

D&O Insurance

D&O Insurance: Safeguard Your Leadership



ESSENTIAL TOPICS FOR IPO PROTECTION

- **Evolving Liabilities:** How personal and corporate risks shift in a public company.
- **Market Snapshot:** Current state of the D&O insurance landscape.
- **Litigation Insights:** Key trends in securities claims.
- **Coverage Limits:** Strategies to determine the right protection levels.
- **Underwriting Mastery:** Navigating the IPO process and positioning your company for success.

Fiduciary Duties: Guiding Your Leadership

DUTY OF CARE

Make informed decisions using all reasonably available material information.

DUTY OF LOYALTY

Act in the best interests of the company and shareholders, avoiding conflicts and maintaining independence.

DUTY OF GOOD FAITH

Violated by intentionally disregarding known risks or a knowing failure to apply minimum levels of diligence/oversight

*Delaware corporations may limit monetary liability for certain duty of care claims, **but not** for loyalty, bad faith, intentional misconduct/knowing violations of law, or improper personal benefit*

DUTY OF DISCLOSURE In the context of a public transaction, there is also a duty of disclosure

- Duty to disclose fully and fairly all material information within the board's control when it seeks shareholder approval
- The court may also apply a heightened standard of review due to conflicts of interest

Business Judgment Rule: Your Directors' Shield

EMPOWER INFORMED DECISIONS

- **Core Presumption:** Courts assume directors act on an informed basis, in good faith, and in the company's best interests.
- **Key Protections:** Shields from liability unless there's evidence of conflict, fraud, or gross negligence—no second-guessing by courts.
- **Tie to Fiduciary Duties:** Reinforces care, loyalty, and good faith; essential for D&O insurance coverage.

THE BUSINESS JUDGMENT RULE PROTECTS DIRECTORS & OFFICERS AGAINST HONEST ERRORS OF JUDGMENT

Corporate Indemnification Limits: Protecting Your Leaders Wisely

NAVIGATE BOUNDARIES FOR ROBUST D&O PROTECTION

- **Practical Financial Constraints:** Insolvency or insufficient funds can block indemnification.
- **Derivative Suits:** Limited to good-faith actions; no coverage for judgments without court approval.
- **Loyalty Breaches:** No indemnification for bad faith or conflicts of interest.
- **Federal Violations:** Securities law breaches (e.g., fraud) cannot be indemnified.
- **Takeover Risks:** New ownership may alter indemnity provisions via bylaw changes.
- **Bylaw Flexibility:** Amendments can modify protections unless locked in by contracts.

KEY ACTION: Strengthen bylaws and secure D&O insurance to bridge indemnification gaps.

Different Liability Landscape as a PubCo

Why It Matters: Public companies face Securities Act (1933) and Exchange Act (1934) rules, increasing litigation risks. Even JOBS Act EGCs need robust D&O coverage. Class actions burden directors, officers and the company.

SECURITIES ACT OF 1933 APPLIES TO OFFERINGS

SECTION 11 RISKS

- **Strict liability** for misstatements in IPO registration statements.
- No need for plaintiffs to prove intent or reliance.
- *Cyan* (2018) allows state and federal lawsuits, amplifying exposure
- But see *Slack* (2023) requiring direct tracing to registration statement for standing

