SEXUAL MISCONDUCT & SECURITIES DISCLOSURE IN THE "#METOO" WORLD

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INTRODUCTION

Beginning on October 5, 2017, the *New York Times* and the *New Yorker* reported that more than a dozen women accused Harvey Weinstein, former co-chairman of The Weinstein Company, of sex-

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ual harassment, assault, or rape.[1] In all, more than eighty women (and counting) have made allegations of sexual misconduct[2] against Weinstein.[3] As a result, Weinstein was fired from his production company,[4] divorced by his wife,[5] sued in civil court,[6] and investigated for[7] and charged with several crimes.[8] The allegations

1. Ronan Farrow, *Sexual Assault: Harvey Weinstein's Accusers Tell Their Stories*, NEW YORKER (Oct. 23, 2017), https://www.newyorker.com/news/news-desk/from-aggressive-overtures-to-sexual-assault-harvey-weinsteins-accusers-tell-their-stories [https://perma.cc/K2S5-LJD4] (reporting on, following a ten-month investigation, the accusations of thirteen women who said that Harvey Weinstein sexually harassed or assaulted them); Jodi Kantor & Megan Twohey, *Harvey Weinstein Paid Off Sexual Harassment Accusers For Decades*, N.Y. TIMES (Oct. 5, 2017), https://www.nytimes.com/2017/10/05/us/harvey-weinstein-harassment-allegations.html [https://perma.cc/4WTV-UT4E] (reporting on sexual harassment and assault charges made against Harvey Weinstein).

2. This Note uses the term "sexual misconduct" as an umbrella term for all wrongful, improper, or unlawful conduct of a sexual nature.

3. Sara M Moniuszko & Cara Kelly, *Harvey Weinstein Scandal: A Complete List of the 85 Accusers*, USA TODAY (Oct. 27, 2017, 11:27 AM), https://www.usatoday.com/story/life/people/2017/10/27/weinstein-scandal-complete-list-accusers/804663001/ [https://perma.cc/KKH2-L5SP].

4. Megan Twohey, *Harvey Weinstein Is Fired After Sexual Harassment Reports*, N.Y. TIMES (Oct. 8, 2017), https://www.nytimes.com/2017/10/08/business/harvey-weinstein-fired.html [https://perma.cc/GAH8-BBGX].

5. Pat Saperstein, *Harvey Weinstein's Wife Georgina Chapman Divorcing Him*, VARIETY (Oct. 10, 2017, 4:29 PM), https://variety.com/2017/film/news/harvey-weinstein-wife-georgina-chapman-divorcing-divorce-1202586378/ [https://perma.cc/52X5-RG9Z].

6. *See* Alex Dobuzinskis, *Judge Allows Ashley Judd Defamation Lawsuit Against Weinstein to Proceed*, REUTERS (Sept. 19, 2018, 7:35 PM), https://www.reuters.com/article/us-people-ashley-judd-weinstein/judge-allows-ashley-judd-defamation-lawsuit-against-weinstein-to-proceed-idUSKCN1LZ2ZX [https://perma.cc/66XH-H8DY]; James C. McKinley Jr., *3 Women Accuse Weinstein of Sexual Assault in Federal Suit*, N.Y. TIMES (June 1, 2018), https://www.nytimes.com/2018/06/01/nyregion/harvey-weinstein-class-action-suit.html [https://perma.cc/66XH-H8DY].

7. *See* Richard Winton & Victoria Kim, *Investigation Launched After Actress Tells LAPD She Was Raped by Harvey Weinstein*, L.A. TIMES (Oct. 19, 2017, 4:05 PM), http://www.latimes.com/local/lanow/la-fi-ct-weinstein-lapd-victim-20171019-story.html [https://perma.cc/BF73-S7JP] (reporting that police investigations were launched in Los Angeles, New York City, and London); Nicole Hong and Bradley Hope, *Federal Prosecutors Exploring New Charges Against Harvey Weinstein*, WALL ST. J. (Sept. 6, 2018, 5:10 PM), https://www.wsj.com/articles/federal-prosecutors-exploring-new-charges-against-harvey-weinstein-1536268233 [https://perma.cc/W3NS-QRFJ] (reporting that federal prosecutors are investigating Weinstein's attempts to silence his accusers).

8. Press Release, Manhattan Dist. Attorney's Office, District Attorney Vance Announces Additional Charges Against Harvey Weinstein Including Predatory Sexual Assault (July 2, 2018), https://www.manhattanda.org/district-attorney-vance-announces-additional-charges-against-harvey-weinstein-including-predatory-sexual-assault/ [https://perma.cc/DPD5-DW5A].

against Weinstein also inspired actress Alyssa Milano to tweet on October 15, 2017, "If you've been sexually harassed or assaulted write 'me too' as a reply to this tweet."[9]

#MeToo quickly accelerated into a movement that encouraged individuals to share their stories as victims of sexual misconduct. By October 16, 2017, "'#MeToo' was used more than 500,000 times on Twitter and in 12 million posts on Facebook."[10] As a result, the number of "public" accusations of sexual misconduct surged.[11] Celebrities throughout media, sports, and politics were among those accused.[12] Likewise, prominent executives of public companies were alleged to have committed sexual misconduct.[13] The fall from grace for the accused was profound—many suddenly faced career-related, personal, and even criminal consequences.[14]

The #MeToo movement has had a negative impact on companies affiliated with individuals accused of sexual misconduct. Accusations of corporate sexual misconduct have led to employment arbitrations,[15] civil rights inquiries,[16] shareholders' derivative ac-

9. Alyssa Milano (@Alyssa_Milano), TWITTER (Oct. 15, 2017, 1:21 PM), https://twitter.com/alyssa_milano/status/919659438700670976?lang=en [https://perma.cc/AV7V-SNST].

10. Nicole Smartt Serres, *Sexual Harassment in the Workplace in a #MeToo World*, FORBES (Dec. 20, 2017, 9:00 AM), https://www.forbes.com/sites/forbeshumanresourcescouncil/2017/12/20/sexual-harassment-in-the-workplace-in-a-metoo-world/#751eb6ea5a42 [https://perma.cc/44JB-QJ5B].

11. *See infra* Appendix A.

12. Among those accused are Matt Lauer (former host of "The Today Show"), Marshall Faulk (Pro Football Hall of Famer), and U.S. Senator Al Franken. Dan Corey, *A Growing List of Men Accused of Sexual Misconduct Since Weinstein*, NBC NEWS (Jan. 10, 2018, 4:34 PM), https://www.nbcnews.com/storyline/sexual-misconduct/weinstein-here-s-growing-list-men-accused-sexual-misconduct-n816546 [https://perma.cc/XZ37-YEQX].

13. *See, e.g.*, Ronan Farrow, *Les Moonves and CBS Face Allegations of Sexual Misconduct*, NEW YORKER (Aug. 6, 2018), https://www.newyorker.com/magazine/2018/08/06/les-moonves-and-cbs-face-allegations-of-sexual-misconduct [https://perma.cc/AJ3V-J9CC]; Alexandra Berzon, Chris Kirkham, Elizabeth Bernstein & Kate O'Keeffe, *Dozens of People Recount Pattern of Sexual Misconduct by Las Vegas Mogul Steve Wynn*, WALL ST. J. (Jan. 27, 2018, 1:02 AM), https://www.wsj.com/articles/dozens-of-people-recount-pattern-of-sexual-misconduct-by-las-vegas-mogul-steve-wynn-1516985953 [https://perma.cc/PXY7-ZPE3].

14. Stephanie Zacharek, Eliana Dockterman & Haley Sweetland Edwards, *2017 Person of the Year: The Silence Breakers*, TIME, Dec. 18, 2018, at 36–37 ("[I]n the past two months alone, [the accusers'] collective anger has spurred immediate and shocking results: nearly every day, CEOs have been fired, moguls toppled, icons disgraced. In some cases, criminal charges have been brought.").

15. *See*, *e.g.*, Drew Harwell, *Hundreds Allege Sex Harassment, Discrimination at Kay and Jared Jewelry Company*, WASH. POST (Feb. 27, 2017), https://www.washingtonpost.com/business/economy/hundreds-allege-sex-harassment-discrimination-at-

tions,[17] class actions,[18] and regulatory investigations.[19] Moreover, the fallout from sexual misconduct allegations damages companies' brands with customers and job applicants.[20] Public companies have often faced a significant decline in stock price.[21]

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kay-and-jared-jewelry-company/2017/02/27/8dcc9574-f6b7-11e6-bf01-d47f8cf9b643_story.html?utm_term=.1c34de2bb5fc [https://perma.cc/7A53-EFHT] ("Declarations from roughly 250 women and men who worked at Sterling, filed as part of a private class-action arbitration case, allege that female employees . . . were routinely groped, demeaned and urged to sexually cater to their bosses to stay employed.").

16. *See, e.g.*, Ben Fritz, Keach Hagey & Mike Vilensky, *Deal Talks to Sell Weinstein Co. Collapse After New York Attorney General Files Lawsuit*, WALL ST. J. (Feb. 11, 2018, 10:46 PM), https://www.wsj.com/articles/new-york-attorney-general-alleges-extensive-sexual-harassment-at-weinstein-co-in-lawsuit-1518391817?mod=djem10point [https://perma.cc/T3DW-NYKA] (reporting that New York Attorney General filed lawsuit against the Weinstein Company that alleges civil-rights violations).

17. *See*, *e.g.*, Scott Flaherty, *Bernstein Litowitz Finds Role for Investors in Fight Against Sexual Harassment*, LAW.COM (Dec. 16, 2017, 9:57 PM), https://www.law.com/sites/americanlawyer/2017/12/15/bernstein-litowitz-finds-role-for-investors-in-fight-against-sexual-harassment/ [https://perma.cc/QV44-ENYR] (reporting that Twenty-First Century Fox agreed to a settlement in the face of a third-party derivative suit premised on the failure of the board of directors and senior executives to address workplace sexual harassment).

18. *See, e.g.*, Class Action Complaint, Samit v. CBS Corp. No. 1:18-cv-07796-NRB, 2018 WL 4056155 (S.D.N.Y. filed Aug. 28, 2018) [hereinafter CBS Complaint] (securities class action filed against CBS Corp.); Class Action Complaint, Ferris v. Wynn Resorts, No. 1:18-cv-01549-DLC, 2018 WL 1023165 (S.D.N.Y. filed Feb. 20, 2018) [hereinafter Wynn Complaint] (securities class action filed against Wynn Resorts).

