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A Newsletter from Chicago Underwriting Group, Inc.
Underwriters of D & O and Professional Liability Insurance

Issue 94 **September 2014**

In this issue ... *we look at the ongoing D&O liability face-off between plaintiffs vs. defendants, and implications for the D&O insurance market.*

INTRODUCTION

In 1947 a group of Manhattan Project atomic scientists created the Doomsday Clock. They sought to provide an arresting visual demonstration of how close the world has come to a nuclear conflict. The device chosen was a clock, with midnight representing apocalypse; the closer the time was to midnight, as determined by the clock's operators, the more likely there would be a catastrophic nuclear event. In less stressful times the clock has been pushed as far back as 17 minutes to midnight (2002). The closest to midnight was in 1953: 2 minutes. The present setting is 5 minutes, and recent world events have done little to suggest the dangers are reduced.

No graphic image currently exists to demonstrate the ebb and flow in the relative ascendancy of securities class action plaintiffs and their counsel versus public companies, their defense attorneys, and their insurers. If it did, such a relationship might be indicated by a pendulum, swinging from one side to the other, reflective of the changing fortunes of either group. What sort of events and situations might affect that imaginary pendulum?

FORUM SELECTION

When this newsletter last looked at forum-selection initiatives in July 2013, the Delaware Chancery court had decided that forum-selection clauses were valid, pending any appeal to the Delaware Supreme Court. In October 2013 that appeal was dropped, leaving intact the original decision, which generally upheld the right of corporations to enact provisions that predetermined in which jurisdiction they could be sued by their shareholders. Following on from that, a recent Delaware decision indicated that Delaware corporations do not even have to select Delaware as their preferred forum for disputes. In *City of Providence v. First Citizens Bancshares* et al., Chancellor Andre Bouchard decided that the Delaware-domiciled Bank could pick North Carolina for its preferred forum, as it had wished. Being permitted to select a single (and presumably friendly) forum for shareholder disputes can be a huge benefit for corporate defendants in helping to reduce the costs incurred from duplicative, multi-forum lawsuits.

Verdict: two significant gains for the defense. Expect an even greater surge in the adoption of such provisions.

PLAINTIFFS' COUNSEL SHOWN BEHAVING BADLY

According to the Stanford Securities Class Action Clearinghouse, the law firm of Robbins Geller Rudman and Dowd is historically the third most active plaintiff firm in securities class action litigation. But for all its eminence, on August 14, 2014 the firm received a stinging rebuke from Chief Justice Ruben Castillo of the

Northern District of Illinois over the firm's conduct in the case of *City of Livonia Employees Retirement System v. The Boeing Company,* et al.

The court found that Robbins Geller had been using information from a confidential witness that the firm knew to be "unverified and potentially unreliable," yet the firm "made assurances to the court as to the truth of the statements." To quote Chief Justice Castillo: "The information turned out to be blatantly false" … "if counsel had made any attempt to verify the information they would easily have discovered this." Chief Justice Castillo concurred with the Seventh Circuit's characterization of Robbins Geller's behavior as: "ostrich tactics — counsel put their heads in the sand to avoid discovering the truth." While noting the court's general reluctance to formally sanction a member of the bar (and the rarity of such a step), Chief Justice Castillo felt that he "could not ignore plaintiffs' counsel's repeated misconduct throughout this litigation," and while it "gave him no pleasure to issue sanctions" they were in this instance appropriate.

Verdict: a black eye for the plaintiffs' bar. It also illustrates the extraordinary lengths to which plaintiffs' attorneys might go to advance their case.

SECURITIES CLASS ACTION FILINGS

The tally of SCA filings as recorded by the latest Stanford / Cornerstone Report shows the numbers near their historic six-month average. On the surface, this is an apparent swing in favor of issuers, but there are hidden stories:

- Defense costs continue to increase. There may not be more cases, but those that are brought are costing issuers and their insurance carriers a lot more.
- The stock market is at record levels. It is almost axiomatic that a strong stock market diminishes the likelihood of SCA lawsuits: It's hard to conjure up a lawsuit alleging financially damaging wrongful acts when the stock price has increased. A downturn in the market often leads to investors seeking to blame corporate executives for their losses.
- More securities cases are being brought in state courts, and so fall outside the realm of Stanford / Cornerstone's numbers, which only track federal SCAs.
- Merger / Acquisition lawsuits continue to accompany almost every corporate merger or acquisition. If suit is brought in state court, data on such suits are generally not captured by Stanford / Cornerstone.

Verdict: SCAs hold steady, but behind the scenes the D&O market is confronted with claims on a broad front, many of them involving significant amounts.

IS THAT POLICY FOR THE INSURED OR THE LAWYERS?

Defense expenses incurred by issuers and typically paid for by insurers are often shrouded in secrecy. Occasionally, however, a particularly notable instance of astronomical expense payments reaches the news media. Such is the case with MF Global Holdings Ltd., a broker-dealer notorious first, for hiring former New Jersey Governor Jon S. Corzine as Chief Executive, and second, for a spectacular descent into bankruptcy in 2011. Several civil actions against former executives resulted. By August of 2014, some $47 million of insurance funds had been used up for legal defense, leading the bankruptcy judge to impose a "soft cap" of $55 million for defense. A Wall Street Journal article indicated that there are more than $215 million of insurance funds still available, but the defendants had yet to give depositions. Then in a later ruling, the judge reluctantly consented to the executives accessing most of the remainder of the insurance funds. The judge did set aside around $13 million to actually pay for a claim — an amount dwarfed by the cost of defense.

Verdict: When brought to public notice, the magnitude of defense costs can be startling. Often, as in this case, insurers foot the bill.

SUMMARY

Forum-selection victories and stable SCA-filing counts would suggest that issuers' fortunes are on the rise, with the imaginary pendulum swinging their way. The D&O market may gain some relief from these influences, however the full picture is more complex: Lawsuits beyond the federal orbit are still very much in evidence, and the wild card of defense costs remains a continual threat. ❖

Chicago Underwriting Group: A D&O market-maker for more than 30 years

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