



BDO Annual Accounting Update – SEC Portion

November, 2019

It's our business to be there for you in the

**MOMENTS
THAT MATTER.**

D&O Market Update

D&O Litigation Trends

Top Stories of 2018

1. Securities class action suits filing remain at near-record levels
2. IPO companies Face State Court Securities Lawsuit Risk
3. Event-driven securities suits represent a serious and growing problem
4. Companies experiencing data breaches get hit with securities suits
5. Privacy issues emerge as another area of D&O exposure
6. D&O lawsuits continue to follow revelations of sexual misconduct
7. CA wildfires-related litigation suggest possible direction of future climate change-related D&O claims
8. SEC enforcement action rebounds
9. Social media communications emerge as a source of potential D&O liability
10. The current landscape creates a difficult environment for D&O Insurers



Source: LaCroix, Kevin. "Top Ten D&O Stories of 2018" | The D&O Diary." The DO Diary Jan. 2, 2019

Changing D&O Market Conditions

Summary

We are seeing unfavorable changes in the D&O market that have not existed for more than a decade. These changes are a result of the perfect storm effect of the following colliding conditions:

LITIGATION AT AN ALL TIME HIGH

- **Traditional securities** suits increasing in frequency and severity. Larger settlements on previous accident years suggest the tail is longer than previously predicted.
- **Large opt-out settlements** are reemerging.
- **Merger objection cases** continue and are shifting from state to federal courts.
- **Derivative actions** are increasing in both frequency and severity, and most are not due to bankruptcy.
- **Event-driven** litigation continues to expand in several areas: #MeToo, cyber breaches, social media, privacy, wildfires, products, and safety. Effectively, any bad news can lead to a claim.
- **Aggressive and innovative** plaintiff firms show no sign of relaxing.
- **Supreme Court's Cyan decision**, Section 11 cases can be brought in both federal and state courts. This affects not just IPOs, but any secondary offering.
- **Enforcement actions** in 2018 were nearly triple the amount seen in the previous periods. One-quarter of actions included claims against individuals, most often CEOs and CFOs.
- **Whistleblower** reports and payouts reached record levels in fiscal year 2018.

DECLINING NEW CUSTOMERS

- 5,350 public companies in 2018 versus 7,994 in 2000
- IPOs not making up for M&A consolidations and bankruptcies



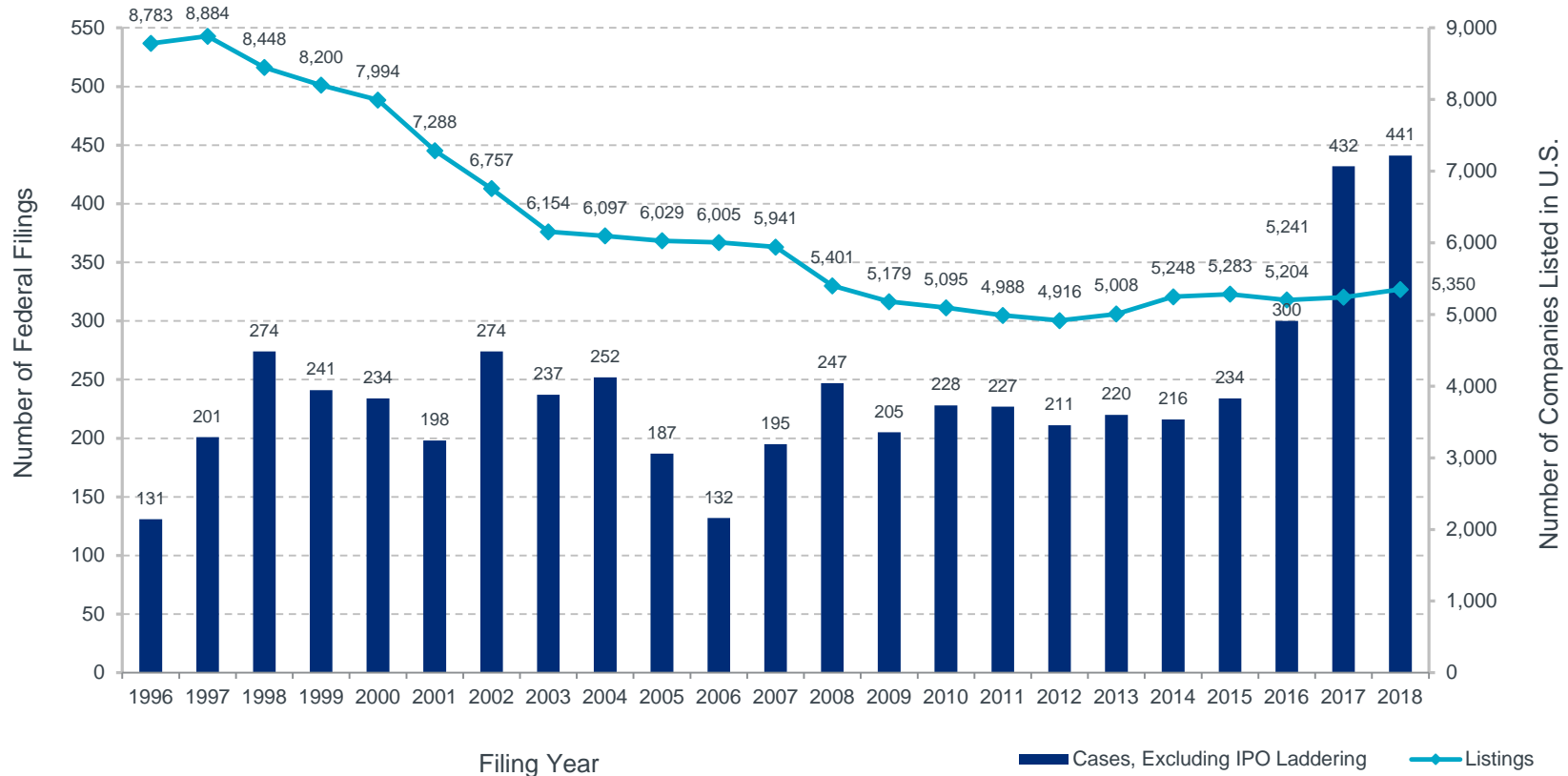
YEARS OF WIDESPREAD PREMIUM REDUCTIONS AND BROADENING COVERAGE "SOFT MARKET CONDITIONS"

- Widespread premium reductions.
- Abundant capacity
- More coverage for less price (coverage kicking in sooner): i.e. Shareholder Derivative Demand sub-limits; Pre-Claim Inquiry Cost Coverage; Investigations Coverage
- New Insurers Not Aggressively Seeking to Grow Market Share by Undercutting Premiums



