D&O Liability

Rise in Litigation Exposes New Areas of Risk

By Sarah Downey

The pressure on boards keeps rising—and along with it individual directors’ personal liability exposure. Three emerging risk areas necessitate that directors and officers (D&O) understand how liability insurance can help mitigate these risks.

Cyber-Risk Exposure

Cyber-related losses remain a worrisome exposure for directors and officers. Despite the occurrence of some significant cyber breaches, few related traditional securities class-action lawsuits had historically been filed. However, the tide is changing: A number of cyber-related securities class actions have recently been filed, including one that settled for $80 million.

Exposure caused by cybersecurity-related incidents isn’t limited to securities class actions: related derivative lawsuits against a company’s directors and officers continue to be filed. These are especially worrisome to directors and officers as oftentimes a company will be unable to, or prohibited from, indemnifying directors or officers for any related settlement or judgment, leaving D&O liability insurance as the sole protection against personal asset exposure.

From a regulatory perspective, the U.S. Securities and Exchange Commission (SEC) has made cybersecurity a priority. In September, the SEC announced the creation of a Cyber Unit. More recently, the agency released interpretive guidance that clarifies the cybersecurity risk disclosure obligations of public companies and their boards. There’s likely to be an uptick in regulatory investigations and civil claims arising out of purported breaches of the SEC’s recommendations.

In their capacity as a director or officer, to limit their personal asset exposure from cyber-related incidents, it is prudent that directors and officers work with their insurance advisors to

■ analyze their current D&O program, including total limits and Side-A Difference in Conditions limits (D&O insurance that only covers individuals);

■ determine the extent of regulatory investigation coverage, which is not always included in corporate D&O policies; and

■ review cyber insurance policies, making sure appropriate coverage is in place.

Sexual Misconduct Suits Rising

The direct impact of the #MeToo movement on directors and officers is coming to light. Many companies understand the importance of broad employment practices liability (EPL) insurance policies, but few appreciate the potential intersection with D&O insurance. The #MeToo movement has already prompted related derivative lawsuits and securities class actions, which often target directors and officers.

Marsh expects both the D&O underwriting and claims environment to respond accordingly. The firm has already started to see D&O underwriters ask EPL-related questions to assess the tone at the top of many organizations, including their culture of enforcing anti-harassment policies.

It is imperative that directors and officers ensure that they have sufficient D&O limits in place, that their policies are broadly worded, and that they understand the limitations and conditions of those policies.

Protecting Oneself

In 2017, the number of securities class-action lawsuit filings surged and this year is shaping up to see even more: 123 federal securities class-action lawsuits were filed in the first quarter, according to NERA Economic Consulting. If filings continue at this pace, 491 suits will be filed by year-end, surpassing 2017’s record of 428 suits.

The increase in exposure to D&O-related losses will make for a challenging claims and underwriting environment. Directors, officers, and the companies they serve should take all necessary steps to prepare for their D&O program renewals or the possibility of a claim. These steps include:

■ Understand your potential exposure areas, and prepare to explain to insurers what protections and response measures are in place.

■ Review specific analytics to ensure you are purchasing appropriate limits of liability and types of financial and professional coverage to match your risk exposure.

■ Look for the broadest coverage and stay informed of coverage enhancements.

■ Understand the composition of your D&O program, your insurers’ claim-adjusting reputation, and the value behind the insured-insurer relationship.

In a heightened risk environment, it’s essential that directors and officers consult closely with their insurance and legal advisors to ensure the companies they serve have robust D&O insurance programs that protect both corporate and personal assets against these exposures.

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