RIMS FEBRUARY PRESENTATION

DIRECTORS AND OFFICERS INSURANCE

HOLLAND&HART

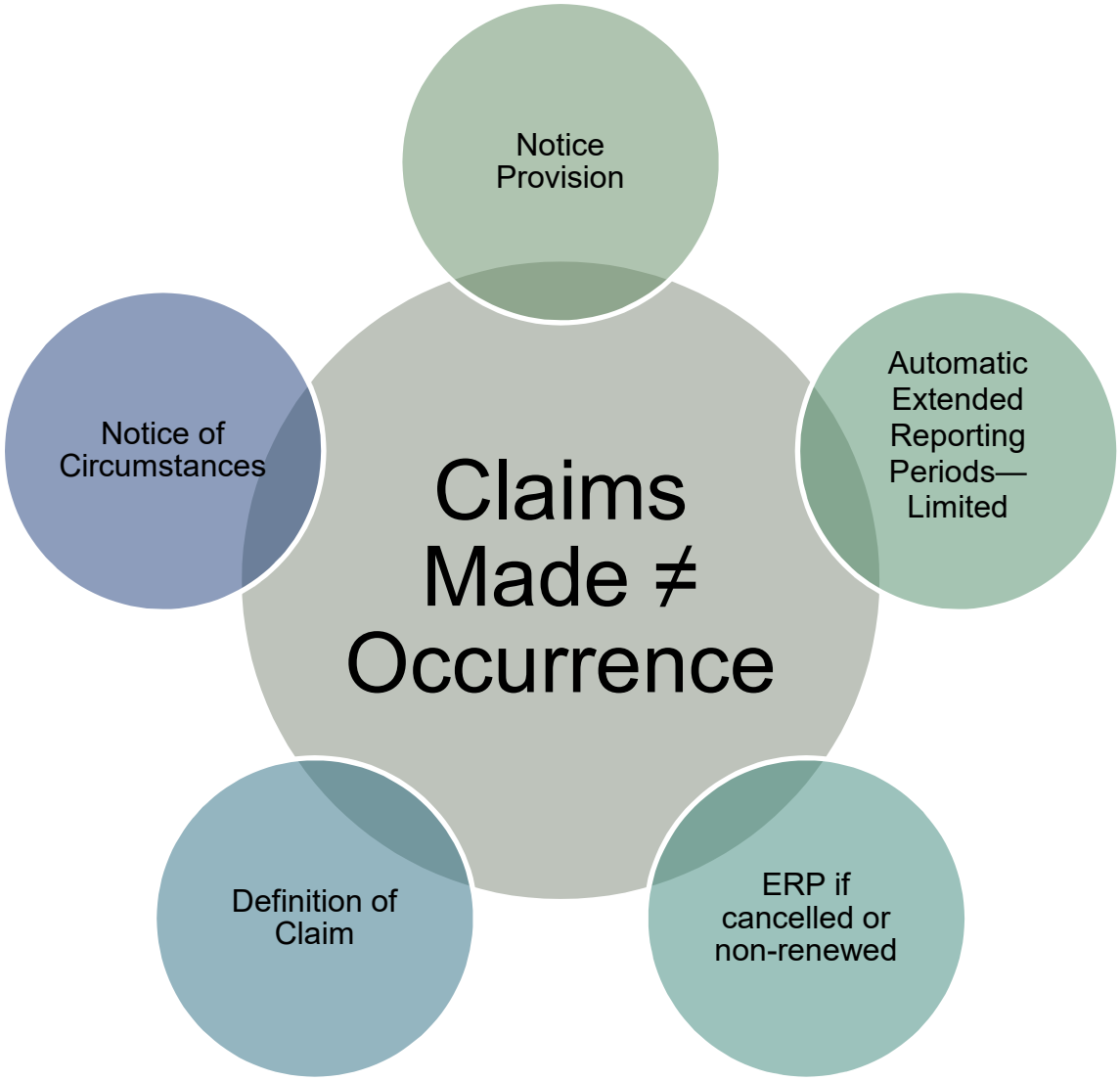
TOPICS FOR DISCUSSION

- Change In Control/Notice of Circumstances
- Class Actions Against D&O's
- Overcoming Initial Denials

CONFUSION IN D&O COVERAGE

- No Standardized Forms
- Coverage Forms Can Vary Even Within One Insurer
- Soft Market Created Unique Enhancements
- Private v. Public Entity Coverage

COMMON CONCEPTS IN D&O



CHANGE IN CONTROL SCENARIO

Oil & Gas Company in negotiations to be acquired

- Chair of BOD asks GC about D&O
- Chair wants to ensure post-transaction coverage
- Chair wants to make sure D&O coverage going forward covers individuals on new board

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ISSUES ADDRESSED

What is a change in control?

