



**Indemnities, guarantees and warranties
by the Commonwealth**

Resource Management Guide No. 414

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The words '**must**', '**required**', '**requires**' and '**requiring**' denote mandatory compliance by accountable authorities/officials. The use of the words 'could', 'may', 'encouraged' or 'consider' convey non-mandatory guidance. The guidance to which these words relate may or may not be applied by accountable authorities/officials in their approach to resource management, depending on the operating circumstances of the entity and its appetite for risk.

Contents

Audience	2
Related resources	2
Key points	2
What is an indemnity?	3
Why grant an indemnity to another person?	3
Does a liability cap create a contingent liability?	4
What must be considered before granting an indemnity?	4
When does Comcover need to be notified of a proposed indemnity?	6
Who can grant an indemnity?	6
When can a delegate (or sub-delegate) grant an indemnity?	6
How can an indemnity be granted, if it is beyond the scope of the delegation?	7
What amounts to explicit agreement by Cabinet or the Prime Minister?	7
How to ask the Finance Minister to grant an indemnity?	8
Who is responsible for managing an indemnity?	9
Do indemnities need to be reported?	10
Appendix — Indemnity grant request form	11

Audience

This guide is relevant to officials in non-corporate Commonwealth entities (NCEs) who:

- have been sub-delegated by their accountable authority the power to grant an indemnity, guarantee or warranty on behalf of the Commonwealth
- need to brief their accountable authority about an indemnity, guarantee or warranty or
- request the Finance Minister grant an indemnity, guarantee or warranty.

Related resources

- [PGPA \(Finance Minister to Accountable Authorities of NCEs\) Delegation 2014](#)
- [RMG 203: General duties of officials](#)
- [RMG 206: Model Accountable Authority Instructions – Non-Corporate Commonwealth Entities](#)
- [RMG 400: Commitments of relevant money](#)
- [Commonwealth Risk Management Policy](#)

Key points

- Officials of NCEs can enter into arrangements that provide indemnities, guarantees and warranties (collectively referred to as indemnities) on behalf of the Commonwealth to other parties, subject to the limitations in the PGPA Act.
 - Indemnities are types of *contingent liabilities* (i.e. they may give rise to a liability on the occurrence of a future event), which are legally enforceable obligations.
- The PGPA Act enables the Finance Minister to grant indemnities on behalf of the Commonwealth ([section 60](#)). This power has been delegated, with directions limiting its use, to accountable authorities of NCEs (Schedule 1, Part 6 of the [Finance Minister's delegations](#)).
- An accountable authority can sub-delegate this power, with written limitations that are consistent with the limits in the Finance Minister's delegation, to officials of their own entity, or officials of another NCE. A sub-delegate must also comply with any other directions of the accountable authority.
- The delegation from the Finance Minister requires that an official who is delegated the power to enter indemnities must consider two overarching principles:
 - that risks should be borne by the party best placed to manage them; and
 - benefits to the Commonwealth should outweigh the risks involved.
- An official can only grant an indemnity, guarantee or warranty involving a contingent liability in relation to an event on behalf of the Commonwealth, if the delegate is satisfied that:
 - the likelihood of the event occurring is remote, i.e. it has a less than 5% chance of occurring; and
 - the most probable expenditure if the event occurred is not significant, i.e. it would be less than \$30 million.

- If an indemnity is beyond the scope of the delegation, an indemnity can only be granted on behalf of the Commonwealth if it has been agreed in a decision of Cabinet, the National Security Committee of Cabinet (NSC) or its successor or the Prime Minister, or a written determination of the Finance Minister.

What is an indemnity?

