WEBINAR

Rise of Ransomware and Other Cyber Risks Impacting D&O Coverage

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March 14, 2024

Rise of Ransomware and other cyber risks impacting D&O Coverage

Presentation part of the Wilson Elser D&O Forum Series
Guest Presenter – Larry Goanos, Executive Vice President, Professional Lines, AMWINS

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Our Goals Today

- Address general cyber risks impacting organizatic
- Growing areas of cyber risk
- Cyber cases against D&Os
- Increasing cyber regulation
- Impact of these claims on D&O insurers

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Introduction

What are some new corporate cyber exposures for D&Os?

- Number of Ransomware
- Number of Business Email Compromise
- Role of the Regulator Changing
- Number of Cyber Class Actions including claims alleging disclosure of biometric information.

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Other cyber related risks that D&Os have to be aware of

- Recent growing cyber risks
  - Internet of Things – *Neilsen v. Lantronix, Inc., et al* - US Dist CDCA (24-cv-385)
  - Wire Transfer Fraud – *NY AG v. Citibank* – US Dist SDNY (24-cv-659)
  - Pixel Tracking Lawsuits – *Jane Doe v. Fullstory, et al* – US Dist NDCA (23-cv-59)
  - More Applications of Artificial Intelligence

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Litigation Statistics

- Combined filings in the U.S. district courts for civil cases and criminal:
  - down 8 percent from 309,102 to 284,220 from March 2022 to March 2023.
  - Case pending cases went down 8.6% from 638,264 to 583,543.
- In 2023, there were 44 mega MDL filings with a total mega Maximum Dollar Loss of $2.9 trillion, a 30% increase from 2022 and the second-highest value on record. Conversely, there were 16 mega Disclosed Dollar Loss ("DDL") filings in 2023, down from 18 in 2022.

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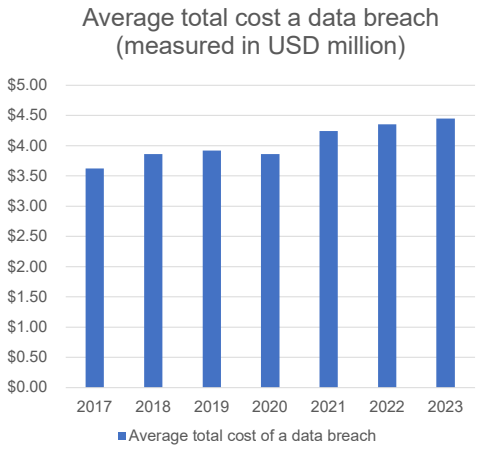
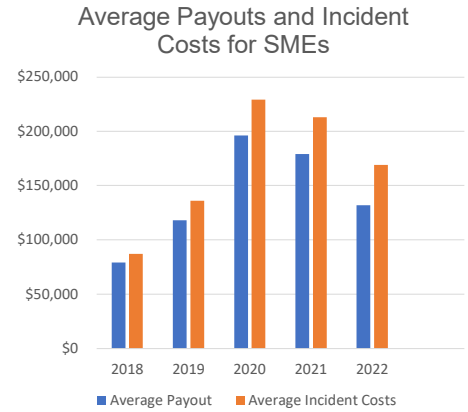
Claims in the Cyber Insurance Market



Source: IBM Security
Cost of a Data Breach Report 2023



Source: NetDiligence Cyber
Claims Study – 2023 Report

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D&O Responsibilities on Cyber Risks

- Board Standard Duties to the Organization
  - Duty of Loyalty, Care, Candor
  - Business Judgment Rules
  - Ethics
  - Board Oversight over the implementation of Technology

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Board Expertise and Reliance on Experts

- A board member does not have to have detailed technical knowledge of a subject area to fulfil its duties to a company.
- While board members must acquire a reasonable level of understanding of the company and its level of exposure to cyber (for example) and other risks, they may rely on advice from those individuals in management or outside experts that they reasonably believe do have the expertise necessary to evaluate the company's cyber risks and determine how to protect against cyber intrusions.

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Board Delegation

- A board can delegate some of its responsibilities or certain topical issues, but it does not have to. A board in its entirety can chose to retain authority to address certain issues.
- Often through, a board will give the authority to make a recommendation on a certain topical issues (and in some cases decision making authority) to a committee. For example, in recent years Board have delegated topics like cyber security to an audit committee, a risk committee, a technology committee or a special committee. It is ideal, but not necessary, if the committee or members have some facility for understanding that topic. If a committee has a member or members with some expertise in a topic that can be helpful but is not required.
- The board should ensure that there are reasonable reporting structures in place to keep the board adequately informed of any delegated topic/issue.