19. Gaming regulators began investigating sexual misconduct allegations made against Wynn Resorts CEO Steve Wynn after allegations were described in a *Wall Street Journal* article. Chris Kirkham, Elizabeth Bernstein & Rebecca Ballhaus, *Steve Wynn Calls on Employees to Rally Behind Him During Company Meetings*, WALL ST. J. (Feb. 2, 2018, 5:30 AM), https://www.wsj.com/articles/steve-wynn-calls-on-employees-to-rally-behind-him-during-company-meetings-1517567401 [https://perma.cc/TKD5-EEDD] (reporting that regulators in Massachusetts, Nevada, and Macau, along with the company's board, were investigating the allegations).

20. *See* FTI CONSULTING & MINE THE GAP, #METOO AT WORK: OVERALL AND WOMEN BY INDUSTRY TOPLINE REPORT (2018), https://www.gender.fticommunications.com/pdf/MeToo_at_Work-research.pdf [https://perma.cc/H8QA-2TPR] (survey showing that 55% of professional women are less likely to apply for a job and 49% are less likely to buy products or stock from a company with a public #MeToo allegation). *See also* Jeremy J. Sierra, Nina Compton & Kellilynn M. Frias-Gutierrez, *Brand Response-Effects of Perceived Sexual Harassment in the Workplace*, 14 J. BUS. & MGMT. 175, 187 (2008) (finding that "perceived sexual harassment in the workplace has a negative effect on attitudes toward the brand, brand image, and intentions to work for prospective employees").

21. *See infra* Appendix B.

Sexual misconduct raises an additional concern for public companies in the form of disclosure liability under federal securities laws (disclosure liability). Disclosure liability arises when a company neglects an affirmative duty to disclose a material fact,[22] or when it voluntarily states a material fact untruthfully or incompletely.[23] Securities laws are flexible enough to encompass sexual misconduct, however,[24] because disclosure liability largely revolves around the concept of "materiality."[25] What is considered a "material" fact is not fixed, but instead incorporates new issues, like sexual misconduct, over time.[26]

Thus far, the business community appears to have overlooked this serious risk.[27] Following the #MeToo movement, however, public corporations face a real risk that sexual misconduct will be deemed material and will give rise to obligatory disclosure. For one thing, sexual misconduct is now more likely to be reported and to

22. *See* SEC, FAST ANSWERS: FORM 10-K (2009), https://www.sec.gov/fast-answers/answers-form10khtm.html [https://perma.cc/G8NM-Q3LD] ("The federal securities laws require public companies to disclose information on an ongoing basis. For example, domestic companies must submit annual reports on Form 10-K, quarterly reports on Form 10-Q, and current reports on Form 8-K for a number of specified events and must comply with a variety of other disclosure requirements.").

23. Under Rule 10b-5, it is unlawful for any person "to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading . . . in connection with the purchase or sale of any security." 17 C.F.R. § 240.10b-5(b) (2019).

24. *In re* ProShares Tr. Sec. Litig., 728 F.3d 96, 102 (2d Cir. 2013) ("[F]ederal securities laws are dynamic and respond to changing circumstances.").

25. *See* BUS. ROUNDTABLE, THE MATERIALITY STANDARD FOR PUBLIC COMPANY DISCLOSURE: MAINTAIN WHAT WORKS 1 (2015), https://s3.amazonaws.com/brt.org/archive/reports/Materiality%20White%20Paper%20FINAL%2009-29-15.pdf [https://perma.cc/28M7-SJWN] (stating that "for approximately eight decades, the principle of materiality has been embedded in the disclosure framework that governs how public companies disclose information to the investing public"). For example, SEC Regulation S-K, Item 103 requires that public companies disclose "*material* pending legal proceedings." 17 C.F.R. § 229.103 (2019) (emphasis added). Additionally, SEC Rule 10b-5 precludes corporations from misstating or omitting *material* information. *See* 17 C.F.R. § 240.10b-5 (2019).

26. For example, the SEC in 2010 issued disclosure guidance regarding material events related to climate change. *See, e.g.*, Commission Guidance Regarding Disclosure Related to Climate Change, Securities Act Release No. 9106, Exchange Act Release No. 61469, Fed. Sec. L. Rep. (CCH) ¶ 88,853 (Feb. 8, 2010) ("In addition to legislative, regulatory, business and market impacts related to climate change, there may be significant physical effects of climate change that have the potential to have a material effect on a registrant's business and operations.").

27. *See* analysis *infra* Section II.A.

be considered a material factor in investor decision making.[28] In addition, the salacious and highly-charged nature of the issue makes it more likely that companies will face both public[29] and private[30] enforcement efforts when they fail to disclose sexual misconduct. While it can be difficult at times to comply with uncertain legal standards such as disclosure rules tied to a materiality standard,[31] one can make generalizations about when and what companies need to disclose when there is proven or alleged sexual misconduct.[32]

This Note will examine the disclosure challenges corporations face while grappling with sexual misconduct issues in the #MeToo world.[33] Part I overviews the disclosure regime surrounding securities enforcement, including the relevant statutes, rules, concepts, and goals. Part II will discuss the #MeToo movement, its impact on disclosure liability, and trends in disclosure liability lawsuits. This

28. *See* analysis *infra* Section II.A.

29. *See infra* Section II.B.1.

30. *See infra* Section II.B.2.

31. *See* James J. Park, *Rules, Principles, and the Competition to Enforce Securities Laws*, 100 CALIF. L. REV. 115, 142 (2012) (noting that principle-enforcement, a broader and thus stricter form of enforcement, can lead to a "chilling effect where parties will be overly cautious for fear that they will be punished for acts that a regulator determines ex post is misconduct"); *see also* John E. Calfee & Richard Craswell, *Some Effects of Uncertainty on Compliance with Legal Standards*, 70 VA. L. REV. 965 (1984) (noting that uncertain legal standards incentivize over- or under-compliance).

32. *See* analysis *infra* Part III.

33. While this Note narrowly focuses on the #MeToo movement's impact on sexual misconduct disclosure liability for corporations, commentators have also begun to explore the influence of #MeToo on other legal regimes and parties. For example, Tippett summarizes the implications of the #MeToo movement for employment law and employment practices. Elizabeth Chika Tippett, *The Legal Implications of the MeToo Movement*, MINN. L. REV. (forthcoming) (manuscript at 1), https://ssrn.com/abstract=3170764. Wexler et al. explore the meaning, utility, and complexities of restorative and transitional justice for dealing with sexual misconduct in the workplace. Lesley Wexler, Jennifer K. Robbennolt & Colleen Murphy, *#MeToo, Time's Up, and Theories of Justice* 1 (Univ. of Ill. Coll. of Law Legal Studies, Working Paper No. 18-14, 2018), https://ssrn.com/abstract=3135442. Finally, Hemel and Lund analyze strategically and normatively why corporate law should be invoked to remedy workplace-based sexual misconduct, and broadly discuss whether and when companies might face corporate liability in connection with such misconduct. Daniel Jacob Hemel & Dorothy Lund, *Sexual Harassment and Corporate Law* 1 (U. of Chi. Coase-Sandor Inst. for Law & Econ., Working Paper No. 661, 2018), https://ssrn.com/abstract=3147130. They conclude that sexual harassment law and corporate law can be complementary, and that the use of corporate law to regulate and remedy sexual harassment can benefit employees, shareholders, and society. *Id.* at 1, 69.

Part will argue that the risk of sexual misconduct disclosure liability and enforcement is real and growing, despite the fact that public companies do not give it sufficient attention. Part III will recommend when and what companies should disclose with regard to alleged and proven sexual misconduct. Essentially, a corporation must first determine if sexual misconduct is a material event, the determining factors being whether a key executive or a significant number of lower-level employees are implicated. Then, a company must determine whether an affirmative duty to disclose is triggered. Even if not, companies should be mindful of Rule 10b-5[34] restrictions, as pre-detection statements can lead to a duty to correct or update, and post-detection statements must be made completely and truthfully. The Note concludes by recommending that companies err on the side of disclosure or at the very least incorporate sexual misconduct disclosure liability into their disclosure conversations, given the potent nature of sexual misconduct issues in the #MeToo world.

I.
SECURITIES DISCLOSURE STATUTES, RULES, AND CONCEPTS

A. Federal Securities Regulation in America: The Importance of Disclosure

Congress enacted the Securities Act of 1933 (the 33 Act) and the Securities Exchange Act of 1934 (the 34 Act) after the 1929 stock market crash and during the resultant Great Depression.[35] The 33 Act enforces disclosure of material facts in connection with the distribution of new securities, while the 34 Act requires continuing disclosure from public companies.[36] A key goal of both acts is to provide investors with information about securities and their issuers in order to prevent the fraudulent practices and speculative frenzy that were thought to have caused the 1929 stock market crash.[37]

34. 17 C.F.R. § 240.10b-5 (2019).

35. The 33 Act was enacted on May 27, 1933. Securities Act of 1933, Pub. L. No. 73-22, 48 Stat. 74 (1933). The 34 Act was enacted on June 6, 1934. Securities Exchange Act of 1934, Pub. L. No. 73-291, 48 Stat. 881 (1934).

36. *See, e.g.*, Elisabeth Keller, *Introductory Comment: A Historical Introduction to the Securities Act of 1933 and the Securities Exchange Act of 1934*, 49 OHIO ST. L.J. 329, 347 (1988).

37. The 33 Act and the 34 Act were enacted "in an effort to eliminate certain abuses in the financial markets which were believed to have contributed to the famous stock market crash of October 1929, and to the devastating depression which followed." Philip A. Loomis, Jr., *Securities Exchange Act of 1934 and the Invest-*

Prior to the 33 Act and 34 Act, states undertook regulation of corporate securities through the use of "blue sky" laws and stock exchanges' required listing requirements.[38] However, for a variety of reasons, these measures were largely ineffective.[39]

Investigations by the Senate Banking and Currency Committee in the 1930s exposed a variety of private efforts to manipulate prices of specific stocks and the markets as a whole.[40] The investigations also revealed that almost half of securities issued in the decade after World War I were worthless.[41] These revelations galvanized broad public support for securities regulation and led legislators to believe that securities dealers had not conducted themselves in a fair or honest manner in the absence of federal regulation.[42] Congress determined that the absence of a disclosure regime facilitated manipulation, speculation on inside information, and other improper practices.[43]

The ultimate impetus for securities regulation, however, came from Franklin Delano Roosevelt. In his first month in office, Roosevelt campaigned for securities regulation in a message to Congress, recommending "legislation for Federal supervision of traffic in investment securities in interstate commerce."[44] The aim of the legislation would be to provide "full publicity and informa-

ment Advisers Act of 1940, 28 GEO. WASH. L. REV. 214, 216–17 (1959). Ultimately, the 33 Act and 34 Act were passed, with disclosure serving as their cornerstone. *See* Keller, *supra* note 36, at 344–47; *see also* Loomis, *supra*, at 226 (stating that the 33 Act and 34 Act combine "to establish a comprehensive scheme of disclosure to investors"). R

38. *See* Keller, *supra* note 36, at 331–34. R

39. *Id.* at 332–34 ("In reality, the laws proved quite ineffective for several reasons.").

