

# The impact of COVID-19 on Directors and Officers insurance

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## Recent adverse trends in securities class action lawsuits and the unprecedented COVID-19 pandemic present challenges for corporate management and their boards.

Inadequate or misleading disclosures in financial statements have attracted the attention of plaintiff attorneys experienced in bringing claims against the management and directors of public entities in the form of securities class action (SCA). These types of claims are generally covered by Directors and Officers (D&O) liability insurance for both the expenses defending such claims and the cost of settlements or verdicts.

The filing of SCAs has been at an all-time high in the 2017-2019 period. More than 400 SCAs have been filed annually compared to fewer than 300 annually in the prior 15 years. The adverse trend can be attributed to several emerging perils, many of them with recently developing legal allegations:

- The **#MeToo movement**, where it has been alleged that boards and companies allowed pervasive environments that made the alleged misconduct possible.
- **Cyber security risks and data breaches**, for which it has been alleged that board and companies did not ensure adequate protections were in place and the associated reputational damage.
- **Environmental, social, and governance (ESG)** failings, which concern the expectations of regulators, investors, and the public about the ability of boards to effectively focus on and address ESG issues.
- **Workplace violence**, where it has been alleged that boards and companies did not adequately prepare for incidents of mass shootings or other forms of workplace violence.

The COVID-19 pandemic is likely to add to the number of SCAs brought against public companies.

We are already aware of two such actions initiated in March 2020. On March 12, 2020, a plaintiff shareholder filed a SCA lawsuit against Norwegian Cruise Line Holdings, Ltd., alleging

that the company was employing misleading sales tactics related to the COVID-19 outbreak. Specifically, the complaint alleges that the defendants made false and misleading statements or failed to disclose that: “(1) the Company was employing sales tactics of providing customers with unproven and/or blatantly false statements about COVID-19 to entice customers to purchase cruises, thus endangering the lives of both their customers and crew members; and (2) as a result, Defendants’ statements regarding the Company’s business and operations were materially false and misleading and/or lacked a reasonable basis at all relevant times.”<sup>1</sup>

Also on March 12, 2020, an Inovio Pharmaceuticals shareholder filed a SCA lawsuit against the company and its CEO based upon the CEO’s statements about the company’s development of a COVID-19 vaccine. The investor as plaintiff alleges that Inovio and its CEO made false and misleading statements in violation of sections of the Securities Exchange Act of 1934.

It is likely that additional SCAs will be brought as fallout from COVID-19 on business results continues to manifest. The following are among the potential allegations.

- There may be allegations concerning inadequate disclosures regarding risks to the organization, including supply chain risks, causing the entity to miss production targets, and the risks to financial results associated with a government mandate to close offices and quarantine employees due to a pandemic or other events.
- There may be allegations concerning inadequate and/or misleading disclosures today about the impact of COVID-19 on operations and financial results.
- There may also be allegations concerning reputational damage related to an entity’s handling of COVID-19 with respect to the personal safety of its employees and third parties with whom they engage.
- A company in extreme financial straits may choose to accept a federal government financial bailout with conditions viewed by investors as too onerous. Investors may allege that in doing so, management and the board violated the best interests of the company.

<sup>1</sup> *Eric Douglas, et. al., v. Norwegian Cruise Lines, et. al.*, United States District Court of Southern District of Florida, Case 1:20-cv-21107-XXXX (entered on FLSD Docket 03/12/2020).

With results from the first quarter of 2020 coming out in late April and May, and the unprecedented challenges presented by the current and future effects of COVID-19, management and directors will need to be cautious with their decisions and consider consequences not presented in prior difficult times.



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