**Inadequate
insurer pricing
for risks
assumed and a
push for
material
increases**

Federal Filings and Number of U.S. Listed Companies

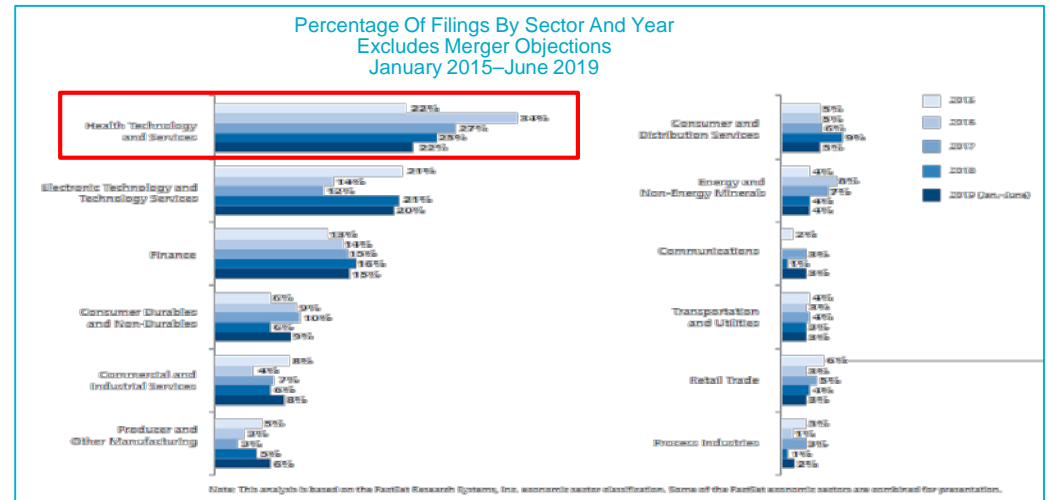
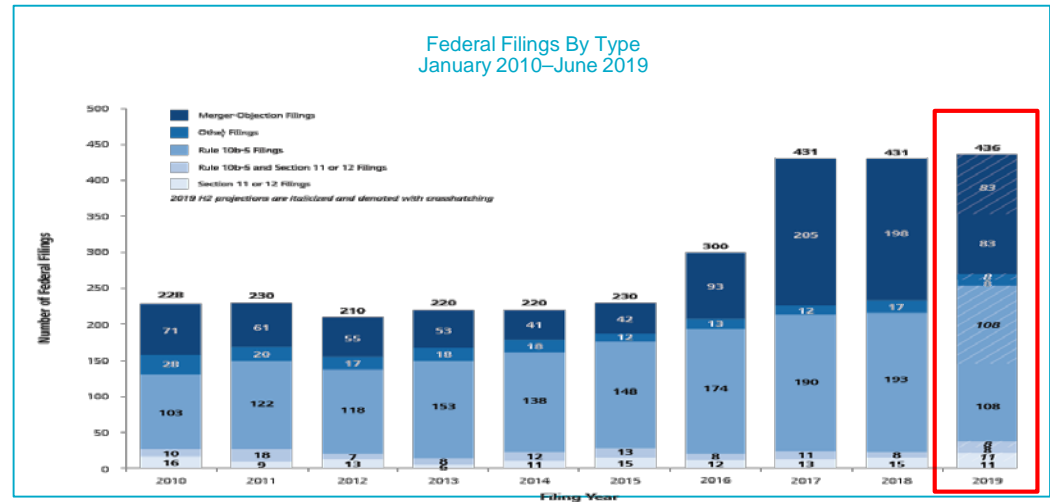


Note: Number of companies listed in US is from Meridian Securities Markets; 1996-2014 values are year-end; NERA - 2017 is as of November .
 Source: NERA, Recent Trends in Securities Class Action Litigation: 2018 Full-Year Review, January 2019

Securities Litigation Trends

Frequency of Securities Claims

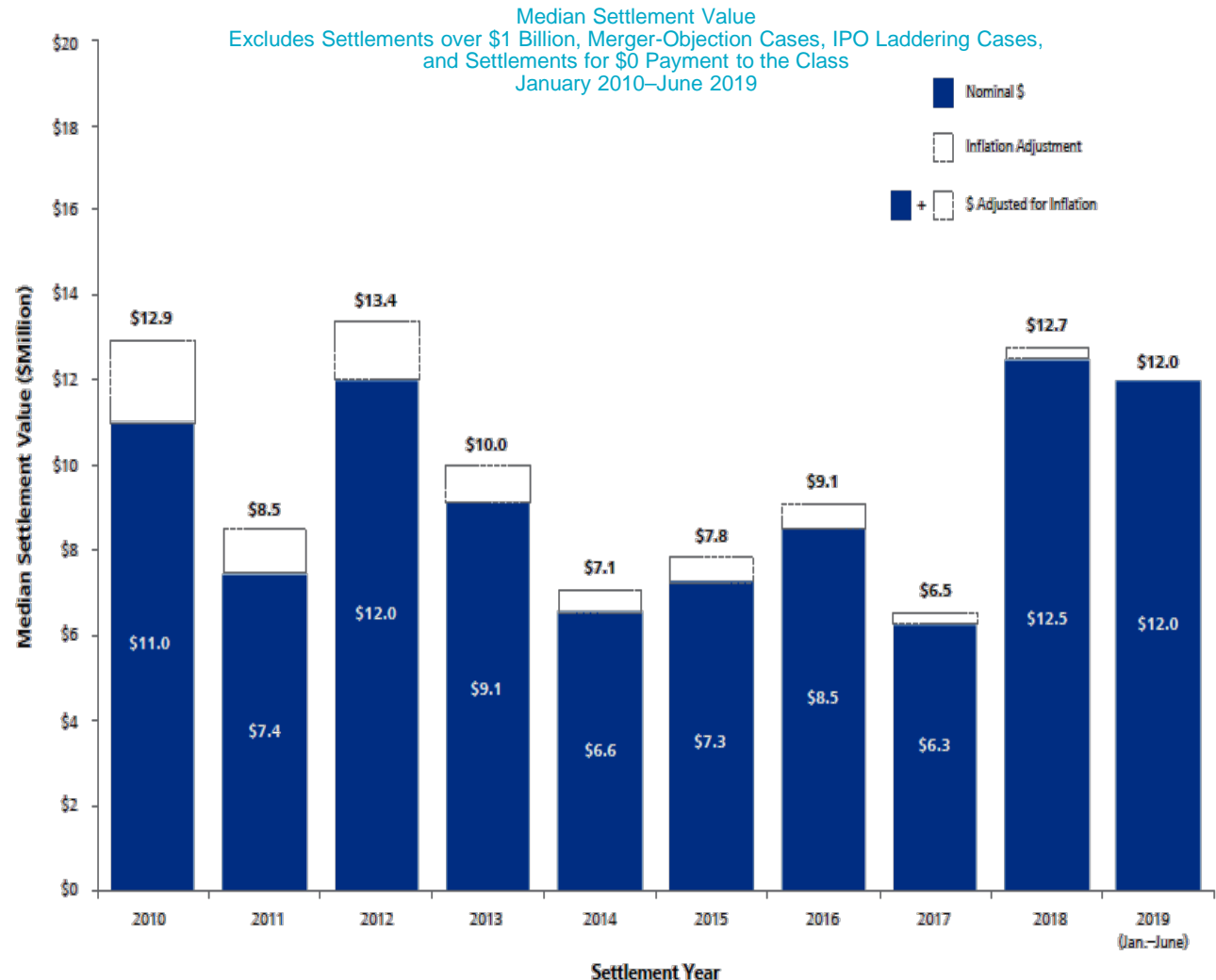
- 2018 Full Year:** The pace of securities class action filings in 2018 was the highest since the aftermath of the 2000 dot-com crash with 441 new cases being filed in US federal courts.
- Merger Objection Suits:** While merger objections constituted about half the 2018 total, filing growth of such cases slowed versus 2017, indicating that the explosion in filings sparked by the Trulia decision may have run its course.
- Rule 10b-5, Section 11, and/or 12:** Filings alleging violations of Rule 10b-5, Section 11, and/or Section 12 of the Securities Act of 1933 ("Securities Act") were roughly unchanged compared to 2017.
- Federal Filings and Number of Companies Listed in the United States:** Approximately 8.2% of all listed public companies were involved in federal class action securities litigation in 2018. The overall risk of litigation to listed firms has increased substantially since early in the decade, when only about 4.0% of public companies listed on US exchanges were subject to a securities class action.
- Filings by Sector:** In 2018 there was a surge in filings against firms in the technology sector, accounting for 21% of the filings in 2018 as compared to 12% in 2017.
- It is extremely rare** for securities class action lawsuits to go all the way through to a jury verdict. Since 1996, there have been more than 5,200 securities class action lawsuits filed, but fewer than 25 cases during that time have gone to trial.