40. *See* JOEL SELIGMAN, THE TRANSFORMATION OF WALL STREET: A HISTORY OF THE SECURITIES AND EXCHANGE COMMISSION AND MODERN CORPORATE FINANCE 16–17 (3d ed. 2003) (including reports of insider trading by corporate executives and family members, and of a public relations person who paid over $300,000 to reporters to manipulate news coverage of public companies).

41. H.R. REP. NO. 73-85, at 2 (1933), *reprinted in* 2 LEGISLATIVE HISTORY OF THE SECURITIES ACT OF 1933 AND SECURITIES EXCHANGE ACT OF 1934, item 18 (comp. by J.S. Ellenberger & E. Mahar 1973) ("During the post-war decade some 50 billions of new securities were floated in the United States. Fully half or $25,000,000,000 worth of securities floated during this period have been proved to be worthless.").

42. *Id.*

43. H.R. REP. NO. 73-1383, at 11 (1934) ("There cannot be honest markets without honest publicity. Manipulation and dishonest practices of the market place thrive upon mystery and secrecy.").

44. President Franklin D. Roosevelt, Address to Congress (March 1933), *as reprinted in* MICHAEL F. PARRINO, TRUTH IN SECURITIES; AN INTRODUCTORY GUIDE TO THE SECURITIES ACT OF 1933 23 (1968).

tion, and that no essentially important element attending the issue [of securities] shall be concealed from the buying public."[45] Yet, the legislation would not provide a guarantee to the public "that newly issued securities are sound in the sense that their value will be maintained or that the properties which they represent will earn profit."[46]

On May 27, 1933, less than two months after Roosevelt's message to Congress, the 33 Act was written, passed, and ultimately reflected Roosevelt's conception of the legislation.[47] Indeed, the purpose of the 33 Act, as stated in its preamble, was "to provide full and fair disclosure of the character of securities sold in interstate commerce and foreign commerce and through the mails, and to prevent fraud in the sale thereof, and for other purposes."[48] But the 33 Act was actually rather limited in its official scope, dealing only with the issuance of new stock and imposing only civil liability for violations of the act.

Roosevelt returned to Congress in 1934 to ask for additional securities regulation, stressing the need for legislation that "has teeth in it."[49] Ultimately, the inadequacies of the 33 Act "and the need for an independent administrative body to enforce the federal securities laws, regulate stock market practices, and curb the evils in the stock exchanges themselves led Congress to enact the [34 Act]."[50] The 34 Act addressed a number of securities-related topics, including the requirement of adequate disclosure by securities issuers.[51] The 34 Act's reporting requirements complement the registration requirements of the 33 Act to establish a comprehensive scheme of required disclosure.[52] In addition, the statute created the Securities and Exchange Commission (SEC) and gave it certain rule-making and enforcement powers.[53]

45. *Id.* at 24.

46. *Id.*

47. James M. Landis, *The Legislative History of the Securities Act of 1933*, 28 GEO. WASH. L. REV. 29, 34 (1959). ("Our draft remained true to the conception voiced by the President in his message of March 29, 1933 to the Congress, namely that its requirements should be limited to full and fair disclosure of the nature of the security being offered and that there should be no authority to pass upon the investment quality of the security.").

48. Securities Act of 1933, ch. 38, tit. 1, Pub. L. No. 73-22, 48 Stat. 74 (1933).

49. Seligman, *supra* note 40, at 95. R

50. Keller, *supra* note 36, at 347. R

51. *See* Loomis, *supra* note 37, at 217. R

52. *Id.* at 226 (stating that the 33 Act and 34 Act combine "to establish a comprehensive scheme of disclosure to investors").

53. *Id.* at 217.

The importance of disclosure to securities regulation has continued over time. After the 33 Act and the 34 Act, Congress passed several statutes that built on the securities disclosure regime, including the Trust Indenture Act of 1939,[54] the Investment Company Act of 1940,[55] and the Investment Advisors Act of 1940.[56] Most recently, Congress passed the Sarbanes-Oxley Act of 2002 (SOX)[57] and the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (Dodd-Frank).[58] SOX was passed in response to financial scandals, including the collapse of Enron, and was meant to supplement the 33 Act and 34 Act regulations.[59] The bill was described as "sweeping" and President Bush called the legislation "the most far-reaching reforms of American business practices since the time of Franklin Delano Roosevelt."[60] Among other requirements,

54. Trust Indenture Act of 1939, Pub. L. No. 76-253, 53 Stat. 1149 (1939). This Act specifies that trust indentures must, among other things, provide for the appointment of an independent trustee to represent the public bondholders. *Id.* This act was intended to address deficiencies prevalent in trust indentures at the time, including a lack of disclosure and reporting requirements. S. REP. NO. 76-248, at 5–8 (1939).

55. Investment Company Act of 1940, Pub. L. No. 76-768, 54 Stat. 789 (1940). This Act requires that certain defined investment companies register with the SEC and also regulates their disclosures to investors. *Id.* This act's purpose is "to mitigate and . . . eliminate the conditions . . . which adversely affect the national public interest and the interest of investors." *Id.*

56. Investment Advisers Act of 1940, Pub. L. No. 76-768, 54 Stat. 847 (1940). This act imposes a number of requirements (including registration) on certain investment advisers. *Id.*

57. Sarbanes-Oxley Act of 2002, Pub. L. No. 107-204, 116 Stat. 745 (2002).

58. Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, 124 Stat. 1376 (2010).

59. In response to the question, "What inspired you to co-author the Sarbanes-Oxley legislation?" Senator Paul Sarbanes responded, "[T]hree years ago . . . we were facing a crisis in investor confidence. In October, 2001 the Enron Corporation announced its first financial restatement. . . . The purpose of the Sarbanes-Oxley Act goes beyond addressing recent scandals to building a durable framework on the foundation laid by the Securities Acts of 1933 and 1934." Nance Lucas, *An Interview with United States Senator Paul S. Sarbanes*, 11 J. LEADERSHIP & ORG. STUD. 3, 3–4 (2004).

60. Elisabeth Bumiller, *Corporate Conduct: The President; Bush Signs Bill Aimed at Fraud in Corporations*, N.Y. TIMES (July 31, 2002), https://www.nytimes.com/2002/07/31/business/corporate-conduct-the-president-bush-signs-bill-aimed-at-fraud-in-corporations.html [https://perma.cc/326A-6SZP]. This act mandated a number of reforms to enhance corporate responsibility and combat corporate and accounting fraud, and created the Public Company Accounting Oversight Board to oversee the activities of the auditing profession. *Id.*

SOX mandated enhanced financial disclosures.[61] Dodd-Frank, like the 33 Act and 34 Act, was passed in the wake of a profound recession,[62] and it focused on, among other things, "improving accountability and transparency in the financial system."[63] Dodd-Frank also addressed disclosure issues by mandating that the SEC promulgate certain disclosure rules.[64] Additionally, the SEC has promulgated disclosure rules on its own initiative.[65] As former SEC Commissioner Troy Paredes acknowledged in 2013, "Disclosure is the cornerstone of the federal securities laws. For nearly 80 years, the SEC's signature mandate has been to use disclosure to promote transparency."[66]

B. Materiality

The concept of materiality is a key component of the disclosure framework that governs public companies. It is included in the 33 Act,[67] the 34 Act,[68] and SEC rules including Rule 10b-5.[69] Materiality seeks to filter irrelevant information from disclosure[70] and is flexible enough to address new issues that emerge over time.[71] In

61. Title IV of the Act, entitled "Enhanced Financial Disclosures" describes enhanced reporting requirements for financial transactions. Sarbanes-Oxley Act of 2002, Pub. L. No. 107-204, §§ 401–409, 116 Stat. 745 (2002).

62. The financial panic of 2008 has been called "the worst recession since the Great Depression." INT'L BAR ASS'N TASK FORCE ON THE FIN. CRISIS, A SURVEY OF CURRENT REGULATORY TRENDS 27 (Oct. 2010).

63. Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, 124 Stat. 1376 (2010).

64. *See, e.g.*, Dodd-Frank Act § 953(b) (directing the SEC to require companies to disclose the annual total compensation of their median employee and chief executive officer, and the ratio of the two amounts); Dodd-Frank Act § 1502 (requiring public companies to make disclosures regarding their use of conflict minerals).

65. Rather than listing every SEC disclosure rule, I have cited two rules that are particularly relevant to sexual misconduct disclosure liability. *See, e.g.*, 17 C.F.R. § 229.103 (2019); 17 C.F.R. § 229.303 (2019).

66. Troy Paredes, Comm'r, SEC, Remarks at The SEC Speaks in 2013 (Feb. 22, 2013), *available at* https://www.sec.gov/news/speech/2013-spch022213taphtm [https://perma.cc/QG7P-2R88].

67. Securities Act of 1933, ch. 38, 48 Stat. 74 (codified as amended at 15 U.S.C. §§77a-77aa (2006)).

68. Securities Exchange Act of 1934, Pub. L. No. 73-291, 48 Stat. 881 (1934).

69. 17 C.F.R. § 240.10b-5 (2019).

70. *See* TSC Indus. v. Northway, Inc., 426 U.S. 438, 448 (1976) (noting that materiality serves an important role in filtering information because "[s]ome information is of such dubious significance that insistence on its disclosure may accomplish more harm than good").

71. Statement of the Commission Regarding Disclosure of Year 2000 Issues, Securities Act Release No. 33,7558, Exchange Act Release No. 34,40277, Invest-

1976, the Supreme Court articulated the standard for materiality that is still widely used today: the materiality of a misrepresentation or an omission depends on whether there is "a substantial likelihood that [it] would have been viewed by the reasonable investor as having significantly altered the 'total mix' of information made available" to a shareholder making a decision concerning their investments.[72]

Materiality is not a bright-line rule. Rather, it is a "fact-specific inquiry that requires consideration of the source, content, and context of the reports."[73] The Supreme Court in *Basic Inc. v. Levinson* stated that "[i]n the securities fraud context, any approach that designates a single fact or occurrence as always determinative of an inherently fact-specific finding such as materiality, must necessarily be overinclusive or underinclusive."[74] The SEC, too, has stated that "an assessment of materiality requires that one views the facts in the context of the surrounding circumstances."[75] In essence, each company must make a personalized, fact-intensive analysis to determine whether a piece of information is material and should be disclosed. For example, the Second Circuit recognized that a 5% deviation is an appropriate numerical threshold for materiality in financial statements, but it is only a "starting place" and courts must consider both "quantitative and qualitative factors" in assessing materiality.[76]

The Supreme Court, in *TSC Industries v. Northway, Inc.,* noted the importance of the concept of materiality as a filtering mechanism.[77] More than ten years later, in *Basic Inc. v. Levinson*, the Court reemphasized that a key purpose of materiality analysis is preventing management from burying shareholders in an "avalanche of trivial information."[78] The SEC has also noted that "as a practical matter, it is impossible to provide every item of information that might be of interest to some investor in making investment and

ment Company Release No. 34,40277, 67 SEC Docket 1437 (August 4, 1998) ("Federal securities laws are dynamic and respond to changing circumstances.").

