Focus On: The Return of D&O Litigation:

Trends Driving Increasing Costs and Frequency of Litigation Against Corporate Directors and Officers

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Professional Risk

Declining securities class action filings in recent years raised the question of whether the strictures of the Sarbanes-Oxley Act (SOX) of 2002 were working, heralding a new era of greater transparency, less fraud, and hence fewer cases – particularly those against directors and officers.[1] To the contrary, 2007 and 2008 have brought the return of case filings and a continued increase in case value. This article summarizes the trends and examines the factors behind the escalation.

Case Filings Increase

Approximately half of all suits against directors and officers are securities suits, most often in the form of class actions.[2] After several years of declining securities class action filings, the number of cases filed in 2007 increased by 40% or 50% (depending on the study) over 2006, and filings for 2008 are currently trending toward 214 cases by the end of 2008, which is a 21% increase. This will be the largest number of filings in this decade other than 2002, the year of Enron, WorldCom, SOX and corporate scandals.

Professor Joseph Grundfest of the Stanford Law School is a proponent of the "fraud reduction hypothesis," contending that "the decline in litigation activity in the second half of 2005 and in 2006 is consistent with the observation that managements may be engaged in less fraud because of the increased federal enforcement activity and improved monitoring by boards and auditors," and that the increase in filings in 2007 is not inconsistent with this hypothesis. He argues that additional years of data are needed to provide adequate statistics for analysis, and that "one-time systemic shocks" such as subprime and options backdating should be subtracted from measurements.[3]

However, securities class action litigation has proven to be, by nature, a catastrophic loss industry: the mutual fund cases of 2001 and 2003, analyst cases of 2001 through 2003, IPO allocation cases of 2001 and 2002, option backdating cases of 2006 and 2007, and subprime cases of 2007 and 2008.[4] Accordingly, to pull out these systemic suits debases the entire analysis, akin to taking catastrophes such as hurricanes out of property loss analysis.

Case Values Increase

2007 securities class action settlements exceeded those in previous years by 15% to 46%, depending on the measurement. Median settlements increased by 30%, from $6,900,000 to $9,000,000, and average settlements increased by 15%, from $54.7 million in the years prior to 2007 to $62.7 million in 2007.[5] Excluding settlements of more than $1 billion, median settlements in 2007 increased by 37%, from $7 million to $9.6 million, and average settlements increased 46%, from $22.7 million in 2006 to $33.2.[6]

In 2007, more than half of all securities class actions settled for less than $10 million, significantly below the year's median and average numbers. However, the percentage of cases settling in the bands of $10 million to $20 million, $50 million to $100 million, and in excess of $150 million increased in 2007 over prior years.[7] Hence, there are a higher percent of cases settling in the higher damage brackets, counterbalancing the volume of cases settling for less than $10 million.[8]

The growing number of larger cases share some common characteristics. The following discussion identifies those characteristics and analyzes them to determine what is behind the increase in the frequency of filings and the rising severity of settlements and judgments.

Credit Crisis

In 2007, 33 securities fraud class actions relating to subprime lending were filed by five law firms.[9] Nearly 80% of the cases were filed in the latter half of the year, split evenly between the two quarters.[10] By May of 2008, there were 80 securities fraud class actions, 23 derivative actions, and 21 individual securities actions.[11] The foregoing makes clear that the emergence of sub-prime problems fueled increased frequency of filings in 2007 and continues to do so in 2008.

Directors and officers were sued in 97% of the cases in 2007, two thirds of which were filed in Florida, New York, and

Federal Securities Class Action Case Litigation Filings

	2001	2002	2003	2004	2005	2006	2007	5/82008
PWC								
All cases	487	264	210	227	173	219	169	
Cases other than IPO laddering, analyst, mutual fund, stock option backdating	178	217	175	206	169	109	163	
Stanford								
All cases	497	267	226	237	182	118	177	78
Cases other than IPO laddering, analyst, mutual fund	179	226	189	215	178	116	174	
Cornerstone								
All cases	179	226	189	214	178	116	166	
Cases other than option backdating and subprime					176	92	126	

Cornerstone Filings, p.5; PricewaterhouseCoopers, "2007 Securities Litigation Study", p.9 ("Pricewaterhouse Study" hereinafter); Stanford Securities Class Action Clearinghouse website, securities.stanford.edu, 5/8/08 ("Stanford" hereinafter).