Securities Litigation Trends

Severity of Securities Claims

- **Average Settlement:** In 2018, the average settlement amount jumped to \$69M from \$25M in 2017, largely due to Petrobras settlement.
- **Median Settlement:** In 2018, the median settlement amount also increased from \$6M to \$13M, largely due to higher settlements of many moderately sizes cases, and generally fewer very small settlements.



Source: NERA Economic Consulting (Recent Trends in Securities Class Action Litigation: Q1 2019 Update)

Securities Litigation Trends

Event Driven Litigation

#MeToo Movement:

Greater accountability to hold boards and corporate management who permitted the behavior or turned a blind eye responsible. There have now been a number of management liability lawsuits filed in the wake of revelations of sexual misconduct, and continuing revelations suggest there may be more to come.

Recent Examples:

- 21st Century Fox (*\$90M settlement for Derivative Lawsuit funded by D&O Insurance*)
- Wynn Resorts
- CBS Corporation
- Nike
- Google

#MeToo

Cyber Breach

During the time frame 2014 to 2016, there were a number of shareholder derivative lawsuits filed against companies that had experienced data breaches. These lawsuits were largely unsuccessful. In 2017, there were several more data breach-related D&O lawsuits filed. By contrast to the earlier lawsuits, which were filed as shareholder derivative lawsuits, these later lawsuits were filed as securities class action lawsuits.

Recent Examples:

- Yahoo
- Equifax



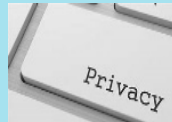
Privacy

Greater focus by regulators into the privacy of data that a company has gathered.

- May 2018 - **General Data Protection Regulation (GDPR)**
- June 2018 - **California Consumer Privacy Act of 2018**

Recent Examples:

- Facebook (Cambridge Analytica)
- Neilson Holdings



Social Media Communication:

The recognition that companies could use social media for company announcements has raised the possibility that an investor could later claim that a company statement on Twitter or Facebook or another social media network could be the basis of a securities class action or SEC investigation. Using social media does involve certain risks.

Recent Example:

- Tesla (Elon Musk)



Products

In recent years there has been a wave of product related failures across a multitude of industries which has resulted in D&O litigation.

Recent Examples:

- Volkswagen (*diesel emissions-cheating scandal*)
- Johnson & Johnson (*personal injury cases regarding baby powder*)
- Intel (*security flaws in its microchips*)
- General Motors (*emission test devices*)