72. *TSC Indus.*, 426 U.S. at 449.

73. Matrixx Initiatives, Inc. v. Siracusano, 563 U.S. 27, 43 (2011) (internal quotations omitted).

74. 485 U.S. 224, 236 (1988).

75. SEC Staff Accounting Bulletin No. 99, 17 Fed. Reg. 211 (Aug. 12, 1999) [hereinafter SAB 99] (internal quotations omitted).

76. Litwin v. Blackstone Grp., L.P., 634 F.3d 706, 717 (2d Cir. 2011) (referencing SAB 99, *supra* note 75). R

77. *TSC Indus.*, 426 U.S. at 448 ("Some information is of such dubious significance that insistence on its disclosure may accomplish more harm than good.").

78. *Basic*, 485 U.S. at 23.

voting decisions."[79] Indeed, the Supreme Court expressly rejected defining a "material fact" as any "fact which a reasonable shareholder *might* consider important."[80] Instead, materiality has been described as "a meaningful pleading obstacle."[81]

One common measure of materiality is the change in a company's stock price following the public release of a material fact, which reflects a consensus from investors about what that information means for the company's future.[82] However, some courts have been less receptive to the idea that a market reaction, or the lack thereof, is always determinative of materiality.[83] Indeed, district courts have observed that a change in stock price is not dispositive of materiality because, for example, a "material misstatement can impact a stock's value . . . by improperly maintaining the existing stock price."[84]

Additionally, some statements or omissions can be categorically deemed immaterial as a matter of law because they present or omit information that obviously would not matter to a reasonable investor. For instance, "Immaterial statements include vague, soft, puffing statements or obvious hyperbole upon which a reasonable investor would not rely."[85] Furthermore, "It is well-established that general statements about reputation, integrity, and compliance

79. Mary Jo White, Chair, SEC, Prepared Speech at the National Association of Corporate Directors Leadership Conference (Oct. 15, 2013), *available at* https://www.sec.gov/news/speech/spch101513mjw [https://perma.cc/V7QM-Q6PT].

80. *TSC Indus.*, 426 U.S. at 449.

81. *In re* ProShares Tr. Sec. Litig., 728 F.3d 96, 102 (2d Cir. 2013).

82. *See, e.g.*, *In re* Merck & Co. Sec. Litig., 432 F.3d 261, 269 (3d Cir. 2005) (stating that the materiality of omissions may by measured after the fact by looking at the movement of the company's stock price in the period immediately following full disclosure).

83. *Cf.* Halliburton Co. v. Erica P. John Fund, Inc., 573 U.S. 258, 268 (2014) (holding that defendants can rebut the *Basic Inc.* fraud-on-the-market presumption if defendants introduce "direct evidence" that the alleged misrepresentation did not impact the market price even if plaintiffs have shown that all three prerequisites (publicity, materiality, and market efficiency) are satisfied; implicit in this idea is that there can be a material misrepresentation that does not impact the stock price).

84. McIntire v. China Media Express Holdings, Inc., 38 F. Supp. 3d 415, 434 (S.D.N.Y. 2014); *see also In re* Pfizer Inc. Sec. Litig., 936 F. Supp. 2d 252, 264 (S.D.N.Y. 2013) ("[A] misstatement may cause inflation simply by maintaining existing market expectations, even if it does not actually cause the inflation in the stock price to increase on the day the statement is made.").

85. *In re* Ford Motor Co. Sec. Litig., 381 F.3d 563, 570 (6th Cir. 2004) (quoting *In re* K-tel Int'l, Inc. Sec. Litig., 300 F.3d 881, 897 (8th Cir. 2002)).

with ethical norms are inactionable 'puffery,' meaning that they are 'too general to cause a reasonable investor to rely upon them.'"[86]

Although sexual misconduct allegations have not traditionally served as a basis for securities disclosure liability, they certainly could do so today. The SEC has recognized that what is objectively important to a reasonable investor changes over time. Indeed, the agency has stated, "[F]ederal securities laws are dynamic and respond to changing circumstances."[87] There have been numerous instances of new developments being considered material facts when they had not been so previously. For example, although the 34 Act and Rule 10b-5 were enacted well before computers and the internet, they now cover and require public companies to disclose certain cybersecurity risks and incidents.[88] The SEC has also provided guidance to companies with respect to changing issues that may be material to investors, including: (1) the introduction of the Euro in July 1998,[89] (2) potential Y2K issues in August 1998,[90] and (3) climate change issues in February 2010.[91]

C. Affirmative Duty to Disclose

Securities disclosure is only required when there is a duty to disclose.[92] A duty to affirmatively disclose material facts "may arise when there is insider trading, a statute requiring disclosure, or, an

86. Pontiac Policemen's & Firemen's Ret. Sys. v. UBS AG, 752 F.3d 173, 183 (2d Cir. 2014) (quoting ECA & Local 134 IBEW Joint Pension Tr. of Chi. v. JP Morgan Chase Co., 553 F.3d 187, 206 (2d Cir. 2009)).

87. Statement of the Commission regarding Disclosure of Year 2000 Issues and Consequences, *supra* note 71. R

88. SEC, Division of Corporation Finance, CF Disclosure Guidance: Topic No. 2, Cybersecurity (October 13, 2011) ("Although no existing disclosure requirement explicitly refers to cybersecurity risks and cyber incidents, a number of disclosure requirements may impose an obligation on registrants to disclose such risks and incidents.").

89. SEC Staff Legal Bulletin No. 6, Fed. Sec. L. Rep. (CCH) ¶ 60,006 (July 22, 1998) ("We expect the conversion may be material to many European issuers, financial institutions, and domestic corporations with significant European operations, markets, investments, and/or contractual counterparties. These issuers may wish to consider the advisability of disclosure, even if the impact is not material.").

90. Statement of the Commission regarding Disclosure of Year 2000 Issues and Consequences, *supra* note 71 ("[W]e believe a company must provide year 2000 disclosure if . . . (2) management determines that the consequences of its Year 2000 issues would have a material effect on the company's business, results of operations, or financial condition."). R

91. SEC, *supra* note 26. R

92. The Supreme Court has long held that "[s]ilence, absent a duty to disclose, is not misleading under Rule 10b-5." Basic, Inc. v. Levinson, 485 U.S. 224, 239 n.17 (1988).

inaccurate, incomplete or misleading prior disclosure."[93] Additionally, some SEC rules impose an affirmative duty to disclose certain material facts.[94]

Public companies have an affirmative duty to disclose certain information as required by the 34 Act and subsequent regulations imposed by the SEC.[95] Typically, a public company must file: (1) an annual report each year on SEC form 10-K; (2) a quarterly financial report every three months on SEC form 10-Q; and (3) a report of major business developments filed within fifteen days of their occurrence on SEC form 8-K.[96] SEC Regulation S-K, Items 103 and 303 are required parts of form 10-K and form 10-Q that can mandate disclosure.[97] Although their disclosures may overlap to some extent, they are not identical.[98] Item 103, entitled "Legal proceedings," naturally mandates disclosure of "any material legal proceedings."[99] Item 303, entitled "Management's discussion and analysis of financial condition and results of operations," requires public companies to disclose "any known trends or uncertainties that have had or that the company reasonably expects will have a material favorable or unfavorable impact on net sales or revenues or income from continuing operations."[100] Additionally, certain corporate actions, such as a corporate merger, can trigger duties to disclose information.[101]

93. *In re* Dig. Island Sec. Litig., 357 F.3d 322, 329 n.10 (3d Cir. 2004).

94. *See, e.g.*, 17 C.F.R. § 229.103 (2019) (mandating disclosure of "any material legal proceedings"); 17 C.F.R. § 229.303 (2019) (mandating disclosure of "any known trends or uncertainties that have had or that the company reasonably expects will have a material favorable or unfavorable impact on net sales or revenues or income from continuing operations").

95. Section 13(a) of the 34 Act provides that every issuer of a security on a national securities exchange must file annual reports with the SEC in accordance with the SEC's rules and regulations and must file "such information and documents as the Commission shall require" in order to keep the issuer's registration statement "reasonably current." 15 U.S.C. § 78m (2019).

96. *See* SEC, *supra* note 22. **R**

97. SEC, Form 10-K General Instructions 8–9, *available at* https://www.sec.gov/files/form10-k.pdf [https://perma.cc/N2Z5-63NY]; SEC, Form 10-Q General Instructions 5, *available at* https://www.sec.gov/files/form10-q.pdf [https://perma.cc/VN63-RS3V].

98. *Compare* 17 C.F.R. § 229.103 (2019) *with* 17 C.F.R. § 229.303 (2019).

99. 17 C.F.R. § 229.103 (2019).

100. 17 C.F.R. § 229.303 (2019).

101. *See, e.g.*, Article 11 of Regulation S-X,17 C.F.R. § 210.11-01 (2014) (generally requiring the provision of pro forma financial information where a significant acquisition or disposition "has occurred or is probable"); Item 14 of Schedule 14A, 17 CFR § 240.14a-101 (requiring Article 11 pro forma financial information

D. Section 10(b) & Rule 10b-5

Section 10(b) of the 34 Act prohibits the use of "any manipulative or deceptive device or contrivance" in connection with the purchase or sale of securities that violates the regulations promulgated by the SEC.[102] Congress intended for § 10(b) to serve as a "catch-all" provision, supplementing the other narrower sections' prohibitions.[103] The approach of "leaving many of the enforcement details to the rule-making power of the SEC" was "typical" of the 34 Act,[104] and § 10(b) is not self-enforcing.[105]

Therefore, the SEC promulgated Rule 10b-5 in 1942.[106] Rule 10b-5 has been described as "by far the most important civil liability provision of the securities laws."[107] It can be enforced by the SEC in injunctive and civil actions[108] and by the Justice Department in criminal actions for willful violations of the 34 Act.[109] Additionally, the Supreme Court has implied a private cause of action from the text and purpose of § 10(b).[110] Today, private enforcement of securities laws is characterized as a "supplement" to public enforce-

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and extensive other information about certain extraordinary transactions if shareholder action is to be taken with respect to such a transaction).

102. 15 U.S.C. § 78j(b) (2012).

