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#MeToo—One Year in and the Continuing Impact on Corporations and Their Boardrooms[1]

When Tarana Burke coined the phrase "Me Too" in 2006 as a way to help women and girls of color who had survived sexual violence, she had no idea that the phrase would become a slogan of the anti-sexual harassment movement in 2017. Nor could she have imagined that she would appear on the cover of TIME Magazine's 2017 Person of the Year issue as one of "The Silence Breakers" (*TIME*, December 6, 2017). While the #MeToo movement began in earnest in the fall of 2017 with accusations against Harvey Weinstein, Larry Nassar, Kevin Spacey, Roy Moore, Matt Lauer, and Garrison Keillor and ended 2017 with allegations against Al Franken, Woody Allen, and Mario Batali, the movement was just getting started.

2018 began with the formation in Hollywood of an anti-harassment coalition called Time's Up and the cascade of allegations continued with the fall from grace of James Levine (Metropolitan Opera), Michael Ferro (Tronc), R. Kelly, Les Moonves, and more ("#MeToo Timeline of Events," *Chicago Tribune*, December 6, 2018). While the individuals allegedly, and sometimes admittedly, involved in these transgressions sustained significant impacts to their lives and livelihoods, their companies as well as their insurers have also paid a steep price for their misdeeds and the alleged misconduct of management in allowing the bad behavior. While sexual misconduct-based cases are only one segment of an expansion of exposures to directors and officers and their insurers, these cases clearly played a significant role in the directors' and officers' (D&O) and employment practices liability (EPL) worlds in 2018 and can be expected to continue to do so for the foreseeable future.

I. Current D&O Landscape

To understand the impact of the #MeToo movement on the D&O world, it is helpful to have some context on other types of claims impacting corporations, their directors and officers, and their insurers.

[1] Any opinions expressed are not the opinions of any individual speaker and/or their employers.

A. Securities Class Actions

While the number of securities class action lawsuit filings remained at near record levels in 2018, the number of lawsuits filed in various categories continues to shift. Federal court filings remained high at 412 which is 210% above the average annual filings from 1996-2006. (*See*, "The Top Ten D&O Stories of 2018," *The D&O Diary*, January 7, 2019.) Even these high numbers of federal court filings are not a full representation of the actual number of cases filed since the number of state court actions filed has increased significantly in the wake of the U.S. Supreme Court's *Cyan* decision which held that state courts retain concurrent jurisdiction for cases involving alleged violations of the Securities Act. *Cyan, Inc. v. Beaver County Employees Retirement Fund*, 583 U.S. __, 2018 WL 1384564, (March 20, 2018). This movement to state courts makes it more difficult to track the total number of filings. Whether filed in federal or state court, it is clear that while the number of filings continues to be high, the types of conduct at issue in litigation against corporations is more varied than has previously been the case.

In addition to the record number of filings, industry observers are concerned about the rate of filings. The high number of filings combined with a reduction in the number of public companies has significantly increased the chance that a public company and its directors and officers will be sued. In 2017, the likelihood that a public company would be sued in a securities class action rose to 8.4%, doubling the rate since 2004. (Coffee, John C., "Securities Litigation in 2017: 'It Was the Best of Times, It Was the Worst of Times,'" *The CLS Blue Sky Blog*, March 19, 2018.) In the first half of 2018, the high frequency rate continued with the risk of being sued at 8.5%. (Dailey and Marder,"The rise in event-driven securities litigation—Why it matters to directors and officers," *WillisTowersWatson.com*, November 12, 2018 citing to Cornerstone Research Securities Class Action Filings—2018 Midyear Assessment.) As discussed below, these figures still include a significant number of traditional filings but increasingly are based on merger objection and event-driven securities litigation.

1. Continued Reduction in Actions Based on Financial Restatements

Securities class action litigation has historically been primarily related to financial or accounting misrepresentations. Traditional accounting-based allegations typically relate to "revenue recognition, improper allowance for losses, delayed asset impairment, or other violations of generally accepted accounting principles." (Dailey & Marder, *supra*.) This landscape has changed as the number of corporations announcing financial restatements continues to decline. In 2017, the number of restatements hit a 17-year low. (*See*, "The Top Ten D&O Stories of 2018," *The D&O Diary*, January 7, 2019.) With fewer restatements to serve as the basis for alleged management misdeeds, the types of cases being filed are changing to adapt to the altered landscape.