California.[12] Allegations include fraud, false registration statements, and false prospectuses and communications with respect to accounting, rating, collateralization, sale of securities and insider trading.[13] The cases are filed as shareholder class actions, derivative actions, ERISA actions, and institutional investor actions.[14]

Median Settlement Amounts, $ Millions								
	2000	2001	2002	2003	2004	2005	2006	2007
All settlements	$5	$5	$6	$5.6	$5.2	$7	$7	$9.6
Public Pension Plans as Lead Plaintiff	$24	$118.8	$25.4	$35	$67.5	$22.6	$99.3	$18

All settlements: NERA, p. 13; Public Pension Plans: Cornerstone Settlements, p.10.

Regulators are also bringing credit cases. A team of more than 100 lawyers in a subprime working group at the Securities and Exchange Commission has opened approximately 36 investigations into conduct relating to subprime mortgage handling.[15] The F.B.I. is investigating 14 companies, examining possible accounting fraud and insider trading.[16] State Attorneys General have brought actions against mortgage lenders and others.[17]

Early subprime cases were filed against companies with direct ties to subprime lending, such as mortgage lenders and investment banks. Thereafter, the impact spread to companies with losses in their investments or those involved with subprime securitization. For example, cases include one against a student loan company and another against a law firm that prepared commercial mortgage securitization documents.[18]

More recently, the credit crisis has spread to auction rate securities. Fifteen of the 76 subprime related securities class actions filed by April 21, 2008, pertain to auction rate securities.[19] In addition, the New York Attorney General is investigating 18 institutions regarding their auction rate securities, after trading was halted in February, effectively making the securities illiquid. Shareholder class actions have been filed, alleging failure to disclose the potential for illiquidity of the securities, instead selling them as cash alternatives.[20]

Accordingly, while it is hard to predict how many suits will ultimately be filed and against what sectors, frequency will continue to grow with the spread of the credit crisis into various industries. In addition, the financial complexity of the cases may result in significant defense costs. One company reportedly spent $25 million in defense costs through trial.[21]

Institutional Investors

Institutional investor cases are dramatically more expensive than cases led by other plaintiffs. In the past eight years, cases led by institutional investors cost anywhere from two to twenty-three times as much as cases without institutions as lead plaintiffs:

Case value may continue to increase, since more and more cases are led by institutional investors. Pension funds and other institutional investors filed only 6 cases in 1996.[22] By 2007, institutional investors were lead plaintiffs in 65 cases, ten times as many cases as in 1996.[23] The impetus was the Private Securities Litigation Reform Act of 1995 (PSLRA), which created a rebuttable presumption that the most adequate plaintiff is the person or group of persons with the largest financial stake in the outcome of the case.[24] Typically, that would be institutional investors.

Their presence as lead plaintiff is costly. As noted above, their recoveries range from two to twelve times the recoveries in non-institutional investor led cases. Indeed, the largest case of the year, Tyco, settling for $3.2 billion, was one with a pension fund as a lead plaintiff.[25]

There are various possible reasons for the additional value attached to institution-led cases. Perhaps the institutional investors choose to invest only in significant cases. While institutional investors were lead plaintiff in only 60% of cases settled in 2007, they garnered 94% of all settlement dollars that year.[26] Perhaps they drive the cases harder and refuse to settle for lower amounts. Perhaps because institutional investors have their own counsel, and perhaps they view it as their fiduciary obligation to their plan investors, thus driving them to demand higher amounts. Whatever the motivation, clearly the results are much higher case settlements. From 2000 through 2007, median settlements involving institutional investors were two to twenty-three times higher than all median settlements.[27]