103. *See* Ernst & Ernst v. Hochfelder, 425 U.S. 185, 202 (1976) ("Of course [§ 10(b)] is a catchall clause to prevent manipulative devices.") (quoting *Stock Exchange Regulation*: *Hearing on H.R. 7852 and H.R. 8720 Before the H. Comm. on Interstate & Foreign Commerce*, 73d Cong. 115 (1934) (statement of Thomas G. Corcoran)).

104. Larry Bumgardner, *A Brief History of the 1930s Securities Laws in the United States—And the Potential Lessons for Today*, 4 J. GLOBAL BUS. MGMT. 1, 5 (2008), *available at* http://www.jgbm.org/page/5%20Larry%20Bumgardner.pdf.

105. *See* Birnbaum v. Newport Steel Corp., 193 F.2d 461, 463 (2d Cir. 1952) ("Section 10(b) of the Securities Exchange Act does not by its terms make unlawful any conduct or activity but confers rulemaking power upon the SEC to condemn deceptive practices in the sale or purchase of securities.").

106. *Security Fraud Curb is Extended by SEC*, N.Y. TIMES, May 22, 1942, *available at* https://timesmachine.nytimes.com/timesmachine/1942/05/22/85554377.pdf [https://perma.cc/K4XE-HY7L] (announcing Rule 10b-5's adoption).

107. *E.g.* Paul Vizcarrondo, Jr., *Liabilities Under the Federal Securities Laws* 4 (2014), *available at* http://www.wlrk.com/docs/OutlineofSecuritiesLawLiabilities2014.pdf [https://perma.cc/RJ6T-T8YD].

108. 15 U.S.C. § 78u(d) (2015).

109. 15 U.S.C. § 78ff (2002).

110. *See*, *e.g.*, Tellabs, Inc. v. Makor Issues & Rights, Ltd., 551 U.S. 308, 318 (2007) ("Section 10(b), this Court has implied from the statute's text and purpose, affords a right of action to purchasers or sellers of securities injured by its violation."); Superintendent of Ins. v. Bankers Life & Cas. Co., 404 U.S. 6, 13 n.9 (1971) ("It is now established that a private right of action is implied under § 10(b).").

ment.[111] It also continues to be perceived as an excessive source of securities litigation,[112] and companies spend significant time and resources on securities compliance issues.[113]

A viable claim under § 10(b) and Rule 10b-5 must contain six essential elements: "(1) a material misrepresentation or omission by the defendant; (2) scienter; (3) a connection between the misrepresentation or omission and the purchase or sale of a security; (4) reliance upon the misrepresentation or omission; (5) economic loss; and (6) loss causation."[114] This Note largely focuses on the first element, a material misrepresentation or omission by the defendant, because the facts necessary to proving it are particularly impacted by #MeToo.[115]

Under Rule 10b-5, it is unlawful for any person "[t]o make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading . . . in connection with the purchase or sale of any security."[116] In other words, when a company makes a disclosure, even if it had no duty to make it, it assumes a duty to disclose all information necessary to make that statement not misleading. There is no *per se* duty to reveal even material evidence of wrongdoing, however, and Section

111. *Tellabs*, 551 U.S. at 313 ("This Court has long recognized that meritorious private actions to enforce federal antifraud securities laws are an essential supplement to criminal prosecutions and civil enforcement actions brought, respectively, by the Department of Justice and the Securities and Exchange Commission (SEC).").

112. *See, e.g.*, Blue Chip Stamps v. Manor Drug Stores, 421 U.S. 723, 739 (1975) ("[L]itigation under Rule 10b-5 presents a danger of vexatiousness different in degree from that which accompanies litigation in general").

113. *See, e.g.*, John Clayton, Chair, SEC, Prepared Speech at the Economic Club of New York (July 12, 2017), https://www.sec.gov/news/speech/remarks-economic-club-new-york [https://perma.cc/FDU2-D7E2] ("[W]e must remember that implementing regulatory change has costs. Companies spend significant resources building systems of compliance, hiring personnel to operate those systems, seeking legal advice concerning the design and effectiveness of those systems, and adapting the systems as regulations change.").

114. Matrixx Initiatives, Inc. v. Siracusano, 563 U.S. 27, 37–38 (2011).

115. To be sure, there are still high hurdles to recovery under Rule 10b-5. For example, a plaintiff must in their complaint "state with particularity facts giving rise to a strong inference that the defendant acted with the required state of mind." 15 U.S.C. § 78u-4(b)(2)(A) (2006). Nevertheless, to the extent that #MeToo results in more material misstatements or omissions, companies risk securities disclosure liability.

116. 17 C.F.R. § 240.10b-5 (2019).

10(b) and Rule 10b-5(b) "do not create an affirmative duty to disclose any and all material information."[117]

An actionable material misrepresentation or omission under Rule 10b-5 has two components. First, applying an objective standard, the misrepresentation or omission must have been "material" to investors.[118] Second, there must be a misleading misstatement or omission.[119] A misstatement concerning "hard information" is actionable if the statement was "a material fact and . . . it was objectively false or misleading."[120] An actionable alleged misrepresentation concerning "soft information," which "includes predictions and matters of opinion,"[121] must be "made with knowledge of its falsity."[122] Indeed, "puffing"—expressing a general opinion rather than a knowingly false statement of fact—is not misleading, so there is no duty to correct such statements.[123]

To summarize, securities regulation revolves around the concept of disclosure. The core principle of securities disclosure is materiality, which encompasses corporate sexual misconduct, especially in the #MeToo environment. Public corporations have certain affirmative duties to disclose that material information. In addition, Rule 10b-5 provides a secondary legal duty to disclose material information and to refrain from making material misstatements.

117. *Matrixx Initiatives*, 563 U.S. at 44.

118. For a complete analysis of this issue, *see supra* Section I.B.

119. *See* Private Securities Litigation Reform Act of 1995, 15 U.S.C. § 78u-4(b)(1)(B) (2012) ("[T]he complaint shall specify each statement alleged to have been misleading, the reason or reasons why the statement is misleading, and, if an allegation regarding the statement or omission is made on information and belief, the complaint shall state with particularity all facts on which that belief is formed.").

120. *In re* Omnicare, Inc. Sec. Litig., 769 F.3d 455, 470 (6th Cir. 2014).

121. Monroe Emps. Ret. Sys. v. Bridgestone Corp., 399 F.3d 651, 669–70 (6th Cir. 2005).

122. *In re Omnicare*, 769 F.3d at 470. To show "knowledge of falsity" it must be proven that the "true facts" existed before the purportedly misleading statement. *See In re* Splash Tech. Holdings, Inc. Sec. Litig., 160 F. Supp. 2d 1059, 1072 (N.D. Cal. 2001) (stating that a complaint in a securities disclosure case "must allege that the 'true facts' arose prior to the allegedly misleading statement").

123. Retail Wholesale & Dep't Store Union Local 338 Ret. Fund v. Hewlett-Packard, 845 F.3d 1268, 1275 (9th Cir. 2017). To be misleading, a statement must be "capable of objective verification." *Id.*

II.
RISK OF SEXUAL MISCONDUCT DISCLOSURE LIABILITY IN THE #METOO WORLD

In the wake of the #MeToo movement, public corporations face a real risk of sexual misconduct disclosure liability. For one thing, sexual misconduct in the #MeToo world is more likely to be reported and considered an important factor in investor decision making.[124] Additionally, the highly publicized and incendiary nature of the issue makes it more likely that companies will face both public and private enforcement efforts when they fail to disclose such misconduct.[125] These factors indicate that companies should pay careful attention to sexual misconduct disclosure issues, although thus far the evidence indicates that they do not.

A. #MeToo Movement and Public Corporations

The "Harvey Weinstein effect"[126] and the #MeToo campaign created a wave of allegations that brought about the swift firings of many men in positions of power across the world.[127] The movement has been described as a "tipping point" and "watershed moment" in America's perception of sexual misconduct.[128] Prominent men in media, sports, politics, and other industries have been among those accused during the #MeToo movement.[129] Also implicated have been high-level executives at public companies such as Leslie

124. *See infra* Section II.A.

125. *See infra* Section II.B.

126. *See, e.g.*, Jessica Guynn & Marco della Cava, *Harvey Weinstein Effect: Men Are Getting Outed and Some Are Getting Fired as Women Speak Up. And it's Spreading*, USA TODAY (Oct. 25, 2017, 3:23 PM), https://www.usatoday.com/story/money/2017/10/25/harvey-weinstein-effect-men-losing-their-jobs-and-reputations-over-sexual-misconduct-charges-bu/796007001/ [https://perma.cc/P5FB-D3K6] (describing the transformation from a culture of silence to public accusations of sexual harassment as the "Harvey Weinstein effect").

127. *See, e.g.*, Jesselyn Cook & Ned Simons, *The Weinstein Effect: How a Hollywood Scandal sparked a Global Movement against Sexual Misconduct*, HUFFPOST (Nov. 8, 2017, 7:49 AM), https://www.huffingtonpost.com/entry/weinstein-effect-global_us_5a01d0e0e4b066c2c03a563b [https://perma.cc/P5FB-D3K6] (describing the worldwide impact of the "Weinstein Effect").

128. Interview by Noel King with Mary Schmich, Elizabeth Blair & Alexandra Schwarz, *Why 'The Weinstein Effect' Seems Like A Tipping Point*, NPR: ALL THINGS CONSIDERED (Nov. 4, 2017, 5:43 PM), audio recording and transcript *available at* https://www.npr.org/2017/11/04/562137110/why-the-weinstein-effect-seems-like-a-tipping-point [https://perma.cc/UC9R-6S35] (discussing why the Harvey Weinstein scandal is a tipping point and why other moments in history were not).

129. *See* Corey, *supra* note 12. R

Moonves, former CEO of CBS Corp.;[130] Brian Krzanich, former CEO of Intel Corp.;[131] Steve Wynn, former CEO of Wynn Resorts;[132] Steve Jurvetson, current board member of SpaceX and Tesla;[133] John Lasseter, former executive at Disney;[134] and Raj Nair, former President of Ford North America.[135]

Sexual misconduct can harm a company in multiple ways, including "difficulties in attracting, retaining, and motivating talented workers to customer defections, ruined business deals, and lost revenue and profit."[136] Following the #MeToo movement, companies may face an increased risk of sexual misconduct disclosure liability because the overall number of sexual misconduct accusations and lawsuits could appreciably increase. In addition, sexual misconduct may now have a larger impact on a company's value, thereby making it more likely that the sexual misconduct is "material."

