

Social Media: Officer and Director Liability

Leigh Chiles and Stacie Winkler
Shareholders
Baker, Donelson, Bearman, Caldwell &
Berkowitz, PC
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How is Social Media Defined?

Social media includes web-based and mobile based technologies which are used to turn communication into interactive dialogue between organizations, communities, and individuals.

- **Popular social media sites**

- Facebook
- Twitter
- Linked-In
- Pinterest
- YouTube
- Internet Forums
- Blogs
- Podcasts



Major Areas of Concern for Director and Officer Liability

- Duties of directors
 - Duty of Care
 - Duty of Loyalty
- Additional duties may be imposed based on financial considerations of company
 - i.e. duties to creditors
- Personal liability



Officers v. Directors and Other Caveats

- Generally officers owe the same duties as directors
- Officers may owe duty to keep the Board informed
- Officers with greater knowledge and involvement may be subject to higher level of scrutiny
- Duties may be statutory in nature
 - Taxes and wages
 - Payment of dividends
 - Fraudulent transfers
 - Breach of duty to ERISA plan



Duties

- Duty of care
 - Governed by statute in most states
 - Tenn. Code Ann. § 48-2-101 *et seq.* (see § 48-18-301 *et seq.*)
 - Requires directors to discharge their duties in good faith and with the care of an ordinary prudent person in a like position under similar circumstances and in a manner the director reasonably believes to be in the best interests of the corporation
 - This is the “standard of care”
- Duty of loyalty
 - Requires directors to act on behalf of the corporation and its shareholders and refrain from acts of self-dealing

Business Judgment Rule

- Discharge of duties is measured against this rule
- Developed by courts in reviewing the actions of directors
- Directors not personally liable for a business decision (even when a decision turns out to be a bad one) so long as the director has not breached a duty to the corporation
- Requires that a director act in good faith, remain informed about the corporation’s business, and not engage in self-dealing or transactions involving conflicts of interest



Business Judgment Rule

- No protection is provided when director:
 - has personal financial interest in transaction
 - lacked independence
 - did not inform himself/herself of all information that was reasonably available
 - failed to exercise requisite level of care
 - stood on both sides of transaction



Social Media in the Boardroom: Where are We?

- *Deloitte Ethics and Workplace Survey*
 - 58% of executives felt that the reputational risk associated with social networking should be a board room issue
 - 17% of executives said that they currently had programs in place to monitor and mitigate reputational risks that may arise with social network usage
 - Social media largely left to management to figure out social media strategy



How does Social Media Affect Officers and Directors?

- Knowledge of information contained on social media sites
- Knowledge of policies and procedures of corporation for usage
- Usage by a director or officer



Knowledge of Information Contained on Social Media Sites

- Directors are responsible for oversight of the corporation
 - Includes monitoring and advising senior executive team
 - Can provide insights into traditional key performance indicators (KPIs)
 - Example- Proctor & Gamble
 - Developed dashboard that analyzes blogs, tweets and social media to summarize consumer sentiment
 - CEO Robert McDonald personally reviews each report

Knowledge of Information Contained on Social Media Sites

- Directors need to understand risks facing corporation including:
 - Operational, reputational, and compliance risk
- Social media- effective early warning in above areas
 - Example- Eli Lilly
 - Sales reps discussed selling drug for off label use months before news was available in mainstream media
 - Example- Nestle
 - Company was criticized in social media about environmentally unsound practices of supplier
 - Neither company monitored social media, and thus were unable to proactively address these issues, which damaged the brands

Knowledge of Information Contained on Social Media Sites

- Duty of Care
 - In making decisions, directors must discharge their duties with the care of an ordinary prudent person in a like position under similar circumstances
 - Business Judgment Rule does not apply when director did not inform himself/herself of all information that was reasonably available
- Information contained in social media, especially when related to the company's site or closely related site (employees posts), is almost always "reasonably available"

Knowledge of Information Contained on Social Media Sites- Problems

- Reasons to NOT have access to this information
 - Responsibilities of directors different from those of management
 - Law provides that board may rely on information from management
 - Might not be accurate
 - Might encourage direct interaction with stakeholders

CAUTION

Knowledge of Policies and Procedures of Corporations Usage

- Exposures existed prior to social media BUT:
 - Reach is broader and quicker
 - Difficult to control once posted
- Areas of concern (current hot topics)
 - Employment Decisions
 - Defamation
 - Invasion of Privacy/ Disclosure of Confidential Information
 - Copyright/ Trademark



Knowledge of Policies and Procedures of Corporations Usage

- In order to discharge duty of care, officers and directors need to consider:
 - Legal risks
 - Especially in area of human resources (Does the director know how social media is being used in hiring and firing?)
 - Business practices
 - What is industry standard?
 - Prepare a written policy for all employees at all levels
 - Disclosure
 - Shareholders need to be informed about policies and risks
 - May be disclosed on annual report