Difference between ERP and Run-Off?

Why is the Run-Off needed?

How long should the Run-Off last?

Found massive discrepancies in D&O tower.

Fixed problems with Side A DIC.

Worked with underwriting to issue 6 year Run-Off.

EXAMPLE CHANGE IN CONTROL DEFINITION

"Change in Control" means

the merger or acquisition of the Organization, or of all or substantially all of its assets…such that the Organization is not the surviving entity	the acquisition of the right to vote, select or appoint more than 50% of the directors of the Organization	the appointment of a receiver, conservator, liquidator, or trustee with respect to the Organization

RESULT OF CHANGE IN CONTROL

Coverage under the policy can terminate on the date of the transaction.

Coverage under the policy will continue but only for wrongful acts committed prior to the transaction date.

If coverage continued, premium is fully earned and the policy cannot be canceled.

SWITCHING D&O COVERAGE

NOTICE OF CIRCUMSTANCES SCENARIO

SAMPLE WARRANTY EXCLUSION

IT IS AGREED THAT IF SUCH KNOWLEDGE OR INFORMATION EXISTS, ANY CLAIM ARISING THEREFROM (WHETHER OR NOT DISCLOSED HEREIN), IN ADDITION TO ANY OTHER REMEDY THE INSURER MAY HAVE, IS EXCLUDED FROM THE PROPOSED COVERAGE.

SAMPLE KNOWLEDGE EXCLUSION

However, in the event that any of the statements, warranties or representations are not accurately and completely disclosed in the **Application**, no coverage shall be afforded for any **Claim** alleging, arising out of, based upon, attributable to or in consequence of the subject matter of any incomplete or inaccurate statements, warranties or representations under:

1. Insuring Agreement A. *Insured Person Coverage*, with respect to any **Insured Person** who knew of such inaccurate or incomplete statements, warranties or representations;