130. Ronan Farrow, *As Leslie Moonves Negotiates His Exit From CBS, Six Women Raise New Assault and Harassment Claims*, NEW YORKER (Sept. 9, 2018), https://www.newyorker.com/news/news-desk/as-leslie-moonves-negotiates-his-exit-from-cbs-women-raise-new-assault-and-harassment-claims [https://perma.cc/CJN6-TGRV]; Farrow, *supra* note 13. R

131. *See* Jay Greene & Vanessa Fuhrmans, *Intel CEO Krzanich Resigns Over Relationship with Employee*, WALL ST. J. (Jun. 21, 2018. 7:53 PM), https://www.wsj.com/articles/intel-ceo-brian-krzanich-resigns-after-violating-company-policy-1529586884 [https://perma.cc/AVX8-L4A9].

132. *See* Berzon et al., *supra* note 13 (reporting on the sexual misconduct accusations against Steve Wynn). R

133. Theodore Schleifer, *Storied Venture Firm DFJ is Investigating Founder Steve Jurvetson for Sexual Harassment*, RECODE (Oct. 24, 2017), https://www.recode.net/2017/10/24/16539644/dfj-steve-jurvetson-sexual-harassment-allegation-venture-capital-vc-draper-fisher [https://perma.cc/Q8KY-T3A8] (reporting that Steve Jurvetson is facing an internal investigation following public accusations of sexual misconduct at his venture capital firm).

134. *Compare* Brooks Barnes, *John Lasseter, a Pixar Founder, Takes Leave After 'Missteps'*, N.Y. TIMES (Nov. 21, 2017), https://www.nytimes.com/2017/11/21/business/media/john-lasseter-pixar-disney-leave.html [https://perma.cc/UJ3N-D2VH] ("One of the Walt Disney Company's most important executives, the Pixar co-founder John Lasseter, said Tuesday that he would take 'a six-month sabbatical' after unspecified 'missteps' that made some staffers feel 'disrespected or uncomfortable.'"), *with Arms and the Man*, WALL ST. J. (May 26, 2011, 12:01 AM), https://www.wsj.com/articles/SB10001424052748704816604576333623057426528 [https://perma.cc/9DDW-7YWN] (displaying photos of five of the reportedly forty-eight hugs Lassiter gave to employees during a *Wall Street Journal* interview in 2011).

135. *See* Austen Hufford & John D. Stoll, *Ford North America President Leaves Following Misconduct Allegations*, WALL ST. J. (Feb. 21, 2018, 6:16PM), https://www.wsj.com/articles/ford-north-america-president-leaves-following-misconduct-allegations-1519249044 [https://perma.cc/XF8M-VD5H].

136. Crystal Kim, Leslie P. Norton & Lauren R. Rublin, *Tipping Point*, BARRON'S, Nov. 6, 2017, at 21–22.

1. Increased Sexual Misconduct Allegations

Harassment pervades the workplace. In a December 2017 survey conducted by American Management Association, 51% of female executives, managers, and professionals said they have been sexually harassed on the job, and a similar proportion said they have witnessed it.[137] Another recent poll, from Microsoft Service Network (MSN), found that almost one in three people (31%) in the United States admit to having been sexually harassed at work.[138] In the past, workplace harassment has been underreported: the MSN poll also found that 73% of women who said they had been sexually harassed at work also said they never reported it.[139]

The #MeToo movement could influence people to be more likely to challenge and report those incidences of sexual misconduct. In a national poll conducted in November 2017 by NBC News and SurveyMonkey, 46% of women responded that #MeToo stories made them more likely to speak up about sexual misconduct issues.[140] In a 2018 survey by Fawcett Society and Hogan Lovells, more than one in three British people (35%) said they were more likely to challenge inappropriate conduct since #MeToo.[141]

Early evidence signals that women are in fact reporting sexual misconduct more frequently since #MeToo. Sexual harassment charges filed with the U.S. Equal Employment Opportunity Com-

137. *See* Joann S. Lublin, *When #MeToo Becomes Catch-22*, WALL ST. J. (Jan. 24, 2018 8:00 AM), https://www.wsj.com/articles/when-metoo-becomes-catch-22-1516798800 [https://perma.cc/C2BQ-5KVH] (citing unpublished AMA survey of 3,247 women and men). For a broader analysis of sexual harassment and assault both inside and outside of the workplace since the beginning of the #MeToo movement, see STOP STREET HARASSMENT, THE FACTS BEHIND THE #METOO MOVEMENT: A NATIONAL STUDY ON SEXUAL HARASSMENT AND ASSAULT (Feb. 2018), http://www.stopstreetharassment.org/wp-content/uploads/2018/01/2018-National-Sexual-Harassment-and-Assault-Report.pdf [https://perma.cc/GF68-4BE8].

138. *See* Rachel Gillett, *Sexual Harassment isn't a Hollywood, Tech, or Media Issue—It Affects Everyone*, BUS. INSIDER (Nov. 30, 2017, 10:49 AM), http://www.businessinsider.com/sexual-harassment-affects-nearly-everyone-2017-11 [https://perma.cc/X4SY-ZW8V] (reporting on MSN's polling results). *See generally* David M. Rothschild, *Polling MSN in 2017*, PREDICTWISE (June 5, 2017), https://predictwise.com/blog/2017/06/polling-msn-in-2017/ [https://perma.cc/Z36N-R868] (touting the accuracy of MSN polling).

139. Gillett, *supra* note 138. R

140. *Sexual Harassment Poll Results*, NBC NEWS — SURVEYMONKEY (Nov. 30, 2017), http://msnbcmedia.msn.com/i/TODAY/z_Creative/NBC%20News%20SurveyMonkey%20Sexual%20Harassment%20Poll%20Toplines%20and%20Methodology.pdf [http://perma.cc/2CW6-TDU9].

141. *#MeToo One Year On—What's Changed?*, FAWCETT SOC'Y, 8 (Oct. 2018), https://www.fawcettsociety.org.uk/Handlers/Download.ashx?IDMF=8709c721-6d67-4d1f-8e30-11347c56a7c5 [https://perma.cc/R5BB-4M2W].

mission (EEOC) in 2018 have increased "by more than 12 percent from fiscal year 2017,"[142] and Victoria Lipnic, the acting chair of the EEOC, believes this is a result of the #MeToo movement.[143] Sexual misconduct-related calls to both corporate hotlines[144] and community organizations have likewise been "surging."[145]

2. The Corporate Costs of Sexual Misconduct Allegations

Sexual misconduct can lead to a variety of direct and indirect costs for companies, including decreased productivity, reputational costs, and legal costs. And, in addition to its potential impact on the incidence of reporting sexual misconduct, the #MeToo movement appears to be increasing those costs for corporations. Despite this, companies do not pay sufficient attention to these issues.

Workplace sexual misconduct results in decreased productivity from both its victims and observers. Victims of sexual misconduct often become less productive at work and more likely to miss

142. Press Release, U.S. Equal Emp't Opportunity Comm'n, EEOC Releases Preliminary FY 2018 Sexual Harassment Data (Oct. 4, 2018), https://www1.eeoc.gov/eeoc/newsroom/release/10-4-18.cfm [https://perma.cc/U5K4-98EV].

143. Jena McGregor, *The #MeToo Effect: Sexual Harassment Charges with the EEOC Rose for the First Time in Years*, WASH. POST (Oct. 5, 2018), https://www.washingtonpost.com/business/2018/10/05/metoo-effect-sex-harassment-charges-with-eeoc-rose-first-time-years/?utm_term=.b5b8ef92c196 [https://perma.cc/PRJ2-MWDC].

144. "Convercent Inc., an ethics- and compliance-software firm that operates reporting hotlines and portals for more than 600 companies world-wide, says the number of harassment reports it took in over the past year jumped 72% from the 12 months before." Vanessa Fuhrmans, *What #MeToo Has to Do with the Workplace Gender Gap*, WALL ST. J. (Oct. 23, 2018, 4:16 AM), https://www.wsj.com/articles/what-metoo-has-to-do-with-the-workplace-gender-gap-1540267680?mod=djem10point [https://perma.cc/VQV4-X9WW].

145. Michael Alison Chandler, *Calls to Rape Crisis Centers Are Surging Amid the Outpouring of Sexual Assault Allegations*, WASH. POST (Nov. 22, 2017), https://www.washingtonpost.com/local/social-issues/calls-to-rape-crisis-centers-are-surging-amid-the-outpouring-of-sexual-assault-allegations/2017/11/22/3d0bec6a-ce12-11e7-9d3a-bcbe2af58c3a_story.html?utm_term=.ac64b82be850 [https://perma.cc/SH92-CFKX]; *see also American Business and #MeToo*, ECONOMIST (Sept. 27, 2018), https://www.economist.com/business/2018/09/27/american-business-and-metoo [https://perma.cc/8RFE-FRDD] (reporting that a worker with the National Domestic Workers Alliance in New York has seen a big increase in women phoning for sexual harassment-related legal advice in the past year); Zach Irby, *Local Hotline Sees Uptick in Sexual Harassment Complaints*, SEATTLE TIMES (Jan. 6, 2018, 6:00 AM), https://www.seattletimes.com/nation-world/local-hotline-sees-uptick-in-sexual-harassment-complaints/ [https://perma.cc/HH68-8QA7] (reporting on comments by a sexual assault advocate at the Bristol Crisis Center in Bristol, Virginia that there are an uptick in sexual harassment calls to the crisis center hotline).

work.[146] Furthermore, several studies have found "ambient effects" on observers, with harassment resulting in lower morale and lower output.[147] Likewise, victims and observers of sexual misconduct are more likely to quit their jobs,[148] thereby increasing hiring costs and workplace disruption. While decreased productivity due to sexual misconduct existed prior to #MeToo, the movement has begun to reveal the full extent of these costs.

Additionally, sexual misconduct allegations can harm a corporation's reputation and impact its relationships with customers, job applicants, and business partners. Much publicity has accompanied #MeToo allegations,[149] thus increasing the reputational risk stemming from sexual misconduct. Moreover, the public now tends to believe allegations of sexual misconduct.[150] Therefore, sexual misconduct allegations negatively impact a corporation's reputation with consumers and job-applicants, because "perceived sexual harassment in the workplace has a negative effect on attitudes toward the brand, brand image, and intentions to work for prospective employees."[151] Furthermore, sexual misconduct allegations may result

146. *See* Chelsea Willness, Piers Steel, & Kibeom Lee, *A Meta-Analysis of the Antecedents and Consequences of Workplace Sexual Harassment*, 60 PERSONNEL PSYCHOL. 127, 137 (2007) (collecting studies).

147. *See id.* at 149 (reporting results of meta-analysis).

148. A survey of female law firm associates found that "[e]xperienced or observed [workplace] sexual harassment . . . increases the likelihood that the respondent reported an intention to quit her current workplace within two years by over 25%." David N. Laband & Bernard F. Lentz, *The Effects of Sexual Harassment on Job Satisfaction, Earnings, and Turnover Among Female Lawyers*, 51 INDUS. & LAB. RELS. REV. 594, 604 (1998).