2. Mergers are Still Driving Large Numbers of Filings

A significant factor in the number of securities lawsuit filings continues to be federal court merger objection lawsuits filed as class actions under federal securities law. Any public company merger or acquisition is likely to be followed, often almost immediately, by a merger objection action. This trend that began in the mid-2000s and has been a focus of the D&O industry for the past decade continued in 2018 with merger objection lawsuits representing 46% of the federal court securities class action filings. (*Id*; *see also*, Coffee, *supra*, noting that 48% of 2017 filings were merger objection cases, up 17% from 2016.) Although not the focus of this discussion, it is important to recognize that merger objection actions remain a huge driver in any current evaluation of corporate liability and D&O trends.

B. Event-Driven Securities Class Actions and Derivative Litigation

While merger objection actions may represent the largest segment of securities class action cases, the trend to watch is clearly event-driven cases. These are cases "filed in response to adverse company events, such as a data security breach, sexual harassment allegations, an explosion, allegations that a drug or product has side effects or has caused injury, or a regulatory or enforcement action." (Dailey, *supra*.)

Most who operate and/or compete in the D&O arena are regular readers of *The D&O Diary*, an almost daily blog authored by Kevin LaCroix. Mr. LaCroix is a broker so one may not always agree with his viewpoint depending on your own, but most will agree that he is a keen observer of the D&O world. In his post "The Top Ten D&O Stories of 2018," he recognizes "event-driven securities suits" as one of those top ten stories. Identifying these suits as "a serious and growing problem," LaCroix attributes the growing number of these actions, at least in part, to the significant reduction in financial restatements by corporations. He suggests that with fewer accounting scandals to be exploited as the basis for securities lawsuits, some creative plaintiffs' lawyers are "focused on pursuing securities suits filed against companies whose share prices have declined following a significant disruptive event in the company's operations." LaCroix identifies these event-driven lawsuits as "a significant factor in the heightened level of securities class action filings in 2018."

The events behind the lawsuits filed in 2018 are quite varied but all relate to a significant event which allegedly caused a decline in share prices. These cases allege mismanagement and breach of fiduciary duties in the operation of a business resulting in damage to shareholders. Commentators have noted that these cases are being litigated by a group of firms that, prior to 2009, had a very small percentage of the federal securities class action market (6%) but now represent over 40% of the filings. (Dailey, *supra*, citing to postings by Coffee and LaCroix.) Many of the events at issue in this litigation relate to business or operational risks subject to a company's risk disclosures and allege that the risk was downplayed or under-disclosed. These event-driven cases have a much higher dismissal rate than more traditional filings—almost 60%—but that does not eliminate the cost of such actions to the companies and their insurers. (*Id*, citing to Cornerstone.) This also means that 40% of filings survive motions to dismiss.

In addition to the cases alleging sexual misconduct (discussed below), key events resulting in litigation for companies and their directors and officers have included:

- Mine explosion (2010) resulting in deaths and subsequent conviction of CEO, *In re Massey Energy Co., 2011 WL 2176479*, (Del. Ch. May 31, 2011). Alleged false and misleading statements during the class period about commitment to safety and safety initiatives.
- BP Deepwater Horizon explosion (2010), *In re BP p.l.c. Securities Litigation*, No. 10-MD-2185 (S.D. Tex.). Alleged to have misstated the effectiveness of its safety procedures prior to the spill thereby minimizing the risk of catastrophic failure.
- Failure of or injury from a product, *e.g.* Zicam Cold Remedy, *Matrixx Initiatives, Inc. v. Siracusano*, 133 S. Ct. 1309 (2011).
- Early data breach cases did not survive dismissal. *See* Wyndham Worldwide, Target, and Home Depot litigation (2014-2016).
- Federal raid to seize evidence after statement company "believed" it was in compliance, *Omnicare, Inc. v. Laborers Dist. Council Constr. Indus. Pension Fund*, 135 S. Ct. 1318 (2015).
- Climate change-based litigation, *Ramirez v ExxonMobil*, (NDTX, 2016). Alleged that the company knowingly understated publicly its internal view of the potential impacts of climate change on its ability to realize the value of its hydrocarbon assets.
- Greenfell Tower fire in London, *Brave v. Arconic, Inc.,* (SDNY, 2017). Alleged that Arconic knowingly supplied highly flammable product without warnings increasing the risk of property damage and injury.
- Another product case, *Hall v Johnson & Johnson*, (DNJ, 2018). Alleges that J&J knew for decades that cancer causing asbestos was present in the talc in its baby powder.
- More federal investigations and search warrants in 2017—USANA (sued based on disclosures in an FCPA investigation) and Caterpillar (sued after multiple federal agencies executed a search warrant at headquarters).
- Data breach-related securities litigation sees first major settlement against Yahoo in March 2018.
- More climate change-related management liability—California wildfire cases filed in November 2018 against electrical utilities, Edison International and PG&E.
- New data breach securities suits filed following Yahoo settlement in 2018 ending with filing against Marriott for breach of Starwood reservation system.