Opt-Outs/Individual Actions

An increasing number of institutional investors are filing individual actions and opting out of participating as a class member in a securities class action. The early opt-out benchmark was the WorldCom actions, in which eight opted-out institutional investors reportedly recovered $651 million, which they assert is more than they would have recovered if they had participated in the class action.[28]

WorldCom was followed by the AOL Time Warner actions, with nine opt-out institutional investors recovering $795 million.[29] The Qwest case followed, with the class settling for $400 million, but some of the opted-out institutional investors settled for even more, $411 million.[30]

There are many reasons compelling institutional investors to opt out. First, some investors are opting out because they may get a larger settlement on their own. "[When] institutional investors exit the class and sue individually, they appear to do dramatically better – by an order of magnitude" and "class members who opt-out and flee the class seem to do extraordinarily better than those who remain within the class…," notes John C. Coffee, a law professor at Columbia University Law School in New York and director of its Center on Corporate Governance.[31] He observes that the increased recoveries in the opt-out cases could lead the well-funded and resourceful pension funds to begin to regularly opt out, creating a two tier system in which the larger plaintiffs opt out, leaving the smaller plaintiffs in the class action.

Second, institutional investors are able to negotiate lower attorneys' fees, given their relative bargaining power. For example, in Qwest, opt-out counsel charged only 5% to the class action counsel's 15%.32 Third, institutional investors may feel it is their fiduciary duty, owed to their investors, to aggressively pursue greater recoveries rather than settle for cents on the dollar, which is more typical in a class action. Fourth, some institutional investors are public pension funds, and management may see a successful opt-out case as a politically astute maneuver.

Opt-out cases create a myriad of problems for the defendant company and its executives. The additional individual cases make the combined matters more expensive to settle. The more cases, the more defense costs. More importantly, the threat of an opt-out action and all that it entails may entice defendants to settle the class action for a greater amount to entice the opt-outs to stay in the case or may entreat the defendants to provide more benefits to the threatened opt-outs than the rest of the class. Moreover, the opt-outs may make the number of shareholders participating in the class action settlement so low that the settlement is cancelled under what are known as "blow provisions" in class action settlements.[33]

Investor Losses

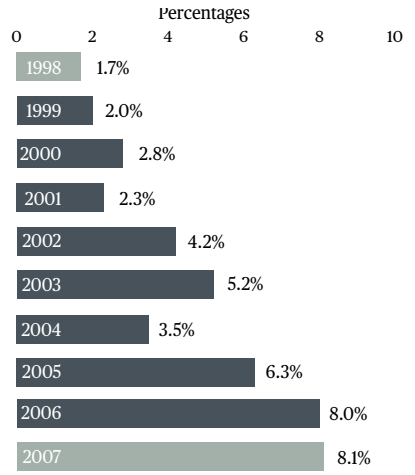
Stock market volatility has created more investor losses than in years past, increasing case values. The median value of investor losses from 2004 through 2007 was more than $300 million each year, whereas the median value of investor losses from 1991 though 1994 was less than $100 million a year.[34]

The upward trend does not appear likely to change soon. Median investor losses for cases settled in 2007 were $310 million, whereas median investor losses for cases filed in 2007 were $355 million, a 15% increase and the highest in the past three years.[35] Hence, it appears that recently filed cases seek greater damages than those filed in prior years, which may translate into even more expensive settlements and judgments in the years ahead.

In addition, each year a larger percent of cases settle for more than $100 million, reflecting the increasingly expensive nature of cases. The number of $100 million-plus cases has increased four times in the past ten years. (See chart)

Proportions of Settlements Over $100 Million, by Year

All settlements: NERA, p. 13 Public Pension Plans: Cornerstone Settlements, p. 10.