1. Indemnities are types of *contingent liabilities* (i.e. they may give rise to a liability on the occurrence of a future event), which are legally enforceable obligations. As a result, they may be included in contractual arrangements between an NCE and another party:
 - an **indemnity** is a legally binding promise whereby the Commonwealth undertakes to accept the risk of loss or damage another party may suffer
 - a **guarantee** is a promise whereby the Commonwealth assumes responsibility for the debt, or performance obligations of, another party on default of its obligation
 - a **warranty** is a promise whereby the Commonwealth provides certain assurances to the other party to an arrangement.
2. The following cases are not indemnities, i.e. the Commonwealth is making a representation to another party that does not create a contingent liability:
 - an NCE agrees to reimburse another party for expenses that person incurs in the ordinary course of providing services to the Commonwealth
 - the Commonwealth warrants that it has title to property that was the subject of sale agreement, or that it is authorised to enter into a transaction.
3. The Commonwealth can enter into arrangements involving a contingent liability with any party other than itself. That is, NCEs cannot enter into these types of arrangements with other NCEs (as they are part of the same legal entity). NCEs may enter into such arrangements with corporate Commonwealth entities due to their separate legal personality from the Commonwealth.
4. If an arrangement does not explicitly allocate liability between the parties, each party's liability may be determined at general law. To create greater certainty and/or allocate liability, a liability regime may be agreed in a contract. If an NCE grants an indemnity that results in a contingent liability, the Commonwealth is ultimately agreeing to accept particular risks (often a greater level of risk) so that the other party will bear less risk.

Why grant an indemnity to another person?

5. The ability to grant indemnities on behalf of the Commonwealth is important in cooperative ventures. The ability of entities to cooperate together and with others outside of government to share resources, knowledge and expertise is increasingly important. Granting indemnities for persons outside of the Commonwealth who are assisting the Commonwealth achieve its outcomes can provide assurance in certain situations.

Does a liability cap create a contingent liability?

6. A liability cap does not create a contingent liability.
7. A liability cap is an arrangement where an entity agrees to a limit on the liability of another party (e.g. a supplier). If the entity subsequently suffers a loss as a result of an act or omission of the supplier in relation to the performance of the contract, the entity has agreed it will not seek to recover from the supplier more than the amount of an agreed cap.
8. Liability caps can operate differently from indemnities, although in some circumstances they may form part of the terms of an indemnity. If a NCE agrees to indemnify a supplier, it is agreeing that if the supplier suffers a specified type of loss then the NCE will meet the cost of that loss. An indemnity need not be unlimited, e.g. it may be activated only after the loss reaches a pre-agreed value, and/or it may be capped.
9. A liability cap may result in the creation of a contingent liability, if:
 - it involves limiting a supplier's contingent liability to a third party so that the Commonwealth is liable to the third party for any excess above that cap or
 - it limits a supplier's exposure for damage the supplier has suffered itself, so that the Commonwealth is liable to the supplier for any excess.
10. A liability cap does not create a contingent obligation to pay another person and cannot be treated as a contingent liability, to the extent that it:
 - limits a supplier's liability to the Commonwealth, under that arrangement with the Commonwealth, so that the Commonwealth cannot recover damages from the supplier if the Commonwealth is sued by a third party
 - limits a supplier's liability to the Commonwealth, under that arrangement with the Commonwealth, for damage it directly causes the Commonwealth or
 - simply caps a supplier's liability for certain expenses that the supplier incurs in the ordinary course of providing services to the Commonwealth, so that the Commonwealth will reimburse the supplier for any relevant expenses over the amount of the cap.

What must be considered before granting an indemnity?

11. Before granting an indemnity, an official must ensure that the:
 - risk management arrangements are appropriate to the complexity and potential costs of the indemnity are in place before entering, after entering and for the duration of the arrangement
 - legislative requirements under the PGPA Act and the delegations (of the Finance Minister and the accountable authority) are satisfied.
12. Officials are encouraged to consider:
 - whether there is an explicitly identified risk, and that indemnities are not issued simply to provide comfort against general, unspecified events (e.g. where an indemnity is provided for 'damage to property', it is generally better practice to specify that only damage caused by the NCE's use is covered so as to expose the Commonwealth to minimum risk)

