UK Collective Actions

In our previous article entitled 'Are there any D&O claims outside the United States?' we touched upon a recent trend emerging within the United Kingdom litigation landscape. Namely, the filing of securities litigation against companies and directors on the back of historic regulatory investigations into allegations of bribery and corruption.

These cases are being brought under existing legislation in the UK and typically allege that investors suffered losses from share price falls linked to these previous regulatory settlements. In this article we expand further upon this, including some background to the legal mechanisms being used to bring these claims, current cases, and contemplations for D&O Insurers.

2. Section 90a / Section 90 – A Background and Coverage Matters

While the system for investor redress via legal action against companies and directors is well established in many jurisdictions, including the U.S. and Australia, the UK has been on its own journey in this regard. Below is a quick reminder of the mechanisms being used in the UK to bring these types of claims.

The UK civil liability regime was introduced via section 90A of FSMA in 2006, followed by Schedule 10A in 2010. This created the broad scheme by which a company could be found liable for the losses of shareholders as a result of it publishing a misleading statement or making a dishonest omission in certain published information relating to their securities, or dishonestly delaying the publishing of such information.

This liability arises where a Person Discharging Managerial Responsibility (PDMR) within the company knew the published statement(s) to be untrue or misleading or reckless as to whether it was so, or knew the omission to be a dishonest concealment of material fact, or acted dishonestly in delaying publication of the information.

Use of the s.90A procedure has to date been limited, meaning that judicial guidance on interpreting key elements of an action is incomplete. However, there are several concluded and ongoing actions which have delivered outcomes of interest.

Section 90 – Brief Overview

Section 90 is often mentioned in the same context as section 90A. However, Section 90 is limited to new listings whereas s90A applies to published information (or delay in publishing information) in relation to existing securities.

Under section 90 of the FSMA investors are able to seek compensation resulting from incorrect statements made in listing particulars or prospectuses.

It is anticipated that there will be an increase in Section 90 claims as new companies are established which have a stated aim of trading on a particular 'Environmental, Social and Corporate Governance' (ESG) agenda.

Section 90A cases – Current State of Play

As outlined, the specific securities actions in question here relate to cases where a company has already settled with the regulator as a result of a bribery and corruption investigation and subsequent charge. The companies in question have often admitted liability in written form and settled in both the UK and possibly other jurisdictions. This settlement could have involved paying a fine, which would not be covered under a typical D&O policy. The company subject to these actions may also have agreed to implement control improvements across the group.

In general, these securities actions are being filed several years after the original settlement with regulatory authorities has taken place, and in some cases, decades after the original wrongdoing itself is said to have occurred.

They are brought on behalf of both institutional and retail investors and are alleging damages running into the hundreds of millions in many cases. They will often quote directly from the settlements in historic bribery allegations, where a company could have admitted failures in its control environment and/or general corporate governance standards. For example, a plaintiff might wait for the result of an SFO investigation, and then file a claim seeking compensation under section 90a of FSMA, alleging that investors suffered losses linked to the share price impact of these settlements and investigations.

The cases are often backed by litigation funders, who are increasingly active in the UK, with collective actions seen as one of the most attractive forms of return for them. This leads us to anticipate that these cases will continue to be brought in the UK at an increasing rate, and that the damages sought will continue to remain at high levels.

Section 90A cases – Current State of Play

Unlike in the U.S. and other jurisdictions, these remain 'opt-in' actions, meaning that there is an onus on investors to become actively involved in the case. In theory, this reduces the risk of damages reaching levels typically seen in the U.S., but plaintiff firms are getting savvier at promoting these claims, and where the damages being claimed are running into such large amounts, these could be seen as attractive cases for investors to participate in.

Building on a current regulatory and investor focus on a company's ESG credentials, these claims are often framing the wrongdoing as a failure of a company's ESG control environment, perhaps to capitalise on heightened interest in this area.

This is all taking place at a time where D&O rates continue to be re-considered by D&O insurers after a period of increased competition in the market.

Current Cases

There are currently to our knowledge at least eight S90A claims that are still ongoing which the majority has been filed in the last 12 months. The legal fees and expenses involved in those civil cases can be significant (£10-20m) and settlements have the potential to erode the full insurance tower. These cases involve both middle-market and SME companies as well as FTSE 100 companies from all different types of industries.

