards of every GOCC and its subsidiaries are competent to carry out [their] functions, **fully accountable to the State as its fiduciary**, and act in the best interest of the State."^[2]

3. Directors/Trustees and Officers Are "Fiduciaries of the State"

By express declaration under Section 19 of R.A. No. 10149, the members of the Boards of Directors/Trustees and the Officers of GOCCs are designated as "**fiduciaries of the State**... [with] the legal obligation and duty to always act in the best interest of the GOCC, with utmost good faith in all its dealings with the property and monies of the GOCC."^[3]

Further, Section 20 of the Act provides that members of the Boards of Directors/Trustees and Officers of GOCCs occupy "*Trustee Relations to the Properties, Interests and Monies of the GOCC*."^[4]

4. Directors/Trustees and Officers Assume Fiduciary Duties of the Highest Level in Relation to the State and the GOCC

Section 19 of R.A. No. 10149 imposes at the highest levels, "to always act in the best interest of the GOCC, **with utmost good faith** in all [their] dealings with the property and monies of the GOCC," the following fiduciary duties and obligations on the members of the Board and Officers of covered GOCC:

- (a) "Act with **utmost and undivided loyalty to the GOCC**"^[5] (*Duty of Loyalty*);
- (b) "Act with due care, **extraordinary diligence, skill and good faith** in

- the conduct of the business of the GOCC”^[6] (*Duty of Diligence*);
- (c) Avoid conflicts of interest and declare any interest they may have in any particular matter before the Board^[7] (*Duty of Loyalty and Transparency*);
- (d) Apply sound business principles to ensure the financial soundness of the GOCC (*Duty of Competence*);^[8] and
- (e) Elect and/or employ only Officers who are fit and proper to hold such office with due regard to the qualifications, competence, experience and integrity^[9] (*Principle that “Management is primarily accountable to the Board”*).

Section 21 of the Act reiterates the standard of diligence required of Directors/ Trustees and Officers: “The members of the Board and Officers must exercise extraordinary diligence in the conduct of the business and in dealing with the properties of the GOCC. Such degree of diligence requires using the **utmost diligence of [a] very cautious person with due regard for all circumstances.**”^[10]

II. OBLIGATION AND AUTHORITY OF THE GOCC TO PROVIDE DOLI COVERAGE FOR DIRECTORS/TRUSTEES AND OFFICERS

Since the underlying principle of public corporate governance embodied in R.A. No 10149 is to the effect that “*The Governing Board of GOCCs is primarily accountable to the State and other Stakeholders, and the Management is primarily accountable to the Board,*” it has become imperative therefore that GOCCs provide the members of their Boards and their Officers, not only the necessary staff support to allow them to fulfill their role as fiduciaries of the State, but also insurance coverage under the commercially accepted term “**DIRECTORS’ AND OFFICERS’ LIABILITY INSURANCE**” (**DOLI**) to afford both the GOCC and the members of their Governing Boards and Officers the means to pursue their fiduciary duties and obligations “to always act in the best interest of the GOCC, with utmost good faith in all [their] dealings with the property and monies of the GOCC.”^[11]

The recognition of the obligation of GOCCs, as well as their authority, to provide DOLI for the members of the Governing Boards and Officers has been expressed under Section 31 of the **Code of Corporate Governance for GOCCs** promulgated by the Commission as GCG Memorandum Circular No. 2012-07, thus:

VI.

OBLIGATIONS OF THE GOCC TO DIRECTORS AND OFFICERS

Sec. 31. *Providing for Staff Support to Directors.* – Each GOCC shall provide the members of its Governing Board with reasonable support staff and office facilities to allow them to properly discharge their duties and responsibilities.

Sec. 32. *Obtaining of Directors and Officers Liability Insurance (DOLI).* – Having imposed the highest level of responsibility and accountability on the members of the Board and Officers, i.e., that of extraordinary diligence, it is equitable that when the GOCC itself and/or the members of the Board and Management are sued before tribunals on matters that are within the official functions and capacity and on matters where business judgment has been exercised in good faith, that there be proper

recovery of the costs of litigation and the judgment liability imposed. It is prudent measure therefore for every GOCC to obtain "Directors and Officers Liability Insurance" (DOLI) coverage for itself and the members of the Governing Board and Officers against contingent claims and liabilities that may arise from, as well as the expenses that may be incurred in prosecuting, the actions that may be filed against the GOCC arising from the actions of the Governing Board and/or Management that may cause loss or damage to third parties.

Nothing in this section shall be construed as to authorize the reimbursement or the incurring of costs, such as the payment of premiums on DOLI coverage, by the GOCC on the litigation expenses incurred and the judgment liability decreed against a Director or Officer for breach of any of his fiduciary duties or for fraud committed in the performance of his or her duties to the GOCC and/or its stakeholders.

III. INSTITUTION OF THE DOLI SYSTEM IN THE GOCC SECTOR

5. Meaning and Legal Significance of "DOLI"

For purposes hereof, "*Directors' & Officers' Liability Insurance (DOLI)*" refers to an indemnity coverage for GOCCs which, and their Directors/Trustees and Officers who, are sued or included as parties to any action or proceeding brought against the government agency or instrumentality pursuant to a provision of law, executive order or regulation by reason of their being Directors/Trustees or Officers.

The basis for the grant of such indemnity is that such Directors/Trustees and Officers act in the best interest of the GOCC so that any suit against them, as such, are really suits against the GOCC.

Where the DOLI coverage is proper and lawful, the premiums paid by the GOCC constitute valid (allowable) expense on the part of the GOCC.