- whether alternatives, such as the use by the other party of commercial insurance, are appropriate
 - that the indemnity does not cover damages resulting from acts by an indemnified person which are malicious, fraudulent, wilful, or reckless
 - whether including a requirement that the indemnified party advise the Commonwealth of relevant information is appropriate
 - whether the proposed indemnity may set an undesirable precedent in an industry, particularly where there is little competition
 - whether the potential cost will be funded from existing resources or from insurance provided by Comcover, this may require:
 - discussing the proposed indemnity with Comcover or
 - if funding cannot be met from existing resources, it may be necessary to request additional funding through the Budget process (this will involve identifying the most probable total cost and the price of the risk to the Commonwealth excluding any potential insurance claims)
 - including a maximum financial limit on payments or claims (the express inclusion of a maximum financial limit can be an important mechanism to protect the position of the Commonwealth)
 - including a time limit (e.g. claims may only be able to be made during the term of the arrangement, so these arrangements are preferably not open-ended), noting that options to extend time limits may be appropriate in certain circumstances, but officials are encouraged not to commit the Commonwealth longer than necessary
 - whether the arrangement will explicitly reserve the right for the Commonwealth to terminate the arrangement when it is no longer needed
 - whether subrogation and notification clauses need to be included in an indemnity. If needed, the arrangement could include subrogation clauses (clauses providing the Commonwealth with the right to exercise the option of conducting, or participating in, the defence of any claims against the indemnified party, and to require full assistance from that party) and clauses giving the Commonwealth the right to take over any litigation related to the indemnity.
13. Where a proposed arrangement with an indemnity will be complex or involve significant potential costs, officials are strongly encouraged to get legal advice. For example:
- whether any legislation restricts the power to enter the arrangement
 - what extra risks the Commonwealth would be accepting if it granted the indemnity. It is expected that legal advisers work with other relevant expert advisers to identify and assess risks
 - whether the proposed indemnity only seeks to replicate liabilities that will already be imposed on the Commonwealth by common law or Commonwealth legislation (including the *Competition and Consumer Act 2010*). If so, consider excluding these provisions as redundant unless there is a clear justification for not doing so.

When does Comcover need to be notified of a proposed indemnity?

14. All NCEs are insured against losses for normally insurable risks by Comcover (other than worker's compensation which is the responsibility of Comcare). Prior to entering into any arrangement that includes an indemnity, entities need to be aware of, and follow, the terms and conditions outlined in the [*Comcover Statement of Cover*](#).
15. If officials are considering a proposed indemnity involving a contingent liability above any liability cap in the [*Comcover Statement of Cover*](#), they are strongly encouraged to discuss it with Comcover prior to granting the indemnity. Comcover can provide support and advice to entities on how best to manage these risks by contacting comcover@comcover.com.au or calling 1800 651 540.

Who can grant an indemnity?

16. The PGPA Act gives the Finance Minister the power to grant an indemnity, guarantee or warranty on behalf of the Commonwealth ([*section 60*](#)). This power has been delegated, with directions limiting its exercise, to accountable authorities of NCEs (Schedule 1, Part 6 of the [*Finance Minister's delegation instrument*](#)).
17. The PGPA Act enables an accountable authority to sub-delegate this power, with written limitations that correspond to the limits contained in the Finance Minister's delegation, to officials of their own entity, or an official of another NCE ([*sections 110\(1\) and \(6\)*](#) of the PGPA Act.). The accountable authority can include directions to suit the context of the power and appetite for risk (which must not be inconsistent with the Finance Minister's directions).
18. An accountable authority or their sub-delegate must consider whether granting an indemnity is appropriate in the circumstances.

When can a delegate (or sub-delegate) grant an indemnity?

19. The delegation requires a delegate to consider two overarching policy principles before granting an indemnity:
 - that risks be borne by the party best placed to manage them and
 - benefits to the Commonwealth need to outweigh the risks involved.
20. A delegate is only empowered to grant an indemnity, guarantee or warranty involving a contingent liability in relation to an event on behalf of the Commonwealth, if:
 - They are satisfied that the likelihood of the event occurring is remote, i.e. it has a less than 5% chance of occurring and
 - the most probable expenditure if the event occurred is not significant, i.e. it would be less than \$30 million.
21. In order to be satisfied, the delegate **must** make reasonable inquiries to determine the likelihood and amount of any contingent liability. A sub-delegate may wish to take a proportionate approach, i.e. consider the complexity, risks and materiality of the proposed arrangement. The greater these factors are, the more extensive the inquiry.
22. When determining the most probable cost in relation to an indemnity, the potential proceeds of insurance **must not** be taken into account. The availability of insurance to cover a contingent

liability may not reduce the most probable expenditure by the Commonwealth as a whole (whether by the NCE, by Comcover, and/or from Budget measures). It cannot be assumed that an insurance claim will result in a payment by an insurer. However, accountable authorities may direct that decisions made in relation to indemnities be recorded in accordance with insurance requirements, such as in the *Comcover Statement of Cover*.