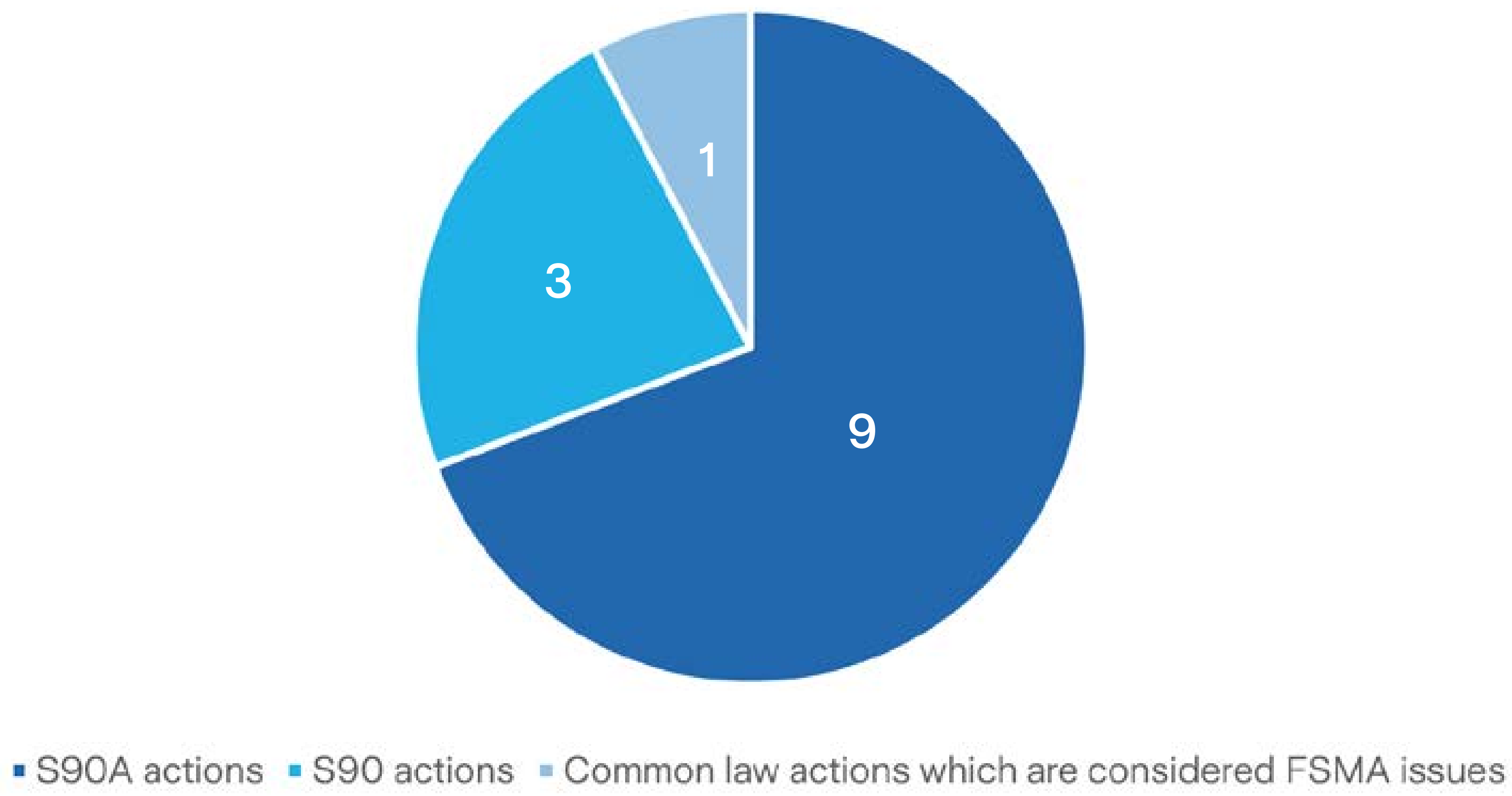
A selection of current cases:

1. A company in the oil & gas industry is facing a potential claim under section 90A of the FSMA after pleading guilty to historic bribery offences – the claimant period is quoted as going back as far as 2005.