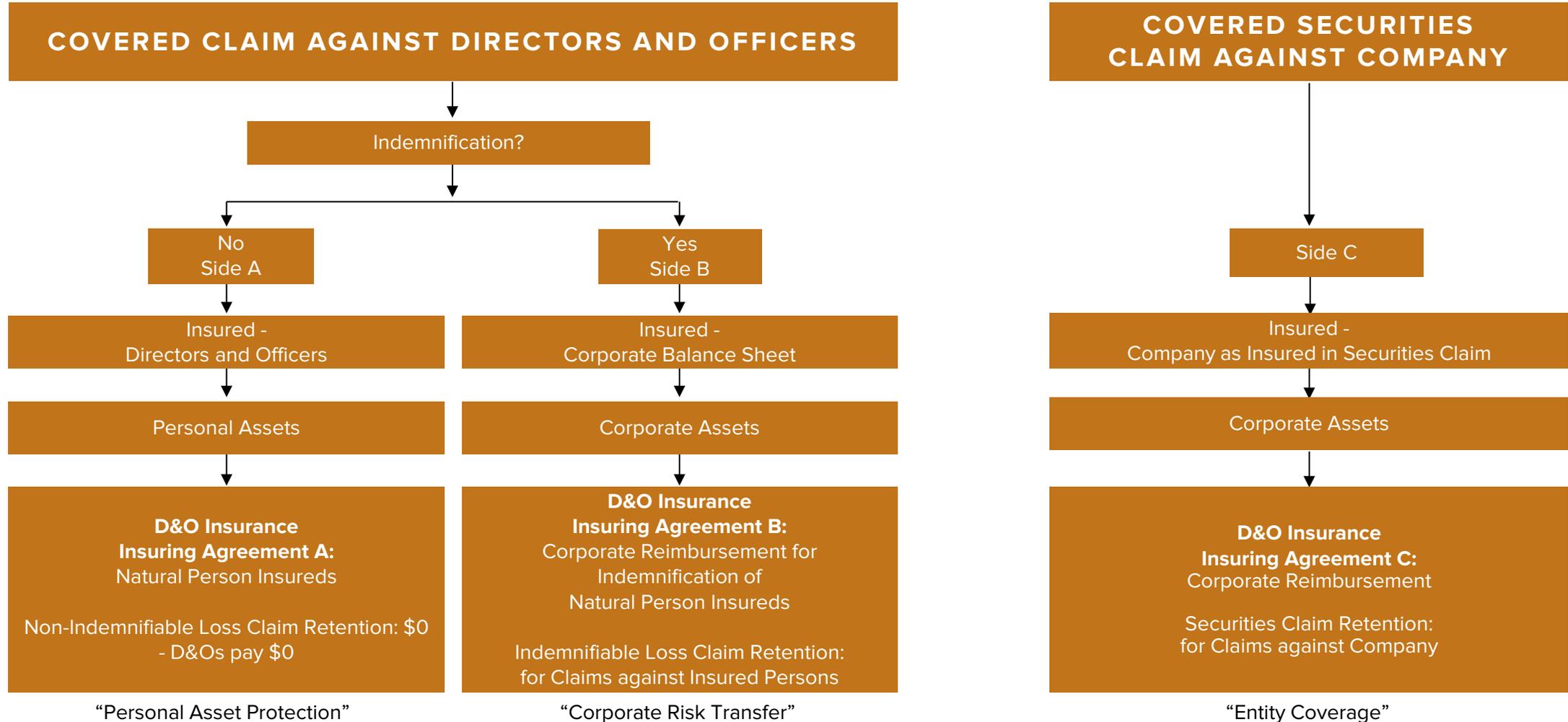
SECURITIES EXCHANGE ACT OF 1934 APPLIES TO ONGOING TRADING

RULE 10B-5 RISKS

- General anti-fraud rule and creates liability for the “maker” of materially misleading statements or omissions (note: liability theories can extend beyond the “maker” concept in some circumstances (e.g., dissemination/scheme theories))
- Requires proof of intent, reliance, and economic loss.

SHIELD YOUR TEAM WITH PROCESS DISCIPLINE, DILIGENCE AND A STRONG D&O PROGRAM

D&O Program Structure



Public Company D&O Program Mechanics

D&O “Tower”

- Built-in layers with excess markets sitting on top of the primary
- Each layer of Full Coverage shares A+B+C components across one limit