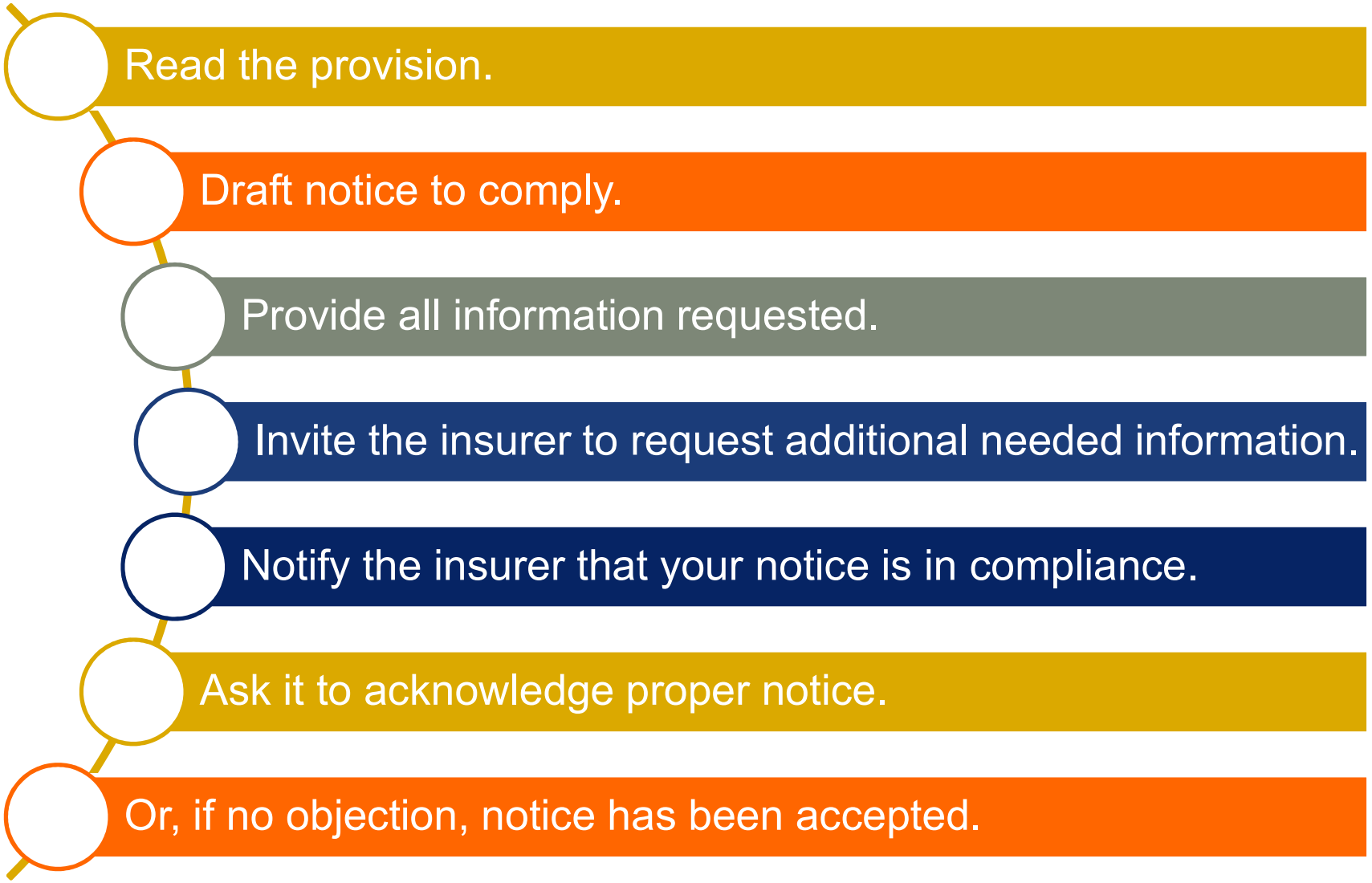
2. Insuring Agreement B. *Indemnification Of Insured Person Coverage,* with respect to the indemnification of any **Insured Person** who knew, as of the inception date of the **Policy Period**, the facts that were not accurately and completely disclosed; and

3. Insuring Agreement C. *Organization Coverage,* with respect to any **Organization** if any past or present chief executive officer or chief financial officer of the **Named Entity** knew, as of the inception date of the **Policy Period**, the facts that were not accurately and completely disclosed.

SAMPLE RESCISSION PROVISION

If the statements, warranties and representations in the Application were not accurate and complete and materially affected either the acceptance of the risk or the hazard assumed by the Insurer, then the Insurer shall have the right to void coverage under this policy, *ab initio*….