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Breach of Duty of Oversight/Caremark

- After a catastrophic cyber incident, an allegation can be brought that the board of directors breached its duty of oversight.
- In order to sustain a claim for breach of the duty of oversight, "the lack of oversight pled must be so extreme that it represents a breach of the duty of loyalty," which in turn "requires an action (or omission) that a director knows is contrary to the corporate weal."
- A viable claim may be established only for either "utter failures by directors to impose a system for reporting risk" or for "failure to act in the face of 'red flags' disclosed to them so vibrant that lack of action implicates bad faith, *in connection with the corporation's violation of positive law."*

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Breach of Duty of Oversight/Caremark (Continued)

- Oversight breach claims remain a difficult claim to sustain.
- A potential claim is that the board failed to adequately oversee the risk to cybersecurity of a criminal attack.
- The criminal acts of third parties means only that the company was the victim of legal violations not the perpetrator.
- The absence of legal duties means that cybersecurity is a business risk, one of many the company faces.
- In order for the cybersecurity-related business risk to give rise to potential board liability, the claimant must establish a "nexus" between the risk and the board.

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Characteristics of a Catastrophic Cyber-Related D&O Securities Claims

A cyber incident does not typically translate into a high severity D&O/Securities claim but for two factors:

1. Cyber security or personal identifiable information is at the core of why the company exists, what the company does, or the services they provide. Examples: Equifax or SolarWinds
2. The cyber security incident or event brings down the company

a catastrophic ransomware event which takes the company completely offline or renders it inoperable or unable to provide services

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Prior Cyber Cases against D&Os

- Equifax Data Breach
  - *Kuhns v. Equifax, Inc., Richard Smith, et al* (17-cv-3463) (D. N.D. Georgia)
    - Data breach involved 143 million U.S. Customers personal information
    - D&O's made false or misleading statements regarding Equifax's measures to protect its data and detect security breaches
    - Settled for $149M in February 2020
- Capital One
  - *In Re Capital One Customer Data Security Breach litigation* (19-cv-1472) (EDVA)
    - Breach of 100 million customers in US and 6 million in Canada
    - Alleges that Capital One misled its investors by making a series of fraudulent statements that covered up its purported knowledge of the risks that such a data breach could occur, including its failure to maintain adequate data security protections
    - Settled for $190 million in 2022
- Other older cases
  - Target, PF Chang's, Neiman Marcus, and Michaels

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Recent Cases on Cyber Risks Impacting D&O Liability

- *In re: SolarWinds Corp. Securities Litigation*, U.S. District Court, Western District of Texas (21-cv-00138); *SEC v. SolarWinds and Timothy G Brown*, U.S. District Court, Southern District of New York (23-cv-9518).
- Block - *Donna Esposito v. Block Inc. et al*., U.S. District Court, Southern District of New York (22-cv-08636) filed 10/11/2022.
- T-Mobile – *Jennifer Baughman v. T-Mobile*, US District Court, Central District of California (23-cv-00477), filed 1/22/23.
- Dish Network – *Miguel Jaramillo v. Dish Network Corp, et al*, U.S. District Court, District of Colorado (23-cv-734), filed 3/23/23.

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Increased Cyber Regulations

- Various State Privacy Laws
- Global Privacy Laws impacting US companies
- NYS DFS Cyber Security Requirements
- SEC Disclosure Requirement

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Future Impact of These Claims On D&O Insurers

- Underwriting
  - The issues in the event driven litigation can potentially impact multiple lines of coverage (D&O, E&O, EPL, etc.);
  - Insurers must understand the risk they are underwriting.
- Claims
  - Regulatory Investigations;
  - Civil and Governmental Litigation;
  - Event-Driven Litigation;
  - Shareholder Activism Claims;
  - Areas for Future Concern

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Current Trends in Coverage

- Issues as to what is a Claim;
- Corporate Forum Selection Clauses;
- Pixel Tracking Exclusion;
- Biometric Claims Endorsement (Exclusion or Sublimit);
- War Exclusion Language.

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The Least You Need to Know

- Cyber risks are evolving, so D&Os have to be aware of it
- Potential litigations against D&Os are changing
- Artificial Intelligence is just one change impacting cyber exposure

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What Sophisticated Practitioners Are Doing

- Implementing best practices for cyber hygiene in their organization;
- Seeking advise of outside consultants on cyber risks;
- Underwriting asking more detailed questions on their D&O applications regarding cyber risks;
- Representations on the applications are becoming more critical.

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Final Thoughts / Predictions for 2024

- The scrutiny of boards will continue to grow
- Threat Actors will continue to use growing regulations to their advantage in threatening organizations with cyber attacks
- Changes in D&O policies will impact what is covered when there is a cyber security incident
- Actions related to the disclosure of genetic information will increase
- Crypto exposure will remain, but to a lesser extent

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Thank you!

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