SIDE A DIC

Provides excess for non-indemnified loss with a drop-down provision

SIDE A

Provides for directors and officers when indemnification is not provided

No Retention

SIDE B

Reimburses the company for its indemnity obligations to directors and officers

SIDE C

Provides coverage to the entity when named in a securities claim

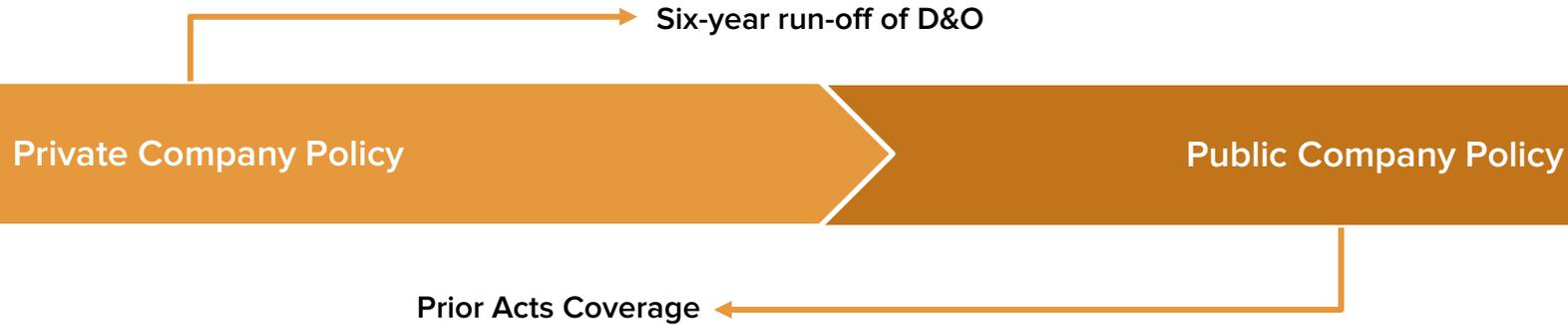
RETENTION

Hypothetical Claim and How Each Coverage Component Responds

Fact Pattern: Company discloses during their 1st public earnings release that they are going to reduce guidance associated with a new product launch and re-state historical earnings - the stock drops 25% in a single trading day

	SIDE-A DIC	SIDE-B	SIDE-C
Securities Class Action brought against a Director or Officer and the Company <u>is not indemnifying</u> them	Covered	N/A	N/A
SEC and DOJ investigation into a Director or Officer and the Company <u>is not indemnifying</u> them	Covered	N/A	N/A
Derivative Action brought against a Director or Officer which ultimately results in a settlement or judgement	Covered	N/A	N/A
Securities Class Action brought against a Director or Officer , the Company <u>is not indemnifying</u> them and the primary insurer wrongfully denies Side-A coverage	Side-A DIC Triggered	N/A	N/A
Securities Class Action brought against a Director or Officer and Company <u>is indemnifying</u> them	N/A	Covered	N/A
SEC and DOJ investigation into a Director or Officer and Company <u>is indemnifying</u> them	N/A	Covered	N/A
Securities Class Action brought against the Company	N/A	N/A	Covered
SEC and DOJ investigation into the Company	N/A	N/A	N/A

D&O Insurance: Private to Public



CONSIDERATIONS FOR PRIVATE D&O PROGRAM

- Add or increase Side A DIC coverage if needed
- Evaluate primary carriers for IPO vs. existing carrier line-up
- Negotiate run-off cost
- Review provisions of policy to ensure private company form will cover pre-combination activity, including any business combination related exposures

PUBLIC COMPANY D&O PROGRAM CONSIDERATIONS:

- Full prior acts coverage secured for pre-IPO activities with broader coverage for Insured Persons
- Public company program is preserved for more severe public company securities claim exposure including Section 11 claims

GENERAL CONSIDERATIONS:

- Companies should strongly consider forum provisions in bylaws, especially DE and CA-based entities
- Public company experience amongst board and/or management teams
- JOBS act filing vs. public prospectus filing
- Potential for direct listing or “de-SPAC” transaction and resulting impact on D&O