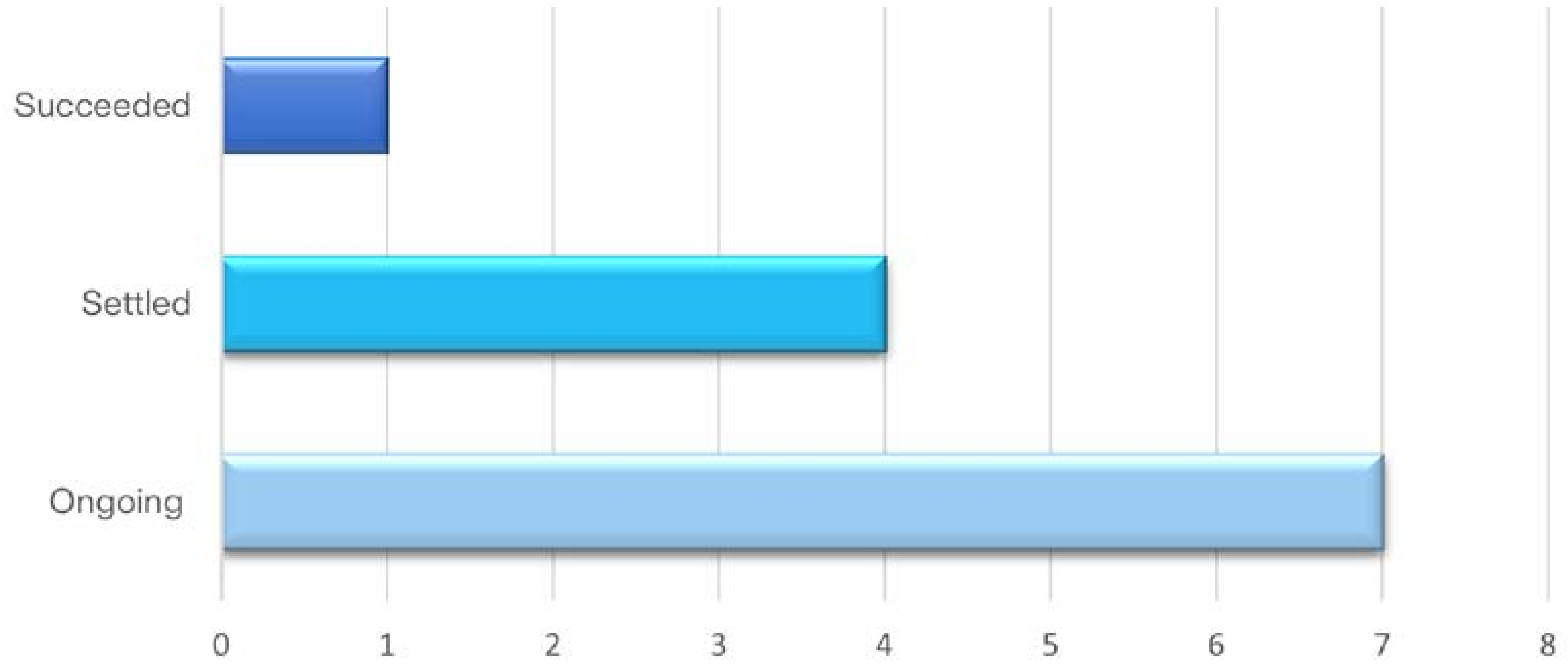
2. A mining company is facing a potential claim under section 90a of the FSMA after pleading guilty to historic bribery offences, the conduct dates back to at least 2011.

Data

Reported claims / actions involving S90 and S90A



S90/90a actions concluded



Largest Known Settlement £200m Section 90 Action

Estimated legal fees to get to trial £20m to £30m

Potential Damages Sought £85m to £110m

Contemplations for D&O Insurers

Claims dialog within the UK D&O space is often centred around both primary and low excess layer trends, given this is where better data has typically been more available in the past to D&O insurers. However, these follow-on securities actions have the potential to fully erode D&O towers, especially where lowers limits were previously exhausted by the underlying regulatory or criminal actions and associated defence costs.

For those clients who bought larger towers, or the original action was only valid to Primary or low excess layers (say for example, the lower layers were exhausted in defence costs payments under Side A and B coverage, but the high layers remained intact), these securities actions will become more relevant to higher excess attachments. This is at a time when excess layer premium is being re-considered by D&O insurers after a period of remediation over the previous few years. This could expose some positions previously modelled as lower risk by insurers and may not have been effectively priced-in by the higher excess insurers across their UK portfolios.

In respect of the clients who bought lesser limits or who have seen their D&O tower exhausted by the original or other actions action, they could be left exposed to funding these new costs directly from their balance sheet, and directors could be personally exposed if these costs are to be funded on a Side A basis (where, for a variety of potential reasons, the company does not indemnify directors for these costs), given these securities actions are likely to link back to the original notification. This can be particularly apparent in the middle market / SME space (generally considered to be companies up to the FTSE250 space) where the average limit purchased is significantly lower. This could see some clients essentially uninsured given the smaller limits purchased.

The future of s.90A and Collective Actions

The viability of s.90A actions has generated interest from both claimant law firms and litigation funders alike. The litigation funding sector continues to grow in the UK, and s.90A and s.90 actions offer significant prospects of strong financial returns, only to increase if future judicial decisions are favourable to claimants. Furthermore, s.90A claims may be more likely in the event of a sustained economic downturn or recession which brings volatility to the stock market. Large claims, including class actions, carry significant costs implications which may prove attractive to claimant law firms.

The regulation of the disclosure of, and general prevalence, of ESG issues in published documents will increase the risk of s.90A actions as shareholders pressure issuers to make the relevant disclosures, which could affect share prices.

Primarily s.90A actions have been prompted by, or contributed to, by prior regulatory action by the Serious Fraud Office (such as deferred prosecution agreements) or settlements with the Government. However, securities class actions may start to shift away from traditional or well established companies towards new entrants into the public markets.

Summary

It remains to be seen if these cases will be successful, but we view this as an emerging trend in the UK securities litigation landscape.

The fact remains that these incidents are continuing to show the ‘long tail’ nature of the D&O market, and this reinforces the need for long-term thinking and a focus on a stable D&O market.

We believe there will continue to be an attraction for long-term partnerships between clients and insurers, with key differentiators including a strong track record in the class market leading/experience claims proposition/team, robust credit rating and a customer-centric focus.

It is certainly food for thought for all parties with an interest in the D&O space, including clients, brokers and D&O insurers.

If you would like to discuss the above, please feel free to reach out to oli.jones@uk.zurich.com, mark.dowsing@uk.zurich.com or another member of the D&O team.