6. Authority to Obtain DOLI Coverage

All GOCCs covered by R A No. 10149, even when acting through their Governing Boards, shall have authority to obtain DOLI coverage for the GOCC itself and/or members of their Governing Boards and Officers, under the following terms and conditions:

- (a) The premiums on DOLI coverage shall constitute part of the annual Corporate Operating Budget of the GOCC, or in supplementary budget when the circumstances so necessitate it;
- (b) Procurement of the DOLI coverage shall be consistent with all applicable procurement laws, rules and regulations, GSIS Law^[12], and Admin. Order No. 33 s. 1987; and
- (c) As an alternative, and when the circumstances so warrant it and clearly evidenced by actuarial and feasibility studies commissioned by the Board, a GOCC may provide for "self-insurance" by constituting a "Directors' and Officers' Liability Fund" under the terms provided for herein.

A GOCC may obtain a DOLI proposal coverage from an Insurance Commission-accredited provider with terms better than what the GSIS may provide or which

GSIS is unwilling to match, and such non-GSIS DOLI coverage is valid and lawful pursuant to Section 5 of Republic Act (R.A.) No. 656, otherwise known as the Property Insurance Law, which among others, would require obtaining a declination letter from GSIS.

7. "Directors/Trustees" and "Officers" Allowed DOLI Coverage

As used in this memorandum, the terms "*Board of Directors/Trustees*" or "*Board*" or "*Governing Board*" ("*Board*") refer to the collegial body that exercises the corporate powers, conducts all business and controls or holds all properties, of a GOCC, whether it be formally referred to as the "Board of Directors" or "Board of Trustees" or some other term in its Charter, Articles of Incorporation or By-laws.^[13]

7.1 Directors/Trustees. – Both *Ex Officio* and Appointive Directors shall be afforded DOLI coverage by the GOCC, as defined below:

- (a) "*Appointive Directors*" refer to: (1) in the case of Chartered GOCCs, all members of its Board of Directors/Trustees who are not *ex officio* members thereof; (2) in the case of Nonchartered GOCCs, members of its Board of Directors/Trustees whom the State nominates, or is entitled to nominate, to the extent of its percentage shareholdings in such GOCC; and (3) in the case of Affiliates, members of its Board of Directors/Trustees whom the GOCC nominates, or is entitled to nominate, to the extent of its percentage shareholdings in such Affiliate.^[14]
- (b) "*Ex Officio Board Member*" (*Ex Officio Director*) refers to any individual who sits or acts as a member of the Board of Directors/Trustees by virtue of one's title to another office, and without further warrant or appointment.^[15]
- (c) *Alternates of Ex Officio Board Members* as authorized under Section 14 of R.A. No. 10149.

7.2 Officers. – Only the following employees of the GOCC shall fall within the term "Officer" to be entitled to DOLI coverage.^[16]

- (a) "*Board Officers*" refer to Officers whose primary task is to serve the Board or to pursue the immediate functions of the Board, such as the Chairman, Vice-Chairman and the Corporate Secretary.^[17]
- (b) "*Executive Officer*" refers to the CEO or whoever is the highest ranking officer in the GOCC, and such other corporate officer of the GOCC as expressly provided for in its Charter (for a Chartered GOCC) or By-laws (for a Nonchartered GOCC), and such other senior officers, such as the Vice-President, Chief Financial Officer, Chief Investment Officer, and General Manager^[18] whose positions are equivalent to the rank of Director, Assistant Secretary or Undersecretary in the National Government Sector. As distinguished from Board Officers, Executive Officers primarily form part of the Management of the GOCC.^[19]

As used in this memorandum, the term “*Officers*” refers to both Executive Officers and Board Officers.

IV. DOLI COVERAGE FOR GOCCs

The DOLI coverage which a GOCC may procure as constituting legitimate company expenditure, may be of two types or both types, namely:

- (a) With the GOCC as the Beneficiary;
- (b) With the Directors/Trustees and Officers as the Beneficiaries.

As a general proposition, therefore, a GOCC may procure DOLI for the purpose of protecting the GOCC itself, its Directors/Trustees and Officers, against the cost of litigation and judgment liability arising from official acts of its Governing Board and Management.

8. DOLI With GOCC as Beneficiary

The portion of the DOLI coverage that reimburses the GOCC from the litigation costs incurred and the damages suffered due to or arising from the breach of a director/trustee/officer of his fiduciary duties would be a legitimate and valid coverage under the principle that every GOCC is expected to take reasonable protection against the damages cause by its Directors/Trustees and/or Officers even for fraud committed by them or those in breach of their fiduciary duties. Such DOLI coverage for the GOCC is similar to the requirement for every responsible public officer to be bonded.

Nothing in this Memorandum shall be construed as relieving any director/trustee/officer from direct personal liability arising from the breach of his fiduciary duties.

9. DOLI With Directors/Trustees and Officers as Beneficiaries

Not all DOLI premium payments constitute valid (allowable) expense on the part of the GOCC. Premium payments for a DOLI that cover costs incurred and judgment liability for a Director’s/Trustee’s or Officer’s breach of fiduciary duties or for fraud committed in the performance of duties is not a valid expense to cover.

The hallmark principles of responsibility and accountability in corporate governance, and the demands that every Director/Trustee or Officer has the duty to act in the best interest of the GOCC, to act with due care, extraordinary diligence, skill and good faith in the conduct of the business of the GOCC, demand that every erring Director/Trustee or Officer must be held personally to account for and therefore cannot be insulated from the effects of his malfeasance or misfeasance through a DOLI coverage.

9.1 Proper Coverage of DOLI. – By way of illustration, without any intention to make the listing exclusive, the following are examples of proper DOLI coverage:

- (a) Costly litigations brought about by employees who have been the proper subject of disciplinary actions.
- (b) Unwarranted or non-meritorious complaints filed with the Ombudsman or other disciplinary agencies for the purpose merely of taking defensive measures to compel settlement.