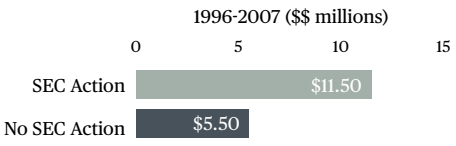


Concurrent Regulatory Proceedings

Securities class actions are more expensive when there are concurrent regulatory proceedings. For example, median settlement values double when there is a simultaneous Securities and Exchange Commission action.

The securities class action may be more expensive where there is a concurrent regulatory claim simply because the regulator files only in the more egregious of cases. Alternatively, the securities class action may become more costly because of the additional evidence produced in the regulatory matter, increased pressure to settle to reduce adverse publicity, or the desire to eliminate any civil litigation because it can compound discovery and defense of the regulatory case.

Median Settlement of Securities Class Action When Accompanied by SEC Action



More than 20% of securities class actions after passage of the PSLRA in 1998 have involved concurrent Securities and Exchange Commission proceedings.[36] The credit crisis may ensure that regulators remain active. As noted previously, the Securities and Exchange Commission has a subprime working group that is pursuing dozens of investigations while, at the same time, the FBI is examining 14 companies and state Attorneys General are investigating and proceeding against still more.[37] This suggests more concurrent regulatory proceedings, creating more expense and more complexity in handling multiple types of actions in one matter.[38]

Criminal Actions

The increasing number of criminal cases brought against corporate executives today must be considered when assessing the severity of litigation against corporate executives. This is because the criminal cases place additional pressure on defendants in concurrent civil cases, making the civil action more costly due to any additional evidence produced in the criminal matter, increased pressure to settle to reduce adverse publicity, or the desire to eliminate any civil litigation because it can compound discovery and defense of the criminal case.

The Corporate Fraud Task Force was established in 1992 as a collaborative effort of prosecutors from the Securities and Exchange Commission, Department of Justice, U.S. Attorneys, and others.[39] By mid-year 2007, the task force won 1,236 corporate fraud convictions, including 419 against top executives:

Many of the sentences, fines and penalties are very significant:

Criminal Convictions, 1992-July 2007	
Chief executive officers and presidents	214
Chief financial officers	53
Corporate Counsels or Attorneys	23
Vice presidents	129
Total	419

www.usdoj.gov/opa/pr/2007/July/07_odag_507.html

Executive	Sentence
Bernard Ebbers, CEO, WorldCom	25 years, ineligible for parole.
Walter Forbes, Chairman, Cendant Corp.	12 yrs, 7 mo.; $3.3 billion restitution to shareholders.
Dennis Kozlowski, CEO, Tyco International	Up to 25 years, eligible for parole in 2013; $97 million restitution, $70 million in fines.
Sanjay Kumar, Chairman and CEO, Computer Associates	12 years; $8 million in fines, $800 million in restitution.
Kenneth Lay, CEO, Enron	Died before sentencing.
Michael Milken, head of junk bond division, Drexel Burnham Lambert	Sentenced to 10 years, released after 2 years. Paid $900 million.
Walter Pavlo, Senior Manager, MCI/ WorldCom	Sentenced to 41 months, released after 2 years.
John Rigas, Chairman and CEO, Adelphia Communications	15 years.
Timothy Rigas, CFO, Adelphia Communications	20 years.
Michael Rigas, Chief of Operations, Adelphia Communications	10 months, home confinement.
Jeff Skilling, CEO, Enron	24 years; $45 million of assets liquidated.
Martha Stewart, re: sale of ImClone stock investment	5 months imprisonment, 5 months home confinement.
Mark Swartz, CFO, Tyco International	Up to 25 years; $35 million fine, $37 million restitution; eligible for parole in 2013.

Norton, Rob, "Let's Reform Those Draconian Sentencing Guidelines" (January/February 2008), Corporate Board Member, p.68-75.