See the articles, *supra*, by LaCroix, Coffee, and Dailey & Marder, for further details and analysis of these categories of event-driven securities litigation.

II. #MeToo Cases in Review

A. Time's Up—No More Silencing/Tolerating/Ignoring Abuse

While all of the other categories of event-driven litigation draw their fair share of attention, the cases arising from alleged sexual misconduct are naturally headline material given the nature of the allegations and the high level executives and numerous celebrities implicated. Of course there were sexual misconduct cases before the #MeToo movement got underway in earnest—think Bill Cosby for instance and numerous politicians—but there is a whole new level of awareness and intolerance. Now allegations alone may sideline an individual and a series of

credible allegations can bring down not only an individual but a whole organization. There can be little doubt that Ashley Judd's allegations in the New York Times against Harvey Weinstein in early October 2017 and the cascade of allegations against him that followed opened a Pandora's box that will never be closed. There is no going back and organizations that don't change are sure to pay a heavy price for their bad behavior.

B. D&O Market Impact

In an early 2018 article, Professor Coffee of Columbia Law School predicted that the scope of event-driven litigation experienced in 2017 could expand rapidly. He suggested that the two "nightmares" in particular for which corporate boards have no answer are cybersecurity and Weinstein-style sexual harassment claims. (Coffee, *supra*.) It should come as no surprise that Professor Coffee was right. After his March 2018 article, The D&O Diary posted numerous blogs dedicated to D&O issues related to sexual misconduct in 2018 including:

- "Sexual Misconduct and D&O Claims" (April 11, 2018)
- "Sexual Misconduct Claims: How Charitable is Your D&O Policy?" (April 19, 2018)
- "Michigan State Agrees to Pay Sexual Assault Victims $500 Million" (May 16, 2018)
- "Investor Files Sexual Misconduct-Related Securities Suit against CBS" (August 28, 2018)
- "Nike Board Hit with Sexual Misconduct-Related Derivative Suit" (October 30, 2018)
- "Dismissal Motion Denied in Sexual Misconduct-Related Securities Suit" (December 12, 2018)

In his annual "What to Watch Now in the World of D&O" blog posted on September 4, 2018, Mr. LaCroix asks "Will the #MeToo Movement Lead to Further Management Liability Litigation?" His discussion tracks the initial efforts to hold wrongdoers liable to the efforts to "hold boards and corporate management who permitted the behavior or turned a blind eye responsible." The first of these cases filed in late 2017 was against 21st Century Fox with allegations that the company tolerated a long-standing culture of sexual harassment and misconduct by high-profile media personalities. This derivative lawsuit ultimately settled in 2018 for $90 million reportedly funded by the company's D&O insurer.

Subsequent lawsuits include derivative and securities class actions lawsuits against Wynn Resorts, National Beverage Corp., CBS, Papa John's, and Teladoc Health. All of these cases were based on allegations of sexual misconduct against the CEO and/or other executives of public companies. As noted above with 21st Century Fox, these allegations are not limited to the conduct of the individuals directly involved but also assert tolerance of long-standing cultures and behavior of sexual harassment and other sexual misconduct.

The most recent cases against a major publicly traded company are two derivative actions against the board of Alphabet based on allegations of alleged sexual misconduct at the company's Google unit. *Northern California Pipe Trades Pension Plan v. Hennessey*, San Mateo Superior Court, (January 9, 2019) and *Martin v. Page*, San Mateo Superior Court, (January 10, 2019). As reported in *The D&O Diary*, both actions assert claims for breach of fiduciary duty, unjust enrichment, and corporate waste. The complaints allege a "culture of concealment"

relating to "a long-standing pattern of sexual harassment and discrimination by high-powered male executives." The complaints assert that the "pattern of concealment" was "intended to protect the Company's top earning executives and the Board." (LaCroix, "Alphabet Board Hit With Derivative Suits Over Alleged Sexual Misconduct at Google," *The D&O Diary*, January 13, 2019.) These actions were fueled by articles in the *New York Times* (October 25, 2018) and the *Wall Street Journal* (November 1, 2018) which reported that credible allegations against senior Google executives did not result in firing for cause but rather in "significant and wasteful exit packages" which hid the "true reasons for their departure." These reports led to a mass walkout of Google employees worldwide on November 1, 2018. The complaints allege extreme conduct including human trafficking and that the board was "directly involved in and approved" the severance packages and made a "conscious and intentional decision to conceal the sexual harassment at Google." (*Id*.) In addition to allegations of sexual misconduct, the Alphabet/Google litigation also references the data privacy breach and that the board "hid the breach from the public and from Alphabet shareholders."