23. The limits in the delegation of the power in *section 60* by the Finance Minister expressly direct that a delegate:
- cannot grant a guarantee for the payment of any amount of principal or interest due on a loan an
 - cannot grant an indemnity that would expressly meet the costs of civil or criminal penalties of the indemnified party
 - must consider the following two overarching policy principles before exercising the delegation, that:
 - risks be borne by the party best placed to manage them and
 - benefits to the Commonwealth outweigh the risks involved.

How can an indemnity be granted, if it is beyond the scope of the delegation?

24. An indemnity can be granted if it:
- has been explicitly agreed in a decision of Cabinet, the National Security Committee of Cabinet (NSC) or its successor or the Prime Minister or
 - is in accordance with a written determination of the Finance Minister.
25. In approval has been provided by one of these sources, the directions in the Finance Minister's delegation of the power to grant an indemnity in *section 60* of the PGPA Act (discussed above) do not apply.

What amounts to explicit agreement by Cabinet or the Prime Minister?

26. To rely on a decision of Cabinet, the NSC (or its successor) or the Prime Minister to grant an indemnity, the decision must explicitly provide details on:
- who the party is that the Commonwealth will make the arrangement with
 - the time period covered by the arrangement
 - the risk of the contingent event occurring and
 - the most probable cost to the Commonwealth.

How to ask the Finance Minister to grant an indemnity?

27. The NCE's responsible minister should write to the Finance Minister to formally request the Finance Minister grant the indemnity. The letter should:
- identify why the accountable authority of the entity cannot grant the indemnity (e.g. the granting of the indemnity involving a contingent liability falls outside the scope of the directions of the Finance Minister's delegation to accountable authorities)
 - contain the model Indemnity Grant Request Form in the [Appendix](#) below.
 - provide reasons why the indemnity is needed.
28. Entities that consider they may need the Finance Minister's approval to grant an indemnity can contact their Agency Advice Unit (AAU) in Finance in the first instance. Where the proposed arrangement will constitute new policy it must be considered in accordance with the Budget process. To assist the Finance Minister's decision, officials can provide Finance copies of any:
- legal advice it has received on the matter
 - risk assessments and
 - draft agreements, contracts or other relevant documents.
29. The Finance Minister will reply, by letter, to the NCE's responsible Minister. If the Finance Minister agrees to grant the indemnity, the letter will provide authority for the accountable authority of the relevant entity, or the accountable authority's delegate, to enter the arrangement with the specific indemnity.

Case study:

An accountable authority wants to establish streamlined processes for officials entering routine arrangements for venue hire. Venue hire arrangements typically contain indemnity clauses covering damage while being used by the hirer.

The accountable authority sub-delegates his/her power under [section 60](#) of the PGPA Act to all officials that have the power to enter into arrangements (i.e. [subsection 23\(1\)](#) delegates) where the chance of triggering the indemnity is assessed as remote and the most likely cost, if a contingent event occurs, would be less than, \$5 million. This will mean that when considering entering into arrangements, [subsection 23\(1\)](#) delegates can also use their powers under section 60 of the PGPA Act to grant the indemnity.

The accountable authority may also provide a checklist in relation to venue hire, through the internal controls of the entity, to guide officials with a delegation to grant an indemnity and a delegation to enter an arrangement.

That checklist may set risk parameters such as:

- the venue is within Australia
- the function will be attended by fewer than 150 people
- the venue is to be used for the purposes of events attended by public servants and/or reputable external people
- the likelihood of unsociable behaviour is remote

- where subcontractors are engaged, the services provided are limited to the provision of facilitation services, scribing services, catering services or the provision of audio/visual services
- the contract does not provide an indemnity that would expressly meet the costs of civil or criminal penalties of the indemnified party.