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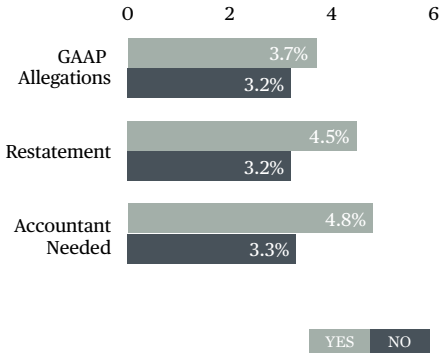
Media Settelment as a Percentage of Estimated Damages and Accounting Allegations, 1996-2007



Accounting

More than 55% of cases settled in 2007 included accounting allegations.[40] This is an indicator of the increasing severity of case values, since cases with accounting allegations settled, on the average, for $22 million more than cases without accounting allegations in 2007.[41] Similarly, cases with GAAP allegations, restatement allegations, or accountants as named defendants settle for a higher percentage of the estimated damages.

It is perhaps not surprising, then, that the largest settlement in 2007 was an accounting case, involving Tyco, settling for $3.2 billion.[42]

More recent filings contain fewer accounting allegations, which may suggest that accounting allegations will not be as significant an indicator of severity in future. Only 50% of cases filed in 2007 contained accounting allegations, in contrast to more than 61% of cases since 1995.[43] Another study puts the decrease as low as 42% of cases filed in 2007, down from 66% in 2006.[44]

Stock Option Backdating Suits

In 2006, stock option backdating cases surged, with 110 derivative and 21 federal securities class actions filed.[45] By April 2008, the numbers had grown to 166 derivative and 36 federal securities class actions.[46] The majority of the cases were derivative because shareholders often suffered no downturn in stock value. The alleged harm was only to the rise to derivative suits rather than individual actions.

Many of the options backdating cases have been closed.[47] In 2007 and 2008, 51 of the 110 derivative cases were resolved: 20 were settled, and 31 were dismissed.[48] These cases were resolved on a fast track, considering the average directors' and officers' liability class action takes approximately three years to settle and 25 months to dismiss.[49] At the current rate, 2008 should see the resolution of many of the stock option backdating cases, barring the notion that the harder, more complex cases will take longer to resolve.

As the stock option backdating cases mature, there have been very few significant, albeit notable, settlements. The UnitedHealth Group settlement is the largest derivative settlement in history, valued in excess of $900 million.[50] The chief executive returned $320 million in stock options, relinquished $99 million in other retirement and executive savings benefits, and acceded to $189 million in repriced stock options, while other executives gave up similar rights and conceded to repricing for the balance, creating a settlement of more than $900 million.[51] The Mercury Interactive securities class action case settled for $117.5 million.[52]

Option Backdating Lawsuits

	Securities Class Actions	Derivative Actions	ERISA Actions
Filed	36	166	5
Dismissed	6	29	
Voluntarily Dismissed	0	4	
Settled	8	21	
Motion to Dismiss Denied	6	7	

LaCroix, Kevin, "Options Backdating Lawsuits: Settlements, Dismissals and Denials" (April 17, 2008); Counting the Options Backdating Lawsuit" (February 9, 2008), both available at: www.dandodiary.com.

Derivative Actions

More and more securities class actions are settled with concurrent derivative action settlements:

Derivative Action Settlements Accompanying Securities Class Action Settlements

2005	2006	2007
35% of Settlements	45% of Settlements	55% of Settlements

Cornerstone Settlements, p.11

Median Settlements Amount, 1998-2007

Cases settled in 2007, without an accompanying derivative action	$5.2 million
Cases settled in 2007, with an accompanying derivative action	$11.2 million

Cornerstone Settlements, p.11

The reason for the increased case value may be that derivative actions tend to be filed with the more serious securities class actions, so, by nature, these are the more expensive cases.[53]

