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Regulatory/Law

Litigation Uptick

D&O insurers are seeing an increase in securities class action lawsuits.

By **Rafael Rivera Jr.**

Last year was the third consecutive year of elevated federal securities class action (SCA) lawsuits filed against publicly traded companies. In part, this was due to event-driven securities litigation, in which shareholders have alleged that directors and officers (D&Os) did not provide adequate disclosures about the possibility of an unexpected disaster, accident or event occurring, or did not put sufficient controls in place to prevent either from transpiring. SCA lawsuits arising from cyberattacks and the #MeToo movement are examples.

Another contributing factor was merger-objection litigation, in which shareholders alleged that D&Os failed to maximize shareholder value or failed to make adequate disclosures. Almost invariably, these lawsuits are settled after the target company agrees to make additional disclosures and cover the plaintiffs' legal fees.

The U.S. Supreme Court's ruling in *Cyan Inc. v. Beaver County Employees Retirement Fund* also played a role in increasing SCA lawsuits. There, the Supreme Court held that state courts have concurrent jurisdiction over actions filed under the Securities Act of 1933. As a result, state SCA lawsuits have been on the rise, sometimes being filed alongside a federal SCA lawsuit and thus unnecessarily increasing defense expenditures.

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From the perspective of D&O insurers, the increase in claim filing and expanding inventory of unresolved matters appears to be the new norm. Reserves must be properly set because these matters may involve significant defense costs and potential settlements. This, in turn, could undermine underwriting profitability or results for a given year. Thus, until legal reforms are adopted to address the influx of SCA filings, insurers must respond accordingly to these new market conditions.

For starters, D&O insurers are addressing these developments by increasing premiums and self-insured retentions, while also lowering policy liability limits. In addition, D&O insurers might also consider amending policy forms. An exclusion could be added to

address an executive's settlement of sexual harassment or assault claims. Similarly, D&O insurers can enhance provisions to control or cap defense counsel rates in reimbursement policies, including preapproved panel counsel requirements, and can strengthen litigation management guidelines to minimize excessive fees and expenses.

Moreover, D&O insurers should effectively monitor such claims and consider evaluating claim and adjustment strategies. To that end, D&O insurers should consider retaining coverage counsel earlier in the life of a claim, coordinating more closely with defense counsel and pursing earlier resolution strategies to limit defense costs.

Such involvement can take the form of: regular status and strategy meetings with trusted coverage counsel, insureds and defense counsel; retaining separate experts to perform damages analysis; obtaining, reviewing and understanding key documents as soon as possible; and attending key depositions and mediations. Combined, these steps could help minimize claim-related costs.

Until legal reforms are adopted to address elevated SCA lawsuits, D&O insurers face new market challenges. To minimize underwriting losses, they should consider adopting pricing-related mechanisms, policy form amendments, and effective claim and adjustment strategies. Doing so may lower the ultimate cost of litigation and thus offset some of the expected costs associated with the increase in claim filing and the expanding inventory of unresolved matters. BR