EFFECTIVE NOTICE OF CIRCUMSTANCE



DERIVATIVE LAWSUITS

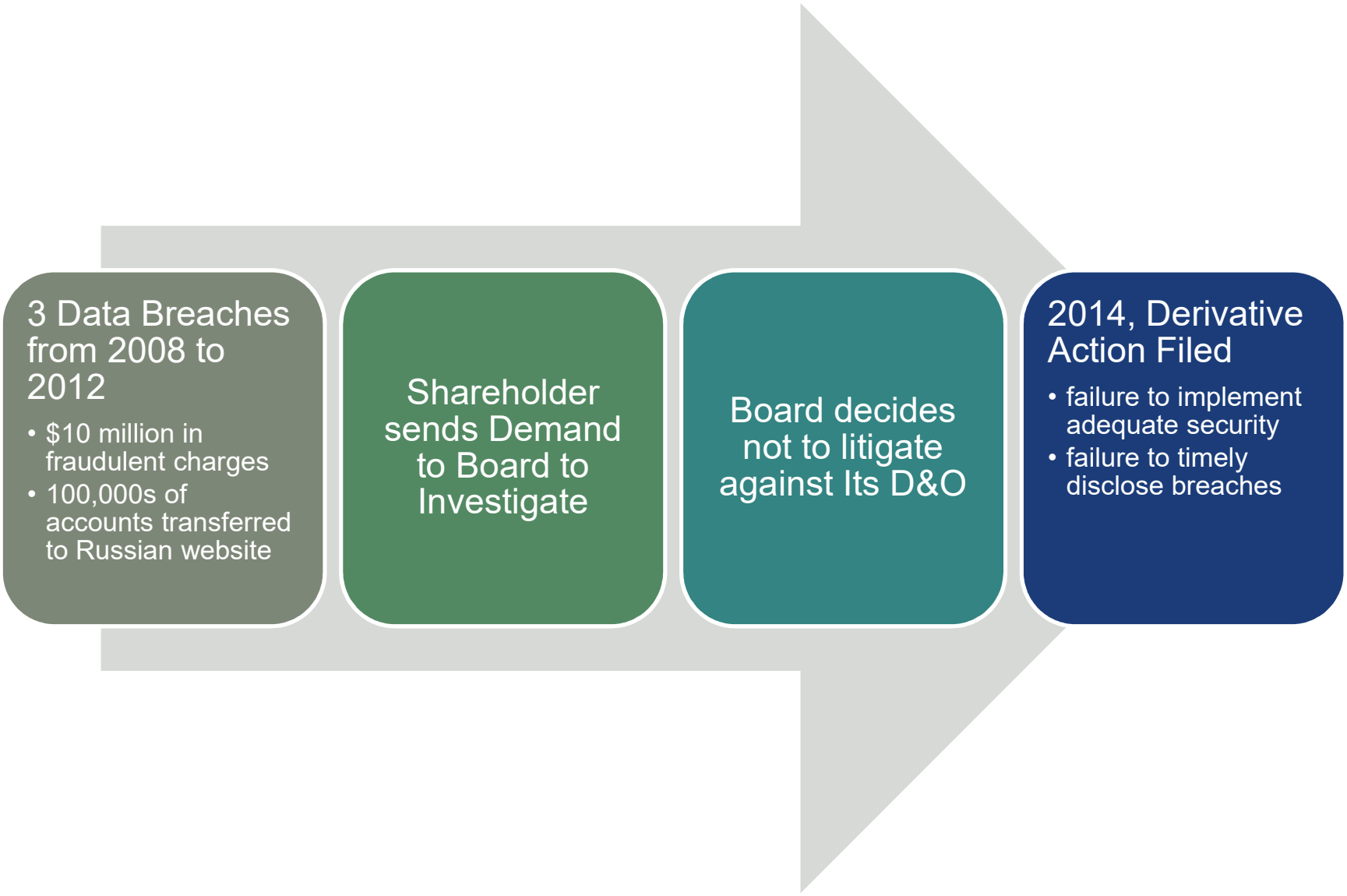
Shareholder derivative suit: action brought by a corporate shareholder on behalf of the corporation to enforce a corporate right that the officers and directors of the corporation have failed to enforce.

Shareholder must claim (1) that corporation was harmed; (2) that D&Os failed to take action to remedy harm; (3) shareholders must take action in place of D&Os.