Not only is a securities claim more expensive when there is an accompanying

derivative claim, but the derivative claims are rising in severity as well, compounding the severity problem for companies. This was made clear in 2007, which yielded the largest derivative settlement in history: UnitedHealth Group settled a derivative action for cash and non-cash valued, in the aggregate, at approximately $900 million. The non-cash elements of the settlement included the surrender of executive stock options, repayment of compensation, reprising of stock options, a Securities and Exchange Commission penalty, relinquishment of claims to post-employment benefits, and reimbursement to the company for incentive and equity based compensation.[54]

At least one author opines that the derivative suit has taken on a diminished role in jurisprudence today, relegated to cases involving self-dealing or other breaches of the fiduciary duty of loyalty.[55] Instead, securities class actions are preferred because plaintiffs recover their own damages, not those of the corporation.[56] However, the vast number of derivative suits filed in 2006 relating to stock option backdating suggests that the derivative suit still has its place today.

Percentage of Federal Securities Class Action Lawsuits by Industry

Industry	Percentage of Total Cases		
	2005	2006	2007
High Technology			
Computer Services	16	11	8
Electronics	9	13	7
Telecommunications	4	6	9
Pharmaceutical	14	9	13
Banking, Brokerage, Financial Services & Insurance	13	6	21
Health Services	7	7	4
Business Services	5	5	5
Retail	4	6	4
Utilities: Energy, Oil & Gas	2	2	2
Other	27	35	26

PWC, p. 16.

Percentage of Federal Securities Class Action Lawsuits Naming Particular Officers or Committees

	2003	2004	2005	2006	2007
CEO	98	96	96	96	91
CEO	88	83	81	83	79
Chairman	70	72	72	61	64
President	77	71	59	68	55
Audit Committee	3	2	2	14	4
Other	1	0	1	11	4

PWC, p. 19.

Defendants

Certain industries, executives, and companies have become the prime targets for litigation. Three industries are the most frequently sued: 25% of 2007 cases filed were brought against high-tech companies, 13% were filed against pharmaceutical, and 21% were filed against the banking/brokerage/financial services sectors.[57]

Tech companies are sued for accounting issues such as lack of internal controls, revenue recognition issues, and disclosure problems.[58] Pharmaceutical company suits for drug efficacy became the most common, increasing from only 7 suits in 2006 to 17 suits in 2007.[59] Banking, brokerage, and financial services companies are sued for estimates and overstatements of assets.[60]

Executives are sued in securities class actions as a rule, albeit certain executives are sued more often than others. The chief executive officer is sued in more than 90% of the cases, the chief financial officer is sued in 79% of the cases, and the chairman and president are sued in 64% and 55% of the cases, respectively.[61]

Committees are much less likely to be sued. In spite of the reported pressure from SOX, the audit committee and compensation committee are sued in only 4% of the cases.[62]

The size of a company is not necessarily a determinant as to whether the company

Number of Federal Securities Class Action Lawsuits Filed Against Fortune 500 Companies					
Year filed	Top 5	Top 100	Top 500	Total Cases	%
2007	4	9	20	163	12
2006	5	5	12	109	11
2005	3	6	24	169	14
2004	7	9	27	206	13
2003	1	3	20	175	11
2002	16	25	60	217	28
2001	5	10	26	178	15
2000	4	8	24	203	12
1999	3	8	25	205	12
1998	2	4	16	245	7

PWC, p. 20.

will be subject to a securities class action. In 2007, only 12% of the filed cases were brought against a Fortune 500 company, for a total of 20 actions out of 163.[63]

Plaintiffs

Years ago, the shareholder was the typical plaintiff in a securities case. Today, the adversaries are much more varied and resourceful, making the cases more complex to litigate and settle.

Regulators

From 1996 through 2001, after passage of the PSLRA and up to passage of SOX, 218 securities class action lawsuits involved concurrent Securities and Exchange Commission investigations, actions, settlements, or case closures. Following passage of SOX in 2002 to date, 326 securities class action lawsuits involved such Securities and Exchange Commission activities, a 50% increase.[64] Thus, the Securities and Exchange Commission is more active post-SOX than pre-SOX. That would indicate more actions, more expense, and more complexity in handling multiple types of actions in one matter.