As litigation against the Weinstein Company shows, private companies are not immune from litigation and demise based on allegations of sexual misconduct but, in that instance, the suits against the company and its executives were by alleged victims rather than investors. (*Id*.) Not for profit organizations and public institutions are also experiencing litigation resulting from sexual misconduct allegations with the most notable being Michigan State University, United States Olympic Committee, and USA Gymnastics, all related to the allegations against Larry Nassar. Another non-profit organization impacted by this type of litigation is The Metropolitan Opera.

The theories of the D&O claims arising out of sexual misconduct are evolving. For instance, the allegations against Nike are more about a hostile work environment than specific allegations of sexual misconduct. Four legal theories found in the early claims are:

- Breach of duties of care and loyalty when corporate executives engage in sexual misconduct putting the company's resources and reputation at risk;
- Failure of management to monitor harassment at their companies making them liable under a *Caremark* theory;
- Management turning a blind eye or otherwise enabling harassment to continue; or
- Violation of securities laws by making misleading statements about workplace sexual misconduct.

("Sexual Misconduct and D&O Claims," *supra*, referencing Hemel and Lund, "Sexual Harassment and Corporate Law," March 22, 2018.)

It is too early to fully understand the impact these cases will have on the D&O market. What we do know is that many of the litigated cases have survived the motion to dismiss stage and are moving forward. It will take some time to determine whether this genre of event-driven securities litigation will have a greater success rate than event-driven litigation in general. We do also know that, whether dismissed or not, these cases can be very expensive for organizations and their insurers to defend and can have devastating impacts on the future of an organization and the individuals who are the subject of the misconduct allegations.

C. EPL Impact

Employment practices liability claims and coverage are a distinct aspect of management liability claims related to sexual misconduct. The Equal Employment Opportunity Commission (EEOC) has a significant role to play in these claims and how they develop and are managed by organizations and their insurers.

1. EEOC

EPL claims often begin with EEOC charges and EEOC filing activity has been very high since the dawn of the #MeToo movement. Sexual harassment charges filed with the EEOC increased by 12% in FY 2018 while the number of total charges remained about the same meaning that the percentage of sexual harassment charges also increased as compared to other categories of charges. Reasonable cause findings and successful conciliations also increased over FY 2017. Title VII (discrimination) claims accounted for 55% of all EEOC filings with sex-based discrimination comprising 74% of Title VII filings. (Golden, Ryan, "EEOC sexual harassment suits jump more than 50% in 2018," *HRDive.com*, October 8, 2018.)

In addition to an increase in sexual harassment charges filed *with* the EEOC by employees, there was a more than 50% increase in the number of sexual harassment lawsuits filed *by* the EEOC in FY 2018. *(Id*.) This shows that the EEOC focus on sexual harassment litigation has not waned in spite of expectations by many observers that things might change after the 2016 election.

The EEOC has also been quite active with new guidelines and plans, some of which pre-date the #MeToo movement. In June 2016, the EEOC published a report of the Select Task Force on the Study of Harassment in the Workplace. This report has numerous recommendations regarding studying the prevalence of harassment in the workplace, workplace leadership and accountability, prevention policies and procedures, anti-harassment compliance training, workplace civility and compliance training, and outreach. In November 2017, following up on the report of the Select Task Force, the EEOC published "Promising Practices for Preventing Harassment," which includes many specific guidelines to address the recommendations of the Task Force report. As with many federal agencies under the Trump administration, several top positions at the EEOC remain vacate but, interestingly, the authors of the Select Task Force Report are currently the Acting Chair and one of the Commissioners of the EEOC. In February 2018, the EEOC published its Strategic Plan for 2018-2022, restating its commitment to prevent and remedy employment discrimination through EEOC's law enforcement authorities and to prevent employment discrimination and promote inclusive workplaces through education and outreach. (All EEOC publications are easily located on its website at eeoc.gov.) It is too soon to tell how the new strategic plan will implement "the strategic application of EEOC's law enforcement authorities" in the current potentially competing political and social environments.

2. EPL Claims

It is likely too soon to determine the full impact of the #MeToo movement on EPL claims but at least one large insurer has been reported to have seen a 50% increase in sexual harassment claims since the Harvey Weinstein story broke in October 2017. (Weintraub, Mark,

"Employment practices liability claim trends," *Lockton.com*, May 2018.) Another insurer reports that claims with a retaliation component, often following an allegation of sexual harassment, account for more than 40% of all EPL claims. (Hemenway, Chad, "Underlying trends keeping EPL underwriters busy," *advisenltd.com*, April 18, 2018.)