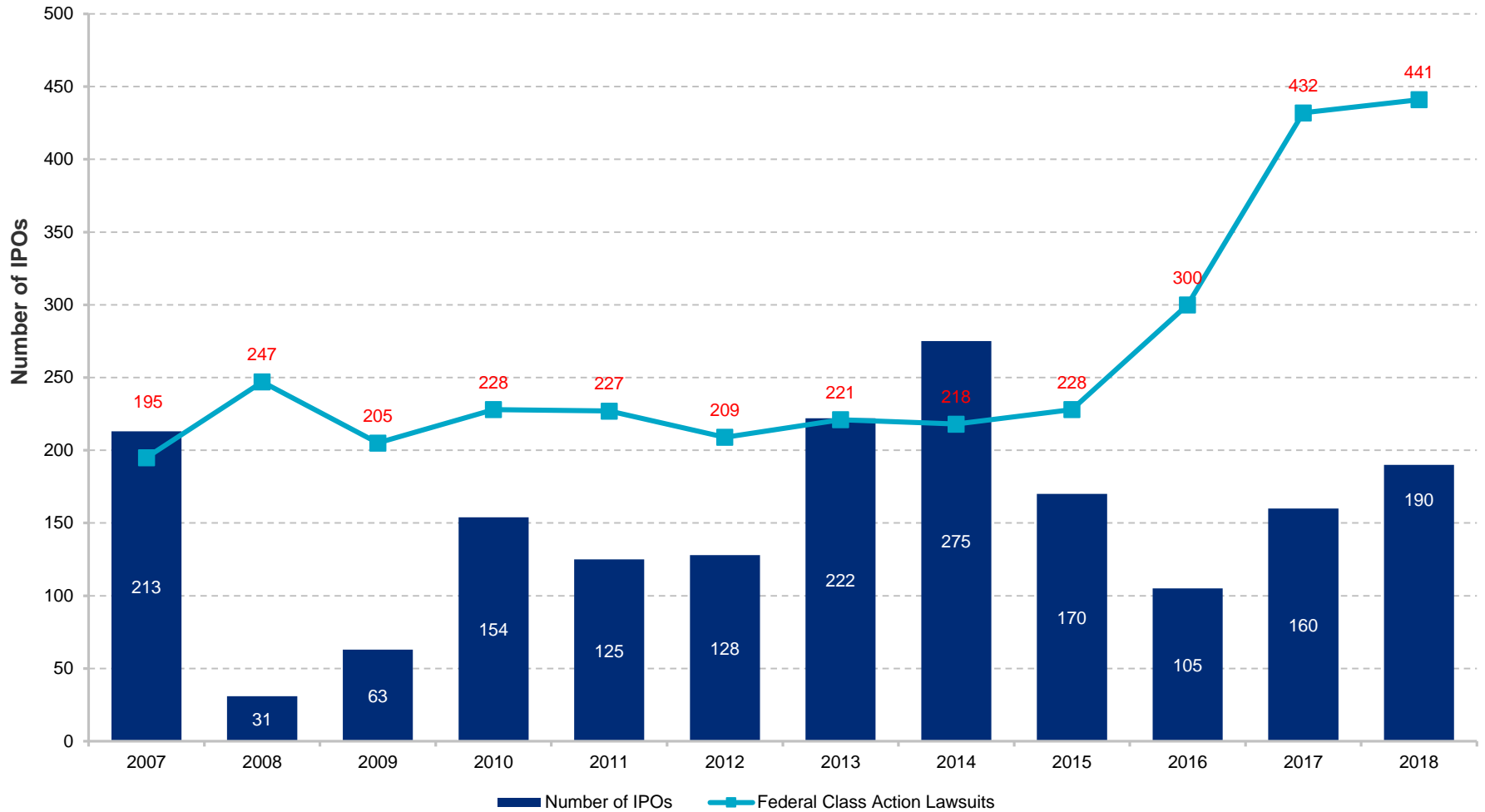
California Wildfires

In November, after the devastating California wildfires, plaintiff shareholders Filed securities lawsuits against Edison International and, separately, against PG&E after news reports that the company's facilities may have caused the wildfires



Source: Marsh Research

IPO Pricing Activity and Number of Federal Class Action Lawsuits



* As of 3/20/2018

Source: **Renaissance Capital - manager of IPO-focused ETFs** renaissancecapital.com/ipohome/press/ipopricings.aspx
 NERA, Recent Trends in Securities Class Action Litigation: 2018 Full-Year Review, January 2019

Securities Litigation Trends

Cyan Decision

Adverse Supreme Court Decision, *Cyan, Inc., et al. v. Beaver County Employees Retirement Fund, et al*

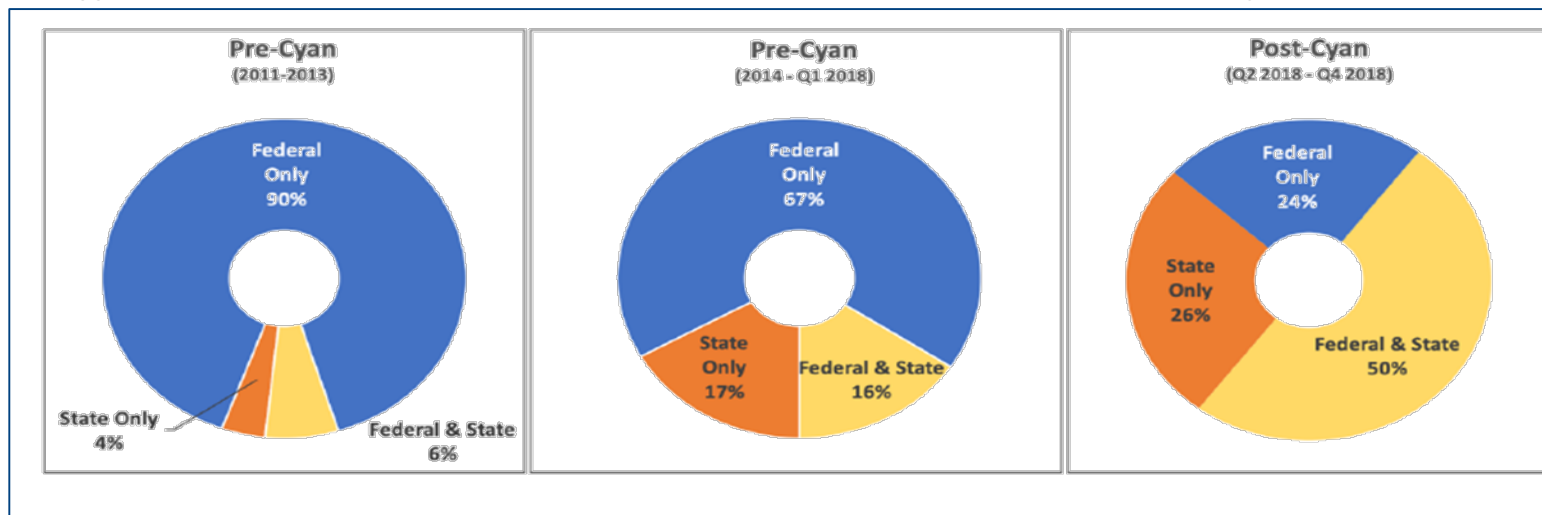
March 20, 2018: *Cyan, Inc. v. Beaver County Employees Retirement Fund*

- The Securities Litigation Uniform Standards Act of 1998 does not eliminate state courts' jurisdiction over Section 11 cases.
- If a company is hit with a 1933 Act securities lawsuit in state court, the company can't remove the state court lawsuit to federal court even if there is a parallel or even identical lawsuit pending in federal court.

Companies undertaking initial public offerings (IPOs) and/or secondary public offerings (SPOs) face the possibility not only of having to litigate claims in both state and federal court, but also face the possibility of having to litigate in multiple state courts at the same time.