However, the Securities and Exchange Commission has filed fewer cases each year since 2004.[65] This suggests that Securities and Exchange Commission matters may not be as problematic in the future.

It should be noted, however, that the credit crisis and related problems may change the trend in the year ahead. As noted above, more than 100 lawyers in a subprime working group at the Securities and Exchange Commission are investigating 36 companies regarding subprime lending.[66] The FBI is investigating 14 companies, and state Attorneys General have brought many actions against mortgage lenders and others.[67]

2002 is an example of the upsurge in filings of which the Securities and Exchange Commission is capable. In that year, with the upheaval over Enron and WorldCom and passage of SOX, the Securities and Exchange Commission brought 98 cases, in contrast to only 45 the year before.

From 1996 through 2001, 123 securities class action lawsuits involved a concurrent Department of Justice criminal investigation, indictment, guilty plea, conviction, or settlement. From 2002 through 2007, 167 securities class action lawsuits involved such Department of Justice activities, which is a 36% increase in the number of Department of Justice proceedings that accompany securities class actions.[68] From 1996 through 2001, 97 securities class action lawsuits involved concurrent criminal Department of Justice and Securities and Exchange Commission activities cases. From the passage of SOX in 2002 through 2007, 137 securities class action lawsuits involved both Securities and Exchange Commission and Department of Justice activities, which is a 41% increase in the number of proceedings by both the Securities and Exchange Commission and the Department of Justice that accompany a securities class action.[69] However, there was an overall decline in Department of Justice and Securities and Exchange Commission filings between 2006 and 2007, but it remains to be seen whether this trend will continue given the current credit issues and investigations in the marketplace.

The foregoing makes clear that, since passage of SOX in 2002, the Securities and Exchange Commission and the Department of Justice proceedings are filed more frequently in matters where shareholder securities class actions are also brought. As such, companies and boards are more likely to be faced with the complexities and expense of defending administrative as well as civil proceedings at the same time.

Foreign Investors

While countries outside the United States eschew the litigiousness of the U.S. legal system, foreign companies are becoming more and more assertive in taking advantage of that system. In 98 cases, the total of 182 institutional investors from 17 countries filed motions to become the lead plaintiffs in 98 securities class actions from 1996 and March 31, 2007.[70] For example, "Borochoff v. Glaxosmithkline PLC," 246 F.R.D. 201 (S.D.N.Y. 2007), a foreign company was appointed to be the lead plaintiff. As such, boards must look not only to U.S. shareholders as potential litigants, but to their expanding global shareholder base as well.

Climate Change

The question is no longer whether there will be litigation arising out of climate change, but rather how far-reaching it might be and whether it will affect corporate executives.

There are numerous cases already filed against companies arising out of global warming and climate change. In one case, the Securities and Exchange Commission reportedly alleged that a former employee of an oil company arbitrarily decreased the estimated costs for anticipated environmental remediation at various oil refinery and chemical sites. The decrease in costs and reserves falsely inflated net income and allegedly resulted in false financials. The case was settled. In several other cases, the Securities and Exchange Commission has reached settlements with companies that allegedly improperly reduced environmental reserve accounts.

In September 2007, the New York Attorney General began an investigation into whether certain large companies in one industry adequately disclosed to investors the companies' financial exposure pertaining to greenhouse gas production at various plants. Shareholders are submitting an increasing number of climate change shareholder resolutions, from 6 in 2001 to 30 in 2005, to 42 in the first six months of 2007. Finally, on September 18, 2007, 22 state pension funds, environmental groups, and other investment managers sent a petition to the Securities and Exchange Commission seeking greater corporate disclosures relating to climate change exposure.