149. *See* Appendix A.

150. A December 2017 poll of American voters by PerryUndem revealed that 85% of respondents said they were more likely to believe women making allegations of harassment or assault than the men who deny them. PERRYUNDEM RES. COMM., WHAT A DIFFERENCE A YEAR MAKES: POLLING UPDATE ON SEXISM, HARASSMENT, CULTURE AND EQUALITY 13 (2017), https://www.scribd.com/document/366406592/PerryUndem-Report-on-Sexism-Harassment-Culture-And-Equality-compressed [perma.cc/J628-YXC5]. Additionally, sexual misconduct allegations are easier than ever to prove due to advances in technology. *See* Jena McGregor, *Fear and Panic in the HR Department as Sexual Harassment Allegations Multiply*, WASH. POST, (Nov. 30, 2017), https://www.washingtonpost.com/news/on-leadership/wp/2017/11/30/fear-and-panic-in-the-h-r-department-as-sexual-harassment-allegations-multiply/?noredirect=on&utm_term=.8974f793f59a [https://perma.cc/5Q6R-L6BU] (quoting a lawyer who said that clear evidence is now "often available in the form of emails, texts or other electronic posts" and "the days of he-said, she-said have essentially been eliminated by technology . . . somebody's got a screenshot somewhere").

151. Sierra et al., *supra* note 20, at 187; *see also* Ted Marzilli, *Pandora Jewelers Takes Xmas Perception Lead Over Softening Signet Brands*, YOUGOVBRANDINDEX (Dec. R

in severed current or potential business partnerships: for example, Amazon cut off all ties with the Weinstein Company after the allegations against Harvey Weinstein emerged.[152]

Workplace sexual misconduct inflicts further costs on companies by negatively impacting investor relations. Anecdotal evidence indicates that investors are now avoiding companies with a history of sexual misconduct.[153] Additionally, some investors are now seeking to introduce and utilize "clawback" provisions to recoup losses related to workplace sexual misconduct.[154]

Companies also face high legal costs when investigating, litigating, and paying sexual misconduct claims. In 2017, the EEOC resolved about 7,500 sexual harassment complaints, with employers paying $46.3 million in employee benefits through the Commission's pre-litigation administrative enforcement process.[155] And Twenty-First Century Fox paid $20 million alone to settle anchor

13, 2017, 8:05 PM), http://www.brandindex.com/article/pandora-jewelers-takes-xmas-perception-lead-over-softening-signet-brands [https://perma.cc/2M99-SSSS] (drawing a connection between allegations of sexual harassment against Signet Jewelry and a downturn in two of their key brand metrics with women).

152. Meg James, *Amazon Studios Cuts Ties with Weinstein Co. Following Harvey Weinstein Sex Scandal*, L.A. TIMES (Oct. 13, 2017, 7:50 PM), http://www.latimes.com/business/hollywood/la-fi-ct-amazon-cuts-ties-weinstein-co-20171013-story.html [https://perma.cc/LDN9-JUQ7] (including canceling a show with a $160 million budget).

153. Eve Ellis, a portfolio manager with Morgan Stanley's Matterhorn Group, recently said that she generally avoids investing in companies facing class action or individual lawsuits dealing with gender because "[t]hey might cost a company money, and lead to reputational risk." Kim et al., *supra* note 136, at 23. Calvert Investments, a "socially responsible" investment management company, has stated that it deliberately steers clear of companies with gender-related controversy. *Id.* This includes Dollar General, which settled a variety of discrimination and harassment suits over the last decade, and Uber Technologies, which recently fired their CEO after he failed to tame a corporate culture rife with sexual-harassment issues. *Id.* R

154. For example, large investors and buyers in mergers-and-acquisitions are increasingly introducing clawback provisions to agreements that automatically fine companies whose employees engage in sexual misconduct. *See* Laurence Fletcher, *Big Investors Seek a #MeToo Clawback*, WALL ST. J. (Sept. 23, 2018, 10:07 PM), https://www.wsj.com/articles/big-investors-seek-a-metoo-clawback-1537754820 [https://perma.cc/SYL5-HJ25] ("[P]roponents of clawback clauses say inappropriate behavior by top executives is evidence of weak corporate governance and a flawed culture . . . [that] can manifest in legal costs, lost time, management distraction and negative publicity.").

155. U.S. Equal Emp't Opportunity Comm'n, *Charges Alleging Sexual Harassment (Charges filled with EEOC) FY 2010 - FY 2017*, https://www.eeoc.gov/eeoc/statistics/enforcement/sexual_harassment_new.cfm [https://perma.cc/K8HE-QC4A].

Gretchen Carlson's lawsuit against former CEO Roger Ailes.[156] Even in cases where employers successfully defend workplace sexual misconduct lawsuits, employers frequently pay six figures or more in outside attorney's fees and investigative costs.[157] As the number of sexual misconduct allegations rise, companies can expect total legal costs to rise as well. For example, the EEOC filed over fifty percent more harassment lawsuits in fiscal year 2018 as compared to fiscal year 2017.[158]

Additionally, efforts by legal defense funds and the finance industry since the beginning of the #MeToo movement are providing financial support to accusers to ensure that victims are able to fund their legal claims. For example, The Time's Up Legal Defense Fund has raised more than $21 million to provide legal help to victims of sexual misconduct and it has received more than 3,500 applications since January 2018.[159] "Settlement-advance" companies, which have traditionally targeted personal injury and medical malpractice plaintiffs, are "racing to capitalize on sexual harassment lawsuits."[160] Other lawsuit funding companies are pursuing sexual misconduct "litigation financing" opportunities.[161] In sum, companies now face increased legal costs because victims are more likely and better able to fight back with sexual misconduct lawsuits.

156. *See* Nick Fountain & David Folkenflik, *Federal Inquiry Said to Focus on Whether Fox News Broke Law in Harassment Payouts*, NPR (Feb. 16, 2017, 2:54 AM), https://www.npr.org/sections/thetwo-way/2017/02/16/515509093/ lawyer-alleges-fox-news-is-under-federal-investigation-related-to-sexual-harassm [https://perma.cc/3CXN-4DG5] (reporting that Twenty-First Century Fox has paid millions of dollars to settle sexual misconduct allegations from multiple women against Ailes).

157. *See* Beth Braverman, *The High Cost of Sexual Harassment*, FISCAL TIMES (Aug. 22, 2013), http://www.thefiscaltimes.com/Articles/2013/08/22/The-High-Cost-of-Sexual-Harassment [https://perma.cc/GYM4-WU4Z] (stating that $100,000 legal bills are common and seven-figure settlements are possible).

158. Press Release, U.S. Equal Emp't Opportunity Comm'n, EEOC Releases Preliminary FY 2018 Sexual Harassment Data (Oct. 4, 2018), https://www1.eeoc.gov/eeoc/newsroom/release/10-4-18.cfm [https://perma.cc/H3BV-MH9A].

159. *American Business and #MeToo*, *supra* note 145. R

160. Matthew Goldstein & Jessica Silver-Greenberg, *How the Finance Industry is Trying to Cash in on #MeToo*, N.Y. TIMES (Jan. 28, 2018), https://www.nytimes.com/2018/01/28/business/metoo-finance-lawsuits-harassment.html [https://perma.cc/VEK4-LAQS]. Settlement advance companies offer money to plaintiffs in anticipation of future legal settlements, sometimes at exorbitant interest rates. *Id.*

161. *Id.* ("In addition to providing cash upfront to sexual harassment plaintiffs, some firms are pursuing the more traditional form of litigation finance, providing money to law firms in exchange for a cut of potential settlements.").

Companies have not historically viewed sexual misconduct as an important corporate risk factor,[162] and despite all indications that they should, companies still do not pay sufficient attention to these issues. According to a May 2018 survey by the American Psychological Association, less than one third of Americans said their employer had done something to deal with sexual harassment following #MeToo, and the most common approach was only to remind employees of existing harassment training or resources.[163] Furthermore, a 2017 survey of 600 mostly female board members of public and private companies conducted by theBoardlist and Qualtrics found that 77% of boards had not discussed accusations of sexually inappropriate behavior or sexism in the workplace, 88% had not implemented a plan of action stemming from recent revelations in the media, and 83% had not reevaluated company risks related to sexual harassment or sexist behavior.[164] One possible explanation for these lackluster statistics is the dearth of female representation in boardrooms: women still only occupy 16% of all available board seats of the 3,000 largest US companies,[165] and the number of female Fortune 500 CEOs has fallen since the #MeToo movement started.[166] Indeed, 624 of the 3,000 largest U.S. companies still have no female directors at all.[167] Regardless of the "why," the fact remains that companies are not properly acknowledging the risk of sexual misconduct disclosure liability.

Recent reports of sexual misconduct by Wynn Resorts' CEO, Steve Wynn, illustrate the impact of sexual misconduct allegations on a corporation in the #MeToo world. On January 26, 2018, the *Wall Street Journal* reported on dozens of people's accounts of decades of sexual misconduct by Wynn.[168] Many investors quickly sold their Wynn Resorts stock, including the $2.6 billion Thornburg

162. Based on a 2017 search of 67,500 post-2009 corporate filings for the terms "gender," "harassment," and "discrimination," gender was mentioned in the risk-factor section of only 166 (0.25%) 10-K filings. Kim et al., *supra* note 136, at 24. R

163. *Workplace Sexual Harassment: Are Employers Actually Responding?*, AM. PSYCHOL. ASS'N: CTR. FOR ORGANIZATIONAL EXCELLENCE 1 (May 2018) http://www.apaexcellence.org/assets/general/2018-sexual-harassment-survey-results.pdf?_ga=2.89809243.1725914266.1539291523-1270113696.1539291523 [https://perma.cc/9Q5S-LU9B].

164. Kim et al., *supra* note 136, at 24. R

165. Oliver Staley, *There Are 624 Public Companies with No Women on Their Boards. Here's the List*, QUARTZ AT WORK (Dec. 15, 2017), https://work.qz.com/1130589/there-are-624-public-companies-with-no-women-on-their-boards-heres-the-list/ [https://perma.cc/BU7W-XNC6].