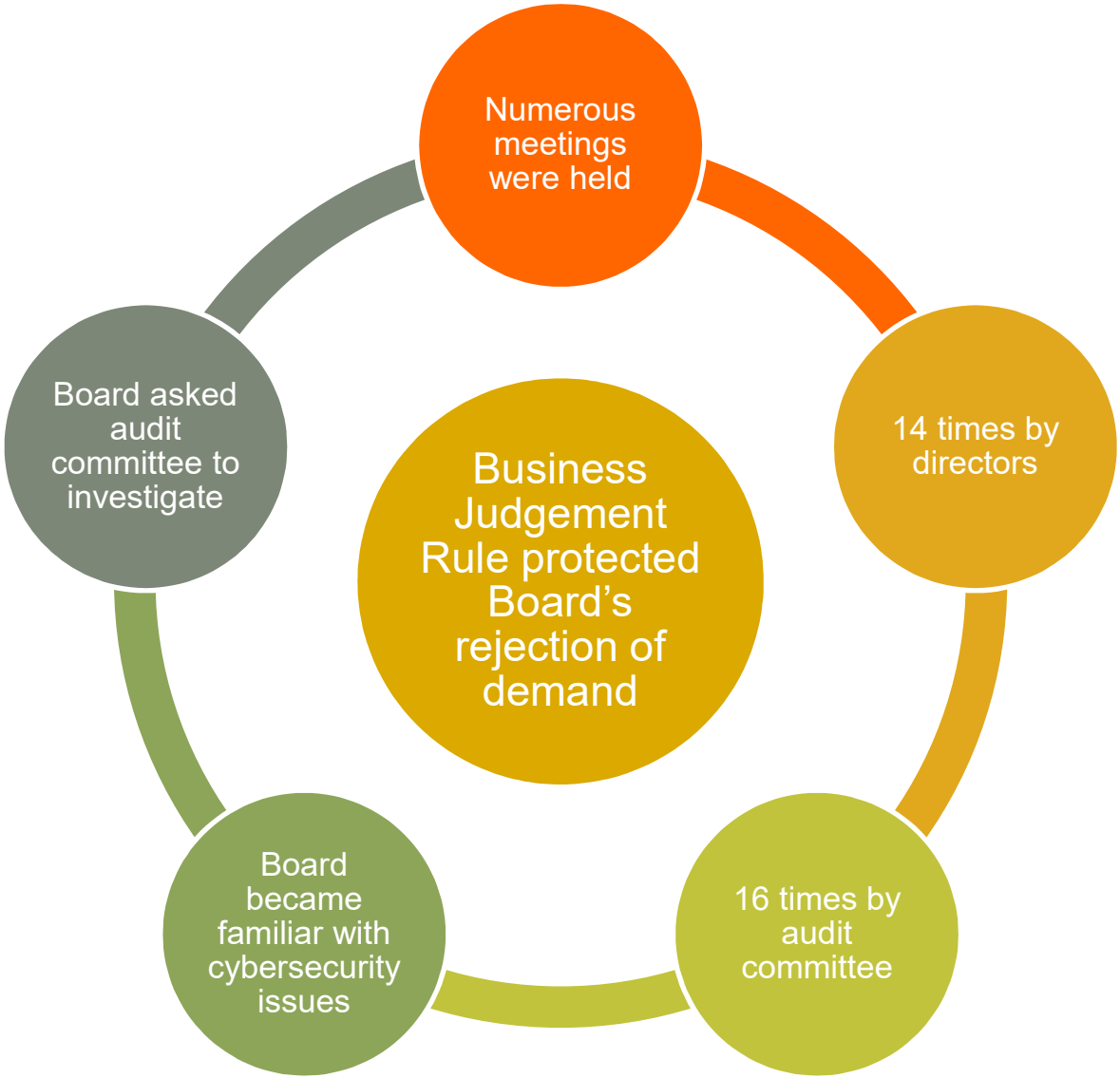
Threshold: before suit, shareholder must make a "demand" on Board clearly identifying alleged wrong and demanding the corporation take action to remedy it, or that it would be futile to do so.

Shareholder must overcome the business judgment rule - a presumption that in making a business decision, the directors acted on an informed basis, in good faith and in the honest belief that the action taken was in the best interests of the company.

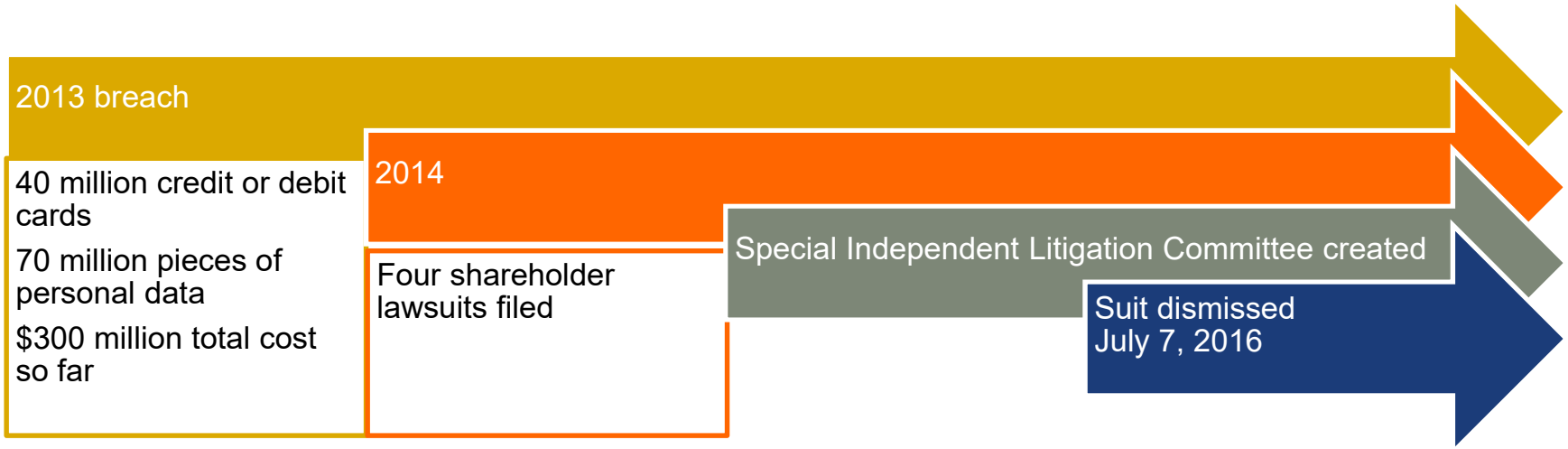
Wyndham (Palkon v. Holmes)