Underwriter's Risk Profile Analysis for IPOs

IPO CHARACTERISTICS

- Offering Size
- Expected Market Capitalization
- Selling Shareholders
- Secondary offering within next 12 months
- Lock up duration
- New shares being offered or insiders / sponsors selling
- Classes of stock (voting vs. regular common)
- Makeup of shareholder base
- Float (insiders vs. public shareholders)
- Use of proceeds
- Strength of bankers and outside counsel
- Indemnification obligations to bankers

COMPANY-SPECIFIC ISSUES

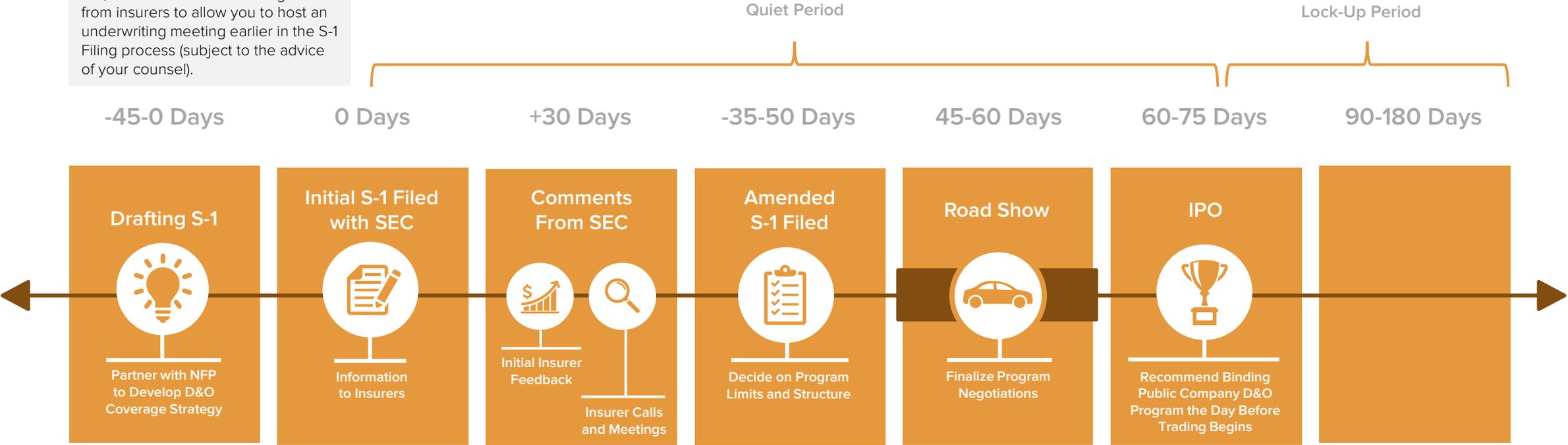
- Financials and access to capital (debt markets)
- Will the Company pursue a credit rating?
- Management's experience, track record and continuity
- Operational differentiators
- Regulatory relationships and track record
- Profitability history
- Revenue diversity
- Industry outlook
- Competitive landscape
- Litigation history
- M&A history and outlook
- Plans to offer guidance
- Exclusive venue in by-laws?

CONTROLS & CORPORATE GOVERNANCE

- Financial controls – Time frame of becoming Sarbanes Oxley compliant
- Internal Audit and relationship with outside auditors
- Disclosure practices
- Insider trading policies – details of any 10(b)5-1 plans
- Ethics policy
- Board composition
- Committee functions
- Outlook for management or board changes
- Compliance program
- Noteworthy related party transactions
- ISS commentary

The IPO Placement Timeline

If filing confidentially under the JOBS Act, we recommend obtaining NDAs from insurers to allow you to host an underwriting meeting earlier in the S-1 Filing process (subject to the advice of your counsel).



PRIVATE COMPANY D&O CONSIDERATIONS

- Discuss Run-off Options or Policy Cancellation

PUBLIC COMPANY D&O CONSIDERATIONS

- Increase Limit
- Expect Significantly Higher Retention and Premium
- Purchase Additional Dedicated Side-A Coverage