Life After Cyan

- *Private Securities Litigation Reform Act (PSLRA)*: not applicable to state cases and as such, defendants don't have the same procedural protections that exist in federal court
- *Judges*: less likely to dismiss cases, very expensive discovery can happen more quickly. Fewer cases were dismissed in state courts vs federal courts
- *The trigger for many state suits*: often the reason stock prices has fallen below the price in the offering



D&O Market Trends

IPO Activity Leads to Increased Demand for D&O Insurance

- In 2018, 190 companies went public, 30 more companies than 2017; US IPO count rises 19% to 190 Deals, proceeds up 32%
- 10 IPOs Raise \$1 Billion or more
- The best performing IPOs of 2018 were mostly healthcare, with four biotech and two medical device companies

Offering value and volume of IPOs by quarter Offering value is US \$billions

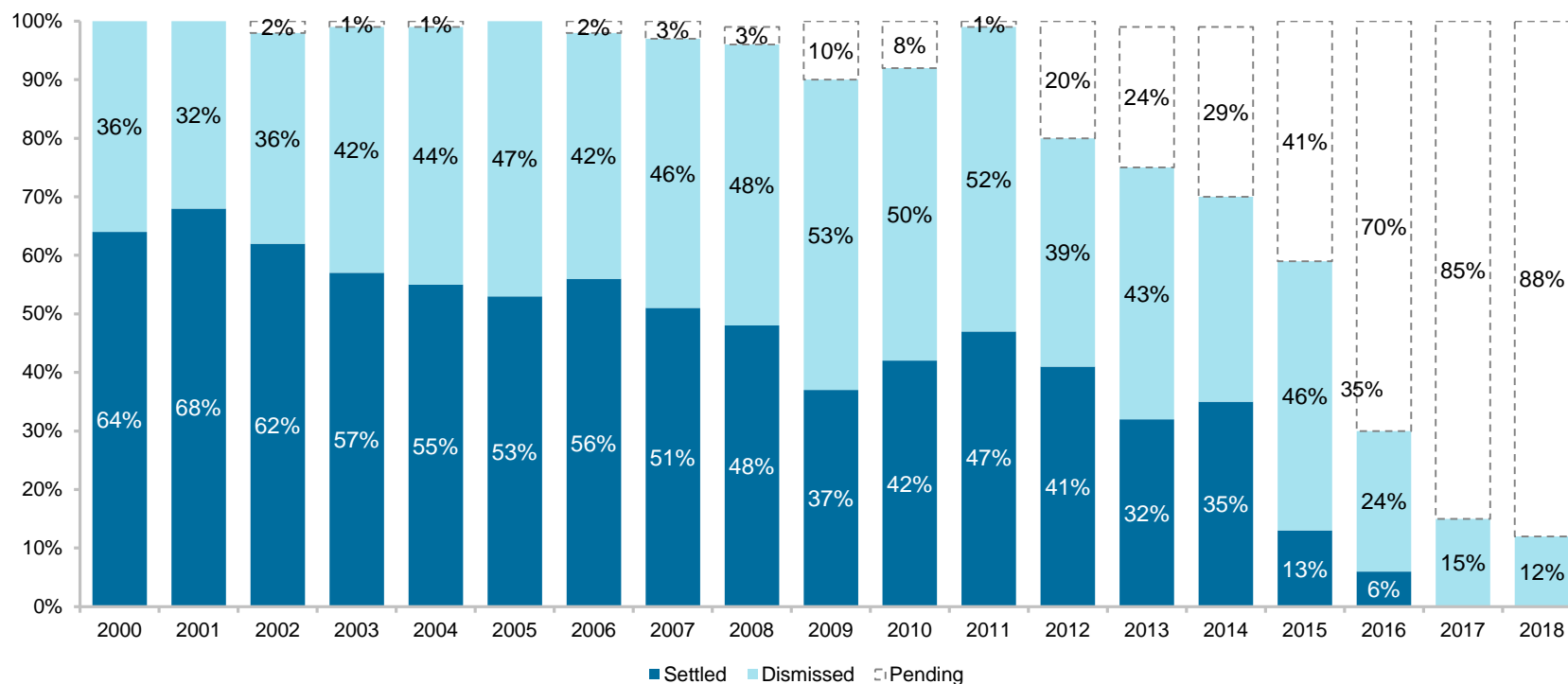


*Value in US \$bn
Source: PwC US Capital Markets Watch

Source: PwC US Capital Markets watch July 2019.