Wyndham Shareholder Lawsuit Dismissed



Target (Kulla et al v. Steinhafel et al.)



Home Depot (Bennek v. Ackerman et al)

2014 Breach of Payment Card Data Systems

- Hackers used 3rd party vendor's credentials to enter the network
- Hackers stole financial data of 56 million customers - similar malware as Target
- Net cost of breach
  - $152 million/ total cost to HD estimated to be $10 Billion

2015 Shareholder Files Derivative Suit

- Home Depot failed to take "responsible measures to protect its customers' personal and financial information."
- Home Depot breached duty of loyalty by failing to institute internal controls sufficient to oversee risks – failed to comply with PCI-DSS
- Home Depot breached duty of loyalty by disbanding Cyber oversight committee

Home Depot (Bennek v. Ackerman et al)

Audit committee received regular reports from management on the state of Home Depot's cybersecurity – regular system of reporting

Board approved a plan to remedy PCI-DSS and other security weaknesses.

"There is no question that the Board was fulfilling its duty of loyalty to ensure that a reasonable system of reporting existed." The Board also approved a plan to fix known security weaknesses; "with the benefit of hindsight, one can safely say that the implementation of the plan was probably too slow," but the directors' decision-making must be "reasonable not perfect."

Suit Dismissed November 30, 2016

Wendy's Derivative Suit December 2016

January 2016

- Wendy's discloses data breach

May 2016

- Credit Union files class action on behalf of financial institutions for losses relating to breach

July 2016

- Wendy's reports breach affected > 1000 locations, spanned from Sept. 2015 – June 2016

