D&O AND FINANCIAL INSTITUTIONS PREDICTIONS 2025

DAC BEACHCROFT

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1. The increase in climate and ESG-focused corporate disclosures will fuel shareholder litigation

The 'anti-greenwashing' rules recently announced by the Financial Conduct Authority (FCA), aimed at ensuring that managers of UK based investment funds are correctly labelling their investment products, are a further example of the FCA's hardening approach to companies that make misleading statements to their customers. With a greater focus on climate and wider environmental, social and governance issues, corporate disclosures and statements are being closely scrutinised for accuracy and they are providing fertile ground for shareholder litigation in England and Wales. Claims are typically pursued under s90 and s90A of the Financial Services and Markets Act 2000, which provide a path to redress for shareholders of listed companies if they have allegedly suffered loss due to untrue or misleading statements. Activists are increasingly buying stakes in companies in order to use their shareholding to hold officeholders to account and challenge corporate behaviour. The increase in regulation, alongside an increasingly active investor population, will continue the growth of shareholder litigation.

2. The litigation funding market faces a long wait for clarification

The omission of the Litigation Funding Agreements (Enforceability) Bill in the King's Speech in July 2024 was surprising. The Bill would have reversed the Supreme Court's decision in the PACCAR judicial review and clarified the enforceability of litigation funding agreements (LFAs) by amending s58AA of the Courts and Legal Services Act 1990 and confirming LFAs are not damages-based agreements. The government is set to conclude its general review of the litigation funding sector, including the need for greater regulation and safeguards to protect claimants, by Summer 2025. Uncertainty over the enforceability of LFAs is therefore now set to continue for at least another year. Such a long wait is disappointing for the litigation funding industry and restricts the vital funding options available to individuals and small businesses, potentially preventing them from accessing justice and pursuing claims against better resourced corporations.

3. Financial institutions are appointing CAIOs to oversee AI initiatives and reduce the risk of consumer claims

AI has reshaped the financial services industry. It is widely used to summarise information, automate credit and loan decisions, detect and prevent fraud, drive operational efficiency and productivity, and reduce the risk of human error. But if AI learns from incomplete or imperfect data, there is a significant risk of unintended discrimination or unconscious bias, and unchecked reliance on AI could affect large data sets within a customer base and ultimately lead to claims for consumer redress. Recognising the critical importance of AI to corporate strategy and operations and the claims risk, financial institutions are increasingly appointing Chief AI Officers (CAIOs) to oversee the execution and integration of AI projects, promote ethical AI-practices, and ensure the adoption of AI aligns with corporate vision and regulatory requirements.

4. New duty on employers to prevent sexual harassment is likely to lead to an increase in claims

On 26 October 2024, a new positive duty on employers to take "reasonable steps" to prevent sexual harassment in the workplace came into force. Employers must now proactively implement measures to embed a respectful work culture through zero-tolerance policies, staff training on inappropriate conduct, and effective and sensitive complaints handling procedures. Neglecting to prepare for this new duty could lead to an increase in harassment claims and more compensation. If an employee succeeds with a claim for sexual harassment and the employer has breached the new duty, the tribunal can increase compensation by up to 25%. The Equality and Human Rights Commission (EHRC) can also investigate and take enforcement action. Action can be taken based on a suspicion of non-compliance; there does not need to be an incident of sexual harassment before the EHRC will consider exercising its enforcement powers.

5. The Economic Crime and Corporate Transparency Act 2023 will put companies and directors under the microscope

Fraud offences in the UK are changing. The Economic Crime and Corporate Transparency Act 2023 (ECCTA) creates a new "failure to prevent fraud" offence, committed when an employee of a large organisation perpetrates a fraud and the organisation has failed to implement reasonable fraud prevention measures. ECCTA also reforms the identification principle, making it easier to attribute criminal liability to corporations for economic crimes committed by a 'senior manager' acting within the actual or apparent scope of their authority. This represents a substantial widening of potential liability, as the definition of senior manager is broader than the board of directors and may include any individual with substantial management authority. ECCTA brings a greater risk of corporate and D&O prosecutions, and therefore organisations must implement robust fraud prevention procedures and safeguards to oversee the conduct of their senior managers. The consequences of non-compliance will otherwise be severe.

6. Insolvency practitioners will continue to target directors of failed companies

High levels of corporate failure in the UK mean that claims against directors remain prevalent. Insolvency practitioners seeking to recoup funds for creditors continue to review the actions of directors prior to the insolvency process. The high-profile court decision in 2024 against former directors of BHS was notable for the liquidators succeeding with a novel claim of trading misfeasance in addition to their wrongful trading claim. This decision will give liquidators encouragement and potentially opens a new avenue for recovering assets from directors of insolvent companies and their D&O insurers.

7. The transition to renewables will unearth new risk exposures

While the output from renewable energy is green, the same is not true for every aspect of the process. The mining and extraction of rare earth materials required may generate significant carbon emissions and create various additional risks. Litigation or allegations relating to breaches of sustainability regulations could generate financial losses for companies. These losses may not only be direct, but also as a consequence of reputational harm. Those financial losses could generate claims from shareholders who have been adversely affected, leading to claims under directors and officers policies. Mining and extraction may also involve dangerous working conditions and raise questions around the human rights of inhabitants of these locations. Litigation relating to the placement of renewable energy infrastructure is also likely to increase. There is also a disconnect between the ambition of the circular economy and recycling of equipment that is now reaching end-of-life. Looking forward, managing expectations around renewables should form part of the ambit of risk manager, broker and insurer discussions.

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