D&O Litigation Trends

Status of Cases as Percentage of Federal Filings by Filing Year

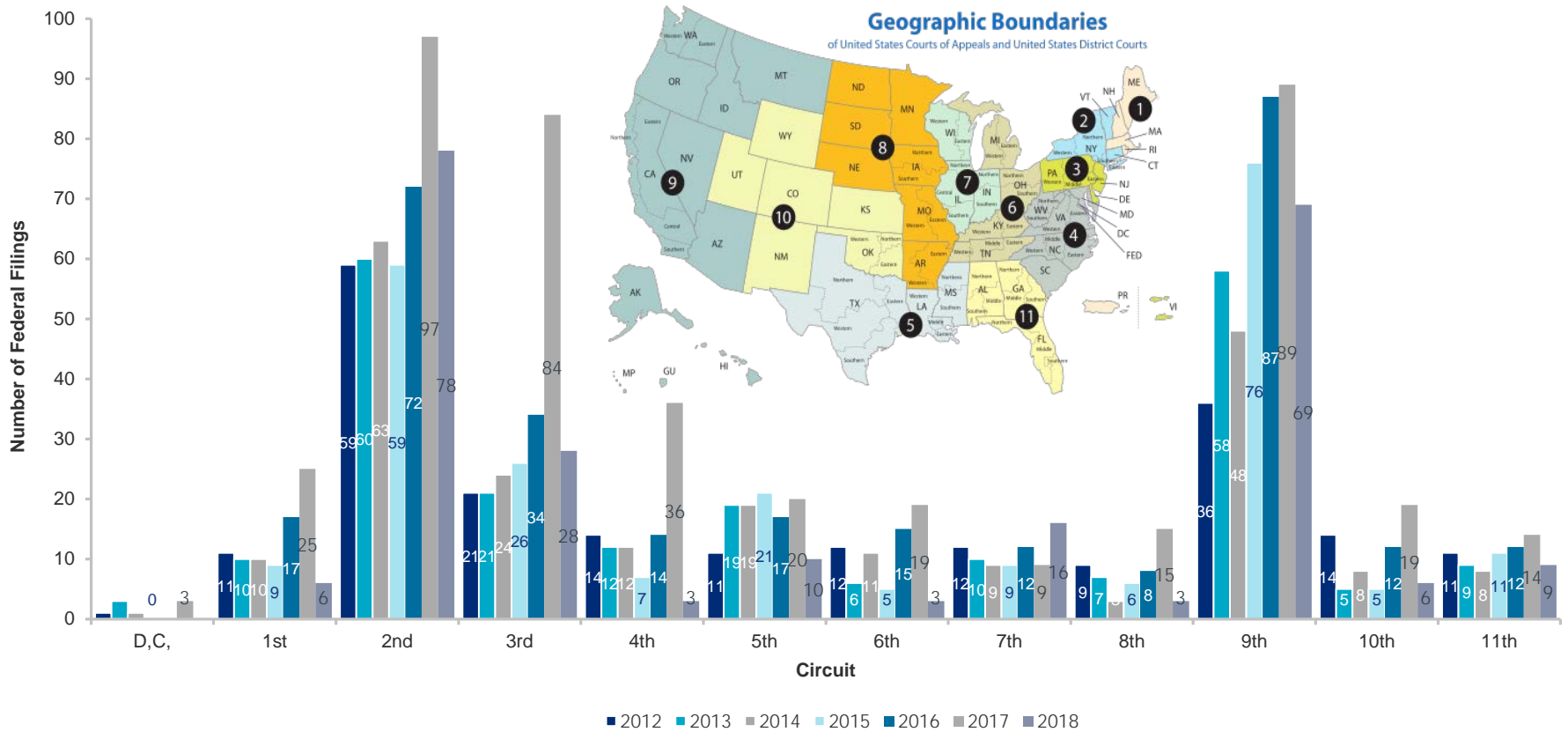


Note: Analysis excludes IPO laddering, merger-objection cases, and verdicts. Dismissals may include dismissals without prejudice and dismissals under appeal

Source: NERA, Recent Trends in Securities Class Action Litigation: 2018 Full-Year Review, January 2019

D&O Litigation Trends

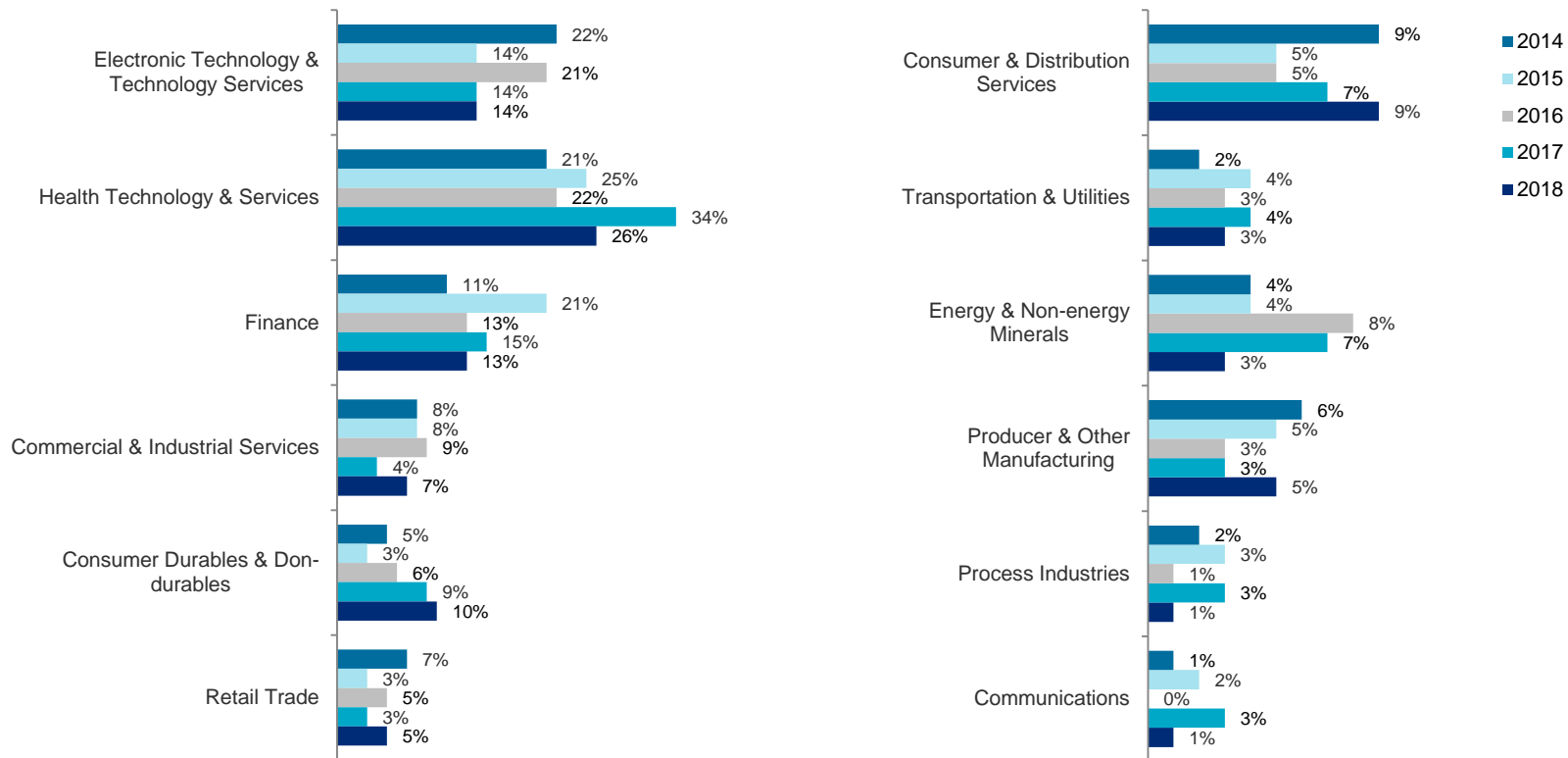
Litigation Activity by Court Circuit



Source: NERA, Recent Trends in Securities Class Action Litigation: 2018 Full-Year Review, January 2019