December 2016

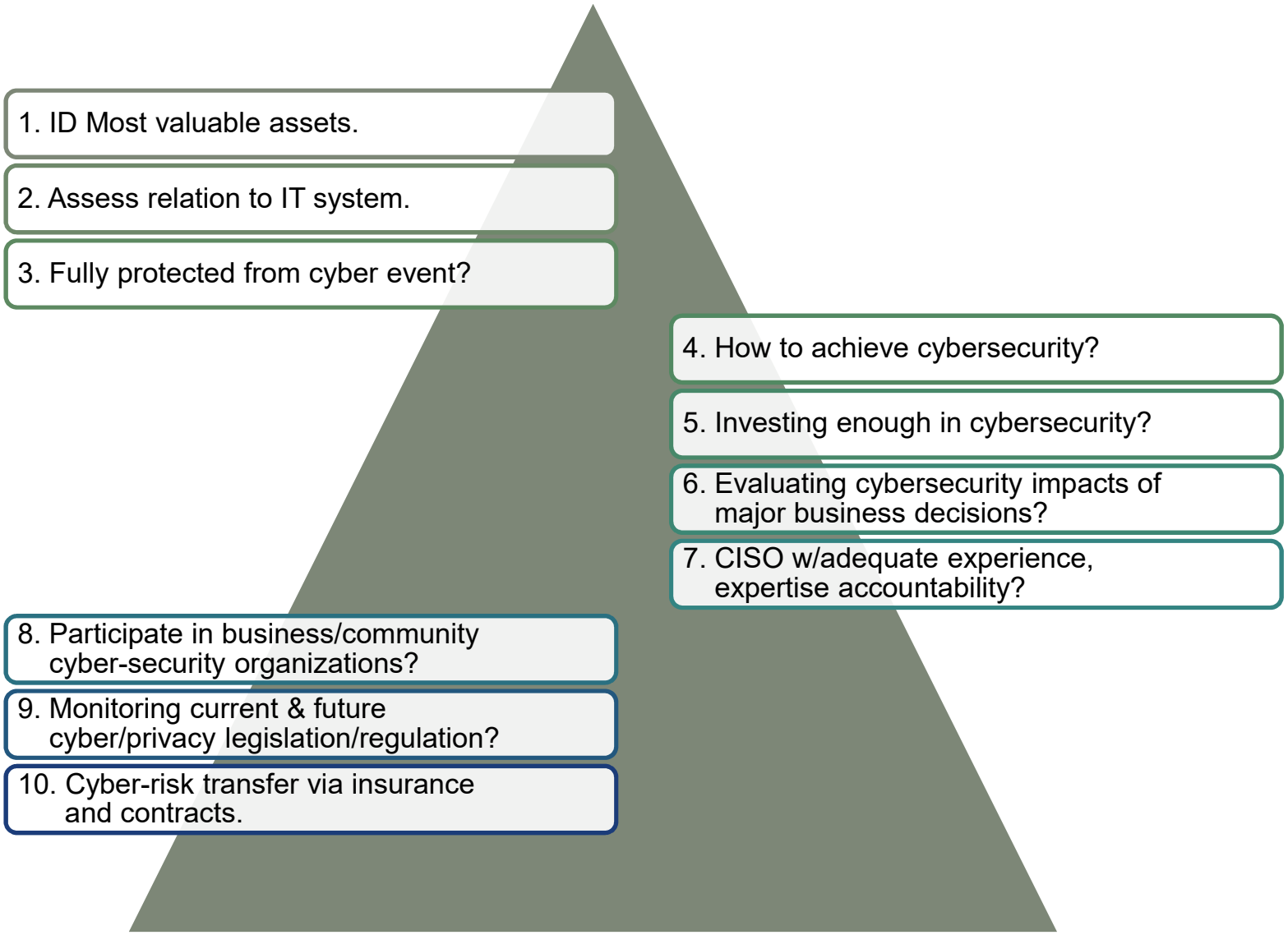
- Derivative suit filed against Wendy's alleging:
  - breach of duty of loyalty, care and good faith for failing to implement adequate cybersecurity measures
  - violation of PCI DSS
  - demand futility b/c D&Os own a controlling interest in Company

YAHOO! Derivative Suit January 2017

July 2016	• Verizon announces plans to buy Yahoo, Inc.'s web assets for $4.83 billion in cash
September 2016	• Yahoo confirms data associated with at least 500 million user accounts were stolen in 2014
December 2016	• Yahoo confirms data associated with more than 1 billion user accounts was compromised in August, 2013 – largest data breach in history
December 2016	• Verizon requests repricing due to MAE
January 2016	• SEC investigation announced January 23 • Derivative lawsuit filed January 24
February 2017	• Verizon and Yahoo agree to reduce price by $300 million (rumored)

NACD 5 KEY OVERSIGHT STEPS

NACD QUESTIONS TO ASSESS CYBER LITERACY



BOARD RESPONSIBILITY FOR CYBERSECURITY

- Policy Approval
- Review and Address Risk Assessment Results
- Oversee Strategic Roadmap & Risk Treatment Plan
- Review Audit & Assessment Reports
- Review Results of Incident Response Readiness Testing
- Funding for Cybersecurity & Privacy Programs
- Approve and Fund Hiring & Training Plan
- Determine Cyber Insurance Coverage Needs
- Promoting a Culture of Compliance
- Promoting a Cybersecurity Aware Culture
- Accountability of Sr. Leadership
- Approve Information Security Investments
- Leverage Outside Experts
- Don't Delegate Solely to IT
- Enterprise Risk Committee

EXAMPLES FROM THE FRONT – 1

MM Construction Group

- Small construction company, acquired by larger company.
- Government Contractor – buildings on military bases.
- Government subpoena based on misuse of programs to promote women owned businesses.
- Contents of subpoena only called for production of information-it did not detail allegations
- Submitted as "claim" for a "wrongful act"
- Triggered $2 million policy, including duty to defend.

EXAMPLES FROM THE FRONT- 2

College Book Rentals

Small, private family owned business, wants to be acquired in the future.

Used U.S. Postal Service for shipping.

Dispute with USPS-mostly a contract dispute, but fashioned as a False Claim—for $4.8 million.

H&H secured coverage for defense, saving company hundreds of thousands in legal fees.

Insurer contributed towards resolution of claim for $325,000.

MEET THE TEAM

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