As seen from the discussion above, there are a number of allegations which can arise out of sexual harassment other than the actual sexual harassment claim. Sexual harassment lawsuits often come with claims of retaliation and may also present allegations of assault, battery and, more rarely, false imprisonment. Other allegations associated with sexual harassment are negligent hiring and/or retention, negligent supervision, failure to follow internal procedures, or deprivation of career opportunities. There may also be claims of negligent infliction of emotional distress, mental anguish, and humiliation. Which of these allegations present covered Loss under an EPL policy is not a new issue for EPL insurers and claim representatives. They are adept at addressing issues and exclusions relating to bodily injury, intentional acts, and criminal proceedings and the potential for coverage under general liability for some alleged acts and even some potential D&O or cyber coverage issues. (See, Scheiner and Broda, "EPL Claims: Changing Norms and New Legislation in the #MeToo Era," *The D&O Diary*, August 23, 2018.) However, the new range of allegations presented against individuals and companies for their behavior in the wake of the #MeToo movement may require more analysis of which policies, if any, provide coverage for certain allegations and how defense and indemnity costs will be allocated.

D. Legislative Impact

In addition to increased activity at the EEOC, there have been a number of state legislative responses to the increased awareness of sexual misconduct in the workplace. For example, New York Human Rights Law Section 296-D (effective April 12, 2018) makes it unlawful for an employer to permit sexual harassment of non-employees in its workplace and the employer may be held liable for such conduct when it knew or should have known about the harassment and took no action to prevent it. On September 30, 2018, California enacted legislation requiring public companies to have at least one woman on their board of directors. (CA Corporations Code, Section 301.3) NJ Bill S121 (under consideration) would bar non-disclosure agreements in employment contracts relating to claims of discrimination, retaliation, or harassment as against public policy.

Other states passing legislation changing the landscape for employers with respect to sexual harassment claims are Vermont, Arizona, and Louisiana. These are just the beginning of the legislative actions we can expect to see from the states. Others relate to expansion of statutes of limitations, new requirements for release agreements, records retention, barring enforcement of arbitration provisions in employment contracts, and more mandatory training.

III. Impact on Corporations and Boards Moving Forward

In a broker publication written by lawyers to advise why event-driven securities litigation should matter to directors and officers, the authors provide the following tips to directors and officers to minimize and mitigate the risk of event-driven litigation:

- Reevaluate public statements about the effectiveness of your practice to avoid allegations of "under-disclosed" risks.
- Ensure all affirmative statements have support.
- Ensure that your insurance coverage does not have gaps. (Dailey & Marder, *supra*.)

With respect to sexual misconduct events specifically, these same authors suggest that the company:

- Take all sexual misconduct allegations seriously and investigate them thoroughly with outside investigators, if necessary.
- Get legal advice on whether the allegations and/or investigation findings should be disclosed, especially if they involve executives or systemic conduct.
- Review relevant public statements, including risk factor disclosures, regarding compliance with the law and adherence to internal standards. (*Supra*.)

A human resources publication for industry professionals notes that the FY 2018 EEOC reports indicate that employees are "more emboldened" to report harassment in the current climate and going to the EEOC to do so and the EEOC's emphasis on sexual harassment litigation has continued. (Golden, *supra*.) This publication suggests that given the likelihood of sex-based discrimination and sexual harassment charges, employers should "take stock of all aspects of their internal process for dealing with harassment, including reporting, handbook composition and investigatory measures." (*Id*.)

Organizations will also have to address and adapt to the new legislative environment. While some of the legislation will have benefits—*e.g.* studies show that corporations with women on their boards perform better by several different measurements—some of the legislated changes will come with implementation and operational costs as well as requiring corporate cultural adjustments.

The history of D&O claims related to sexual misconduct is not new—however, the recent high-profile claims may make it appear that way. What is clear is that there will continue to be more litigation against organizations as well as individuals arising out of sexual misconduct for the foreseeable future. The heightened focus generated by the #MeToo movement and the willingness of victims to come forward as a result will spawn litigation until significant changes occur in organizations and how they are managed. States and the federal government will legislate and regulate to try to ensure appropriate behavior and proper management while corporations adapt to a new era of behavioral scrutiny with all of its implications. Brokers will try to assist their clients in insuring against these risks while insurers continue to analyze their existing products and how to underwrite against risks which may be very difficult to identify and evaluate.