D&O Litigation Trends

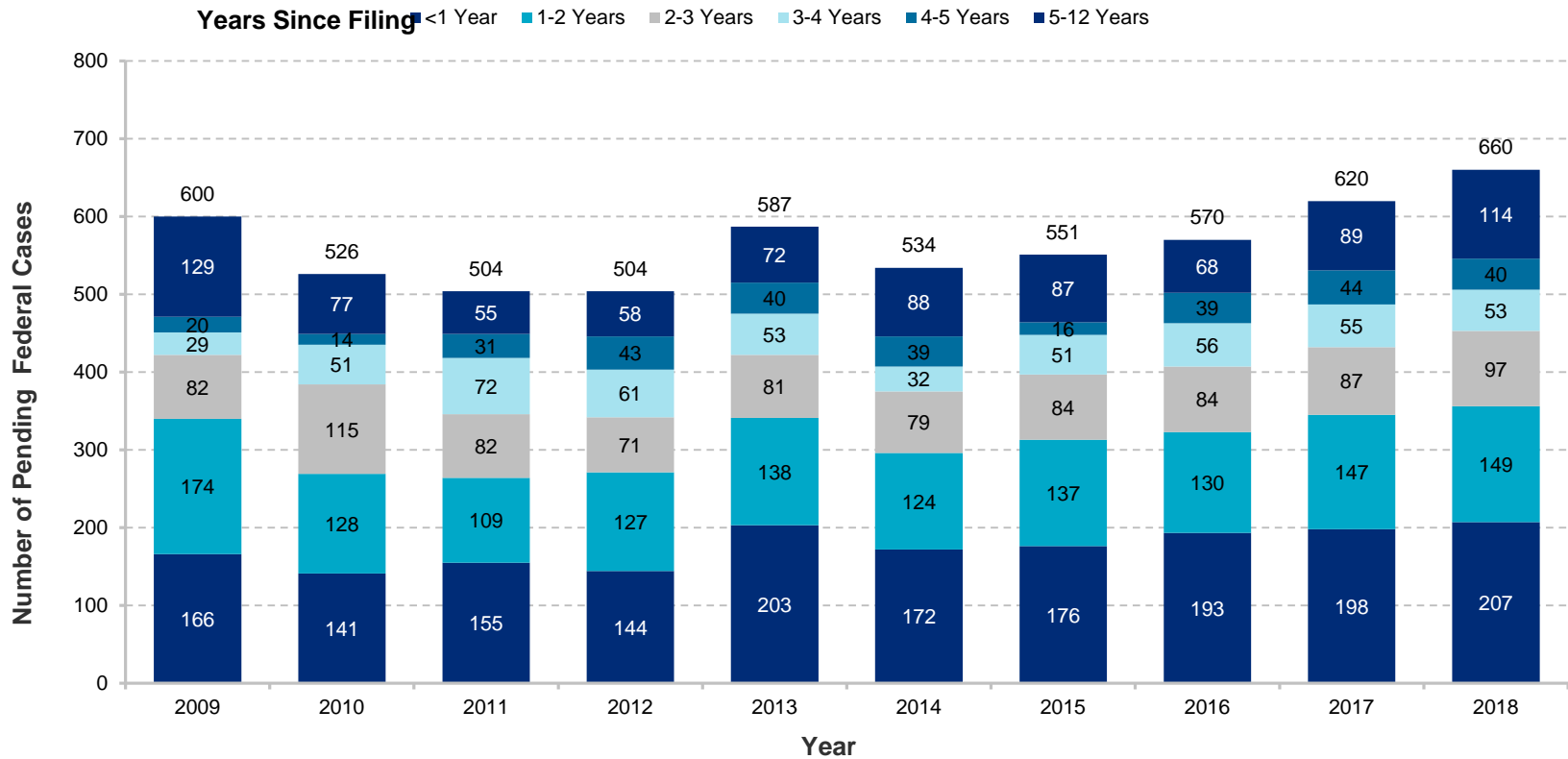
Percentage of Filings by Sector & Year January 2014 – December 2018



Note: This analysis is based on the FactSet Research Systems, Inc. economic sector classification. Some of the FactSet economic sectors are combined for presentation.
Source: NERA, Recent Trends in Securities Class Action Litigation: 2018 Full-Year Review, January 2019

D&O Litigation Trends

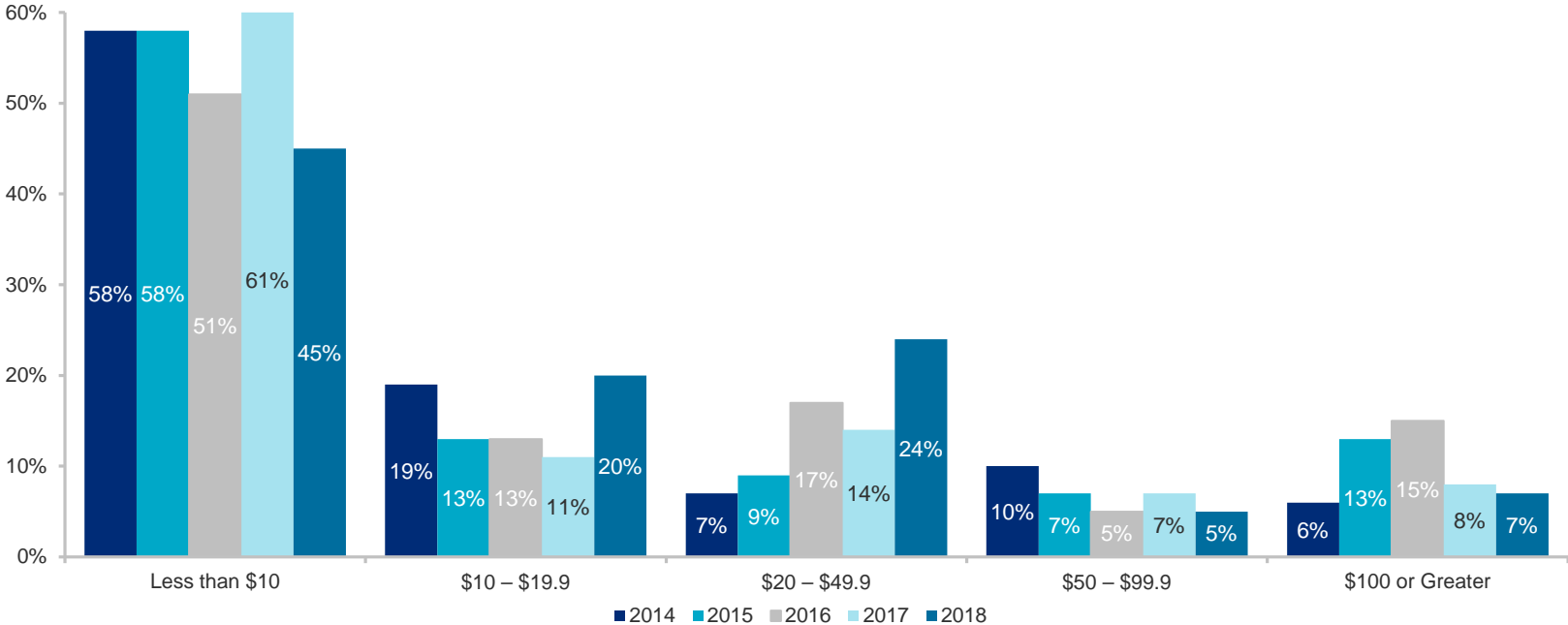
Number of Pending Federal Cases (Excluding IPO Laddering Cases)
January 2009-December 2018