Knowledge of Policies and Procedures of Corporations Usage

- Risk management
 - Undertake an initial risk assessment
 - Take into account potential damage from incidents and cost of opportunity in not using social media
- Monitoring
 - Ensuring that internal controls are in place
- Communication
 - Determine type of information that will be received and disseminated by corporation through social media



Usage by a Director or Officer

- Statistics
 - 70% of Fortune 500 CEOs have no social media presence
 - Most popular for CEOs is LinkedIn- 26% of executives had pages
 - general population- 20% LinkedIn
 - 36 CEOs have 0 connections; 10 have more than 500
 - Only 7.6% of CEOs on Facebook; 4% on Twitter
 - general population- 50% Facebook; 34% on Twitter
 - Less than 1% on Google Plus; 0% on Pinterest
 - 6 CEOs contributed to blogs
 - Only 1 CEO maintained his own blog- John Mackey (Former CEO of Whole Foods)

Usage by an Officer or Director

- Directors and officers are subject to greater regulation and scrutiny when engaging in social media themselves
- Example- John Mackey, Former CEO of Whole Foods
 - Posted numerous messages on a Yahoo financial forum under the user name "rahodeb"
 - Came to light during an FTC investigation during planned takeover of Wild Oats Markets Inc. (painted a bright future for Whole Foods Market Inc. and downplayed the threat posed by competitors)
 - SEC considered whether the CEO had selectively disclosed material corporate information (violating Regulation Fair Disclosure)
 - Cleared of charges on April 25, 2008

Industry Specific Risks with Social Media

- Healthcare/ health information
 - Directors and officers need to understand how this information is being protected
 - Implicates HIPAA, HITECH and Tennessee state law
- Financial institutions
 - Directors and officers need to understand what regulations already exist
 - Implicates FINRA



Specific Risks- Health Information Related

- **The Health Insurance Portability and Accountability Act (HIPAA)**
 - HIPAA Privacy
 - Protects the privacy of individually identifiable health information
 - Disclosure only allowed under certain defined circumstances
 - HIPAA Security
 - Sets national standards for the security of electronic protected health information
 - Providers must keep protected health information secure

Specific Risks- Health Information Related

- **Health Information Technology for Economic and Clinical Health (HITECH)**

- Under HITECH, the government can bring charges against facilities that have violated patient privacy
- The Act strengthens the provisions of HIPAA and patient privacy.



Specific Risks- Health Information Related

- **Tenn. Code Ann. § 68-11-1502- Tennessee Patient Privacy Law**

- Every patient entering and receiving care at a health care facility licensed by the board for licensing health care facilities has the expectation of and right to privacy for care received at such a facility.
- A patient's expectation that his or her medical records will remain private has constitutional, statutory, and decisional protection, *McNeil v. Cooper*, 241 S.W.3d 886 (2007).
- This protection extends to information that is displayed on social media websites.

Specific Risks- Financial Institution Related

- FINRA
 - Regulatory Notice 10-06, Guidance on Blogs and Social Networking Sites
 - Required to retain records of communications related to broker-dealer's business made through social media
 - If a firm recommends a security through social media, triggers the requirements of NASD Rule 2310
 - Firms must monitor interactive electronic communications
 - Third party posts may become attributable to a firm



TIPS AND PRACTICAL CONSIDERATIONS

Tips to Minimize Director and Officer Liability in Social Media

- Put in place a clear, defined policy for directors and officers as it relates to their social media use on behalf of the corporation
- Consider D&O or E&O Insurance policy that covers social media
 - D&O policy with personal injury and/or publishers liability may be inadequate- sometimes includes “professional services exclusion” that applies to all media activities
 - E&O policies tend to be more geared toward media activities
- For corporations that do not have D&O policies, ensure some sort of insurance coverage for social media activities
 - Homeowner’s (usually does not cover media activities) or personal umbrella policies

Social Media- Check list for D&O/ E&O Policies

- General Issues
 - Is the dollar amount of the coverage sufficient?
 - Are the premium payments competitive?
 - Is the deductible too large?
 - Are legal fees covered?
 - Does the insurer promise to advance the costs of legal fees in the event of a claim or merely reimburse for out of pocket costs?

Social Media- Check list for D&O/ E&O Policies

- Social Media Specific
 - Does the policy cover all directors and officers or do they have to be specifically named? Does the policy also cover the corporate entity?
 - When must claims be made?
 - Does the insured have any experience paying claims related to social media?
 - Are the exclusions from coverage too broad?
 - These may be negotiable.
 - Are their special endorsements that may be appropriate?
 - What offsets from coverage apply?

Sites to Keep Informed of Changing Social Media Laws for Officer and Director Liability

- www.facebook.com/socialmedialaws
- www.boardmember.com
- <http://www.hubdando.com>
- www.allbusiness.com

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