Legislative and regulatory strictures are creating more rules that corporations and their executives will have to follow, creating a web of potential liability for failure to meet the new laws. The compliance environment will be difficult because it will be balkanized among Federal and state laws, rules, and cases. Moreover, multinational companies will be faced with tracking the laws around the globe. The matrix exposes management to a nascent and unpredictable global liability environment.

The Return of D&O Litigation

Contrary to what others have "prematurely predicted," shareholder class action lawsuits "will not die or whither away" as Professor John Coffee has recently observed.[71] To the contrary, frequency of filings is up along with rising severity of settlements and judgments. The cases are characterized by credit allegations, increasing investor losses in a fluctuating marketplace, and accounting questions. Institutional investors are leading many of the class actions and reaping enormous rewards and are opting out for even more significant recovery in an ever increasing number of opt-out cases. At the same time, the Securities and Exchange Commission and Department of Justice are prosecuting more cases and more executives, resulting in fines, penalties, and imprisonment. Derivative actions have surged with stock option backdating case filings in 2006, and several very significant settlements have resulted. The end result is that executives and corporations today are faced with defending sophisticated financial litigation on more varied fronts, making the cases costly and compromising. D&O litigation is back, and appears to be poised to continue unabated in the near future.

About the author

Carol Zacharias is Senior Vice President and Chief Counsel to Chubb's Professional Risk and Surety divisions. Ms. Zacharias received her Master's degree in Corporate Law from New York University School of Law and her law degree from the New England School of Law. She has served as Chairman of the American Bar Association Business Law Section's Business Insurance Committee and is currently Vice Chairman of the Professional, Officers' and Directors' Liability Law Committee of the Tort and Insurance Practice Section. She is also Co-Chair of the insur. ance subcommittee of the American Bar Association Litigation Section's Committee on Corporate Counsel. She is a member of the United States Supreme Court, Federal and New Jersey bars, the American Bar Association, and the American Corporate Counsel Association. Ms. Zacharias has been published in a securities law textbook and a variety of periodicals. She is a frequent speaker and has taught liability at New York's College of Insurance.

Notes

1. Public Company Accounting Reform and Investor Protection (Sarbanes-Oxley) Act of 2002, Pub. L. No. 107-204, 116 Stat. 745 (codified as amendment in scattered sections of 15, 18 U.S.C.) (hereinafter "SOX").
2. Towers Perrin, 2006 D&O Liability Survey on Insurance Purchasing and Claims Trends, available through www.towersperrin.com.
3. Cornerstone Research, "Securities Class Action Filings, 2007: A Year in Review", p.5. ("Cornerstone Filings" hereinafter), p.4.
4. Stanford. The fraud reduction hypothesis is also known as the 'less fraud theory'.
5. "Securities Class Action Settlements, 2007 Review and Analysis", Cornerstone Research, p.2. ("Cornerstone Settlements" hereinafter.)
6. Plancich, Saton, Starykh, "2007 Year End Update: Recent Trends in Shareholder Class Actions: Filings Return to 2005 Levels as Subprime Cases Take Off; Average Settlements Hit New High" (December 2007). National Economics Research Associates Economic Consulting, pp.9,13. ("NERA" hereinafter.)
7. Cornerstone Settlements, p.3.
8. However, arguments and statistics suggesting increased case values have their detractors. One analysis from 2006 contends that cases are not more costly today than before the PSLRA, taking into account certain factors. See, James D. Cox, Randall S. Thomas with Dana Kiker, "Does the Plaintiff Matter: An Empirical Analysis of Lead Plaintiffs in Securities Class Actions", 106 Colum. L. Rev. 1587 (2006).
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11. Advisen MSCAd as of May 1, 2008.
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14. Id. at p.5.
15. Younglai, Rachelle, "U.S. SEC Subprime Probe Moving Vigorously – Enforcer" (February 1, 2008), Reuters.
16. RiskMetrics, p.5.
17. Id. at pp.4,5.
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