Source: NERA, Recent Trends in Securities Class Action Litigation: 2018 Full-Year Review, January 2019

D&O Loss Trends

Distribution of Settlement Values



Note: Settlements exclude IPO laddering and merger objection cases
 Source: Nera Economic Consulting, Recent Trends in Securities Class Action Litigation: 2018 Full-year Review. January 2019

Other D&O Update

SEC

- SEC ended 2018 fiscal year with 821 enforcement actions up from 754 in FY 2017
- Of the 821 enforcement actions in FY 2018, 490 were stand-alone actions, representing an increase of about 10% over the 446 stand-alone actions brought in the prior fiscal year.
- As of the end of 2018 FY, the enforcement division had more than 225 cyber related investigations ongoing.
- In FY 2018 the agency ordered whistleblower awards to 13 individuals totaling \$168 million, compared to \$158 million in all the programs prior years.
- A separate analysis of the SEC's enforcement figures by the NYU Pollack Center for Law & Business against public companies & subsidiaries "jumped substantially" in the second half of FY 2018, reversing a decline in filings that began in the second half of 2017 and continued through the first half of 2018.
- The increased level of activity in FY 2018 presents quite a contrast with the reduced levels of enforcement activity during the 2017 fiscal year. The increase suggests that whatever the overall administrative view may be toward regulatory activity, the approach is not so comprehensive that it precludes an active enforcement approach from the SEC.

FCPA

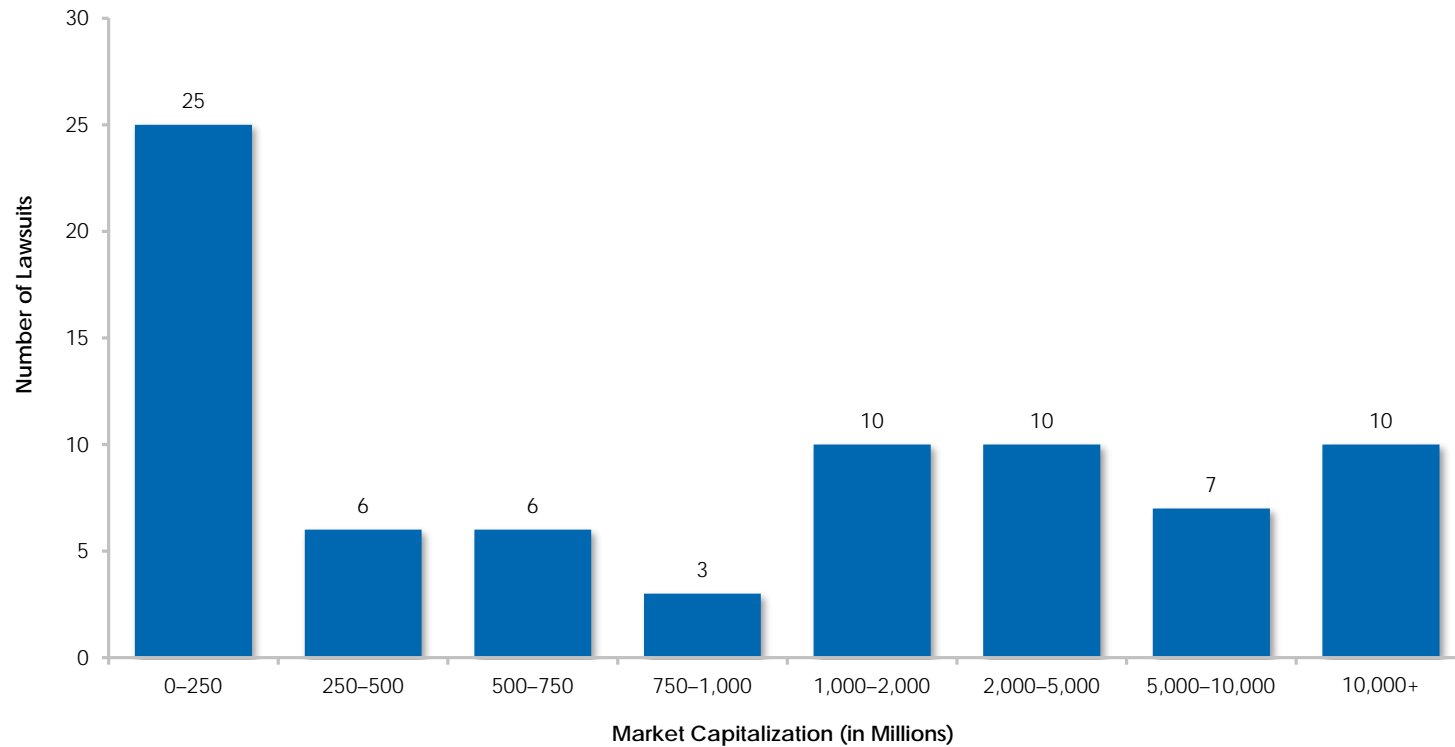
- A record 29 FCPA-related enforcement actions in FY 2017
- 11 companies paid just over \$1.92 billion to resolve FCPA cases in 2017
- DOJ continues to demonstrate a focus on culpable individuals
- New FCPA Corporate Enforcement Policy

Source: NERA Recent Trends in Securities Class Action Litigation 2018 Full Year Review
U.S. Securities and Exchange Commission, Fiscal Year 2018 Division of Enforcement Annual Report sec.gov
Gibson Dunn 2018 Year-End FCPA Update
Cornerstone Securities Class Action Filings 2018
Grant Thornton SEC Briefing January 17 2019

Life Science Litigation and Loss Trends

Life Science Class Action Lawsuits

2018 Securities Fraud Class Action Lawsuits



Source: Dechert LLP. Dechert Survey Developments in Securities Fraud Class Actions Against U.S. Life Sciences Companies. February 2019

Life Science Class Action Lawsuits

Allegations

- Nearly 22% (19 of the 86) of all the class action securities fraud cases filed against life science companies in 2018 alleged misrepresentations or omissions regarding product safety, and/or the likelihood of FDA approval
- 15% (13 of the 86) alleged misrepresentations regarding regulatory hurdles and the timing prospects of FDA approval
- Over 29% (25 of the 86) alleged unlawful conduct in both the United States and abroad, including illegal kickback schemes and anticompetitive conduct
- 26 cases alleged financial misstatements, improper accounting, price fixing, improper sales or marketing practices
- A roughly equal amount of claims were filed in the first half of 2018 as in the second half, with 26 complaints files in the first quarter alone

Source: Dechert LLP. Dechert Survey Developments in Securities Fraud Class Actions Against U.S. Life Sciences Companies. February 2018



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