The accountable authority may also decide to provide risk mitigation strategies as part of their internal controls, such as:

- officials granting an indemnity are encouraged to vet attendees
- officials are encouraged to advise attendees that they are responsible for their personal equipment and ensure adequate physical security of valuable equipment
- officials are encouraged to ensure there is appropriate security at the venue
- officials are encouraged to ensure alcohol service (if included) is controlled
- officials are encouraged to incorporate contingent liabilities into subcontractor arrangements (where applicable) and ensure the use of reputable subcontractors.

Who is responsible for managing an indemnity?

30. An official who is responsible for managing an arrangement that contains an indemnity must exercise this power with the degree of care and diligence that a reasonable person would exercise in the same position ([section 25](#) of the PGPA Act) and act honestly, in good faith and for a proper purpose ([section 26](#) of the PGPA Act). This means being aware of and complying with the directions or instructions of their accountable authority, and seeking to prevent events from occurring that could generate additional financial costs for the Commonwealth. An event occurring that activates an indemnity can place financial obligations on the Commonwealth, and potentially constrain its ability to allocate resources. In this case, the official needs to manage risks and ensure the proper use and management of public resources.
31. Sound risk management is fundamental to the effective management of exposures that result from granting an indemnity. Under the PGPA Act, responsibility for risk management resides with the accountable authority. The [Commonwealth Risk Management Policy](#) requires accountable authorities to embed risk management as part of the culture of the entity so that the shared understanding of risk leads to well informed decision making, in a way that:
 - minimises the long term costs to the Commonwealth
 - manages the relationship with the indemnified party to reduce the likelihood that a contingency is triggered and
 - manages the risks from an entity perspective, by:
 - identifying the context the risk is to be managed in
 - identifying the risks to be managed, this can be done in consultation with other parties who may have a greater understanding of the risk
 - analysing the risks, possible consequences and likelihood of occurrence
 - identify the need to retain the risk or whether the risk may be transferred

- if the risk is to be retained how is the risk to be treated.
32. Systematic reviews are essential to ensure the changing profile of the risks do not expose the Commonwealth to an increased level of risk.

Do indemnities need to be reported?

33. Legislative requirements for reporting contingent liabilities, such as indemnities, are contained in the [Charter of Budget Honesty Act 1998](#). Contingent liabilities with a possible impact on the forward estimates greater than \$20 million in any one year, or \$50 million over the forward estimates period are disclosed in Budget Paper 1 – Budget Strategy and Outlook. (e.g. [2016-17 Budget Paper No. 1: Budget Strategy and Outlook](#), Statement 8: Statement of Risks). Indemnities do not impact fiscal or underlying cash balances unless the contingent event occurs, creating a liability.
34. NCEs are also required to report contingent liabilities in their annual financial statements in accordance with the [PGPA Financial Reporting Rule 2015](#).

Appendix — Indemnity grant request form

Note: In completing this form, please be succinct, but provide sufficient information to enable the Finance Minister to understand the issues and probable cost involved.

1. Brief description of the proposed arrangement and contingent liability.

2. Explanation of why the arrangement requires agreement from the Finance Minister.

3. Name of the relevant outcome and program (if applicable).

4. Date by which agreement is required and reason.

5. Term of agreement (including detail on options for extension) including specific term of all contingent liabilities.

6. Attach a copy of the risk assessment (if complex, please provide a summary. However, you will need to have a comprehensive risk assessment in place for your own records)

- a) Has a risk management plan been established? (yes or no)
- b) Is there a liability cap in place? (yes or no)
- c) If yes to b) what is the amount of the cap? \$
- d) What is the most probable total cost of all contingent liabilities?
- e) Is the most probable cost that might be payable under any contingent liability significant(*)? (yes or no)
- f) Is the likelihood of the contingencies occurring remote(#)? (yes or no)
- g) Is there a guarantee for the payment of any amount of principal or interest due on a loan? (yes or no)
- h) Is there an indemnity by the Commonwealth to expressly meet the costs of civil or criminal penalties of the indemnified party? (yes or no)

7. Has legal advice been obtained in relation to the contingent liability? (yes or no)

Please attach a copy of the legal advice.

***significant** and **#remote**: as defined in the Finance Minister's Delegation to Accountable Authorities for section 60 of the *Public Governance, Performance and Accountability Act 2013*.