166. *See American Business and #MeToo*, *supra* note 145. R

167. *See* Staley, *supra* note 165. R

168. Berzon et al., *supra* note 13. R

Global Opportunities Fund, which cited the harassment allegations against Wynn as a "material contributing factor" in the fund's decision to sell its entire stake of 891,000 shares of Wynn Resorts stock (0.864% equity stake).[169] The allegations also seriously tarnished Wynn Resorts' reputation with gaming regulators, who vowed to investigate the company even after Steve Wynn's resignation.[170] Wynn Resorts' stock price immediately tumbled from $200.60 on January 25 to $163.22 on January 26,[171] interrupting what had previously been a sharp rise in the company's stock.[172]

The Wynn example also reveals how companies that do not take sexual misconduct disclosure seriously risk liability. In its most recent 10-Q filing, the company indicated, "If we lose the services of Mr. Wynn, or if he is unable to devote sufficient attention to our operations for any other reason, our business may be significantly impaired."[173] Despite the company's acknowledgment of this key-

169. Chris Kirkham, Joann S. Lublin & Sarah Krouse, *Wynn Resorts Board Faces Scrutiny Following Allegations Against Steve Wynn*, WALL ST. J. (Jan. 30, 2018, 7:00 PM), https://www.wsj.com/articles/wynn-resorts-board-faces-scrutiny-following-allegations-against-steve-wynn-1517338504 [https://perma.cc/628D-PNVR]. *Compare* Wynn Las Vegas, LLC, Annual Report (Form 10-K) at 1 (Feb. 24, 2017) (noting that as of February 15, 2018, 103,017,861 shares of Wynn Resorts common stock were outstanding), *with* Chris Isidore, *Steve Wynn Allegations Punish His Company's Stock*, CNNMONEY (Feb. 6, 2018, 12:01 AM), http://money.cnn.com/2018/02/06/news/companies/steve-wynn-investors/index.html [https://perma.cc/E6QX-FPQG] (reporting that Thornburg's stake was 891,000 shares).

170. *See* Kirkham et al., *supra* note 19; Mark Arsenault, *Despite Wynn's Ouster, State Gaming Panel's Probe Will Go On*, BOS. GLOBE (Feb. 7, 2018), https://www.bostonglobe.com/metro/2018/02/07/gaming-commission-investigation-continue-despite-wynn-ouster/15OXc4MSFTXtShpvgLlGtI/story.html [https://perma.cc/66UY-D35B]. R

171. Maggie Astor & Julie Creswell, *Steve Wynn Resigns from Company Amid Sexual Misconduct Allegations*, N.Y. TIMES (Feb. 6, 2018), https://www.nytimes.com/2018/02/06/business/steve-wynn-resigns.html?emc=edit_th_180207&nl=todaysheadlines&nlid=69949744 [https://perma.cc/8B9F-LAPU].

172. Ben Eisen, *Misconduct Report Shaves $2 Billion From Wynn Market Value*, WALL ST. J. (Jan. 26, 2018, 1:49 PM), https://blogs.wsj.com/moneybeat/2018/01/26/misconduct-report-shaves-nearly-2-billion-from-wynn-market-value/ [https://perma.cc/T2F4-PWXE] (reporting that Wynn Resorts had made strong gains in stock-price over the previous twelve months because the company had posted growth in revenues and its most recent earnings report had topped analyst expectations).

173. *Compare* Wynn Las Vegas, Ltd., Current Report (Form 10-Q) at 52 (Nov. 8, 2017) ("A description of our risk factors can be found in . . . our Annual Report on Form 10-K for the year ended December 31, 2016. There were no material changes to those risk factors during the nine months ended September 30, 2017."), *with* Wynn Las Vegas, Ltd., Current Report (Form 10-K) at 11 (Feb. 24, 2017) ("Our ability to maintain our competitive position is dependent to a large degree on the efforts, skills and reputation of Stephen A. Wynn.").

person dependency, many of the sexual misconduct allegations against Wynn had been known to executives at Wynn Resorts for years, yet had not been explicitly disclosed to investors.[174] Wynn Resorts quickly filed 8-K Forms on January 29th and February 7th disclosing an internal investigation of the allegations and the firing of Wynn, respectively.[175] Given that key company executives had long known of the allegations and appreciated the obvious impact of their disclosure, Wynn Resorts' shareholders should question why the allegations were not disclosed earlier.

B. Impact on the Enforcement of Sexual Misconduct Disclosure Liability

With the rise of the #MeToo movement, public corporations must also deal with stepped-up enforcement of sexual misconduct disclosure liability. The new reality of more instances of material sexual misconduct[176] coupled with the salacious, headline-grabbing nature of sexual misconduct allegations will motivate heightened enforcement.[177] Moreover, there has been an increase in securities disclosure enforcement overall, which may also lead to increased enforcement of sexual misconduct disclosure liability.[178]

1. Public Enforcement

While there are valid public policy reasons favoring the disclosure of alleged or proven sexual misconduct to investors,[179] the

174. Steve Wynn's ex-wife, a board member of Wynn Resorts, knew of a sexual misconduct settlement as early as 2009 and informed the General Counsel of Wynn Resorts of it in 2015. *See* Kirkham et al., *supra* note 169. Wynn Resorts also reportedly failed to disclose to gaming regulators a known $7.5 million sexual misconduct settlement against Wynn in 2013 "on advice of counsel." Steve LeBlanc, *Massachusetts Casino Panel: Wynn Settlement Was Kept From Us*, U.S. NEWS & WORLD REP. (Jan. 31, 2018, 5:21 PM), https://www.usnews.com/news/business/articles/2018-01-31/massachusetts-gambling-regulators-to-review-wynn-allegations [https://perma.cc/P3XD-3NTT]. R

175. Wynn Resorts, Ltd., Current Report (Form 8-K) (Jan. 29, 2018) ("On January 26, 2018, the Board of Directors of Wynn Resorts, Limited announced that it formed a Special Committee of the Board comprised solely of independent directors to investigate allegations contained in a January 26, 2018 *Wall Street Journal* article."); Wynn Resorts, Ltd., Current Report, (Form 8-K) (Feb. 7, 2018) ("On February 6, 2018, Wynn Results, Limited announced that Stephen A. Wynn has resigned as Chairman of the Board and Chief Executive Officer of the Company, effective immediately.").

176. *See supra* Section II.A.

177. *See infra* II.B.1.

178. *See infra* II.B.2.

179. *See, e.g.*, H.R. REP. NO. 73-1383, at 11 (1934) ("There cannot be honest markets without honest publicity. Manipulation and dishonest practices of the market place thrive upon mystery and secrecy.").

prominent media attention given to sexual misconduct adds an extra incentive for public enforcers to address these issues.[180] Although the SEC is the primary securities regulator whose jurisdiction is implicated, there are several other enforcement authorities, such as federal prosecutors and state attorneys general, who could conceivably have sufficient authority and motivation to respond to public revelations of corporate sexual misconduct. Companies confronting sexual misconduct allegations must therefore predict how these public enforcers might apply disclosure liability rules to a novel course of conduct.[181] While it may be difficult at times to comply with uncertain legal standards, such as Rule 10b-5,[182] companies must necessarily expect that law enforcement and regulators will use all of the tools at their disposal to respond to a public and politically-charged issue like sexual misconduct.

The SEC is unlikely to lead the charge in enforcing sexual misconduct-related securities enforcement. The agency is large and bureaucratic, and bureaucracies are by their very nature risk-averse.[183] Further, given the SEC's extensive rulemaking authority, it may be viewed as unnecessary and even undesirable for the SEC to attempt a novel form of securities enforcement such as a Rule 10b-5 action predicated on non-disclosure of sexual misconduct.[184] Finally, as an

180. Pessimists might argue that public allegations of sexual misconduct allegations might attract the attention of regulators seeking to make headlines through enforcement actions. *Cf.* JAMES M. BUCHANON & GORDON TULLOCK, THE CALCULUS OF CONSENT: LOGICAL FOUNDATIONS OF CONSTITUTIONAL DEMOCRACY 19 (1962) (suggesting that public officials do not always act in the public interest, but rather act in the pursuit of private benefits).

181. *See, e.g.*, William L. Cary, *Corporate Standards and Legal Rules*, 50 CAL. L. REV. 408, 408 (1962) (urging attorneys to advise corporate clients to anticipate how standards will be applied).

182. *See* Park, *supra* note 31, at 142 (noting that strict enforcement can lead to a "chilling effect where parties will be overly cautious for fear that they will be punished for acts that a regulator determines ex post is misconduct"); *see also* Calfee & Craswell, *supra* note 31 (noting that uncertain legal standards incentivize over- or under-compliance). R R

183. *See* Park, *supra* note 31, at 146 (noting that the SEC is a large bureaucracy and "bureaucracies tend to be governed by rigid hierarchies that are risk adverse"). R

184. *See id.* at 152 ("[R]ather than bringing an innovative case that would create controversy, the SEC can simply pass a rule prohibiting such conduct in the future."). While politically independent, moreover, the SEC is often judged by the quantity of enforcement cases it brings rather than the prominence of those cases. *See id.* at 147 (noting that it is often said that the SEC is risk adverse because it is judged by the number of enforcement cases it brings).

industry regulator, the SEC must balance the needs of market stability with any possible interest in aggressive enforcement.[185]

Instead, companies should be more concerned that federal prosecutors will pursue sexual misconduct disclosure liability. Federal prosecutors have often sought out securities enforcement roles "through headline-grabbing convictions."[186] Some federal prosecutors' offices also have elite securities lawyers, who may be better equipped to bring "edge" cases.[187] Indeed, the SEC often refers difficult cases to federal prosecutors.[188] Federal prosecutors also operate in a less bureaucratic environment than the SEC. Moreover, federal prosecutors have already indicated an interest in pursuing sexual misconduct disclosure liability enforcement with an investigation into the disclosure practices of Twenty-First Century Fox.[189]

185. Donald C. Langevoort, *Managing the "Expectations Gap" in Investor Protection: The SEC and the Post-Enron Reform Agenda*, 48 VILL. L. REV. 1139, 1143–44 (2003) (noting that the role of being the "investor's champion" can conflict with enforcement that portrays the risks of investing as so severe that investors become discouraged and drop out the market).

186. Park, *supra* note 31, at 117. Some federal prosecutors have been accused of having political ambitions and the opportunity to pursue charges against a company for failure to disclose sexual harassment could be viewed as a convenient way to advance a personal political agenda in the #MeToo environment. *See* Dan M. Kahan, *Is Chevron Relevant to Federal Criminal Law?*, 110 HARV. L. REV. 469, 486 (1996) ("U.S. Attorneys are extraordinarily ambitious and frequently enter electoral politics after leaving office."). *But see* Daniel C. Richman, *Federal Criminal Law, Congressional Delegation, and Enforcement Discretion*, 46 UCLA L. REV. 757, 777 (1999) (noting that U.S. Attorneys have a reputation for being objective). R

187. *See, e.g.*, A.C. Pritchard, *The SEC at 70: Time for Retirement?*, 80 NOTRE DAME L. REV. 1073, 1096–97 (2005) ("The Justice Department has many lawyers and investigators who are proficient at prosecuting securities fraud (e.g., the fraud unit of the U.S. Attorney's office in the Southern District of New York).").

188. Park, *supra* note 31, at 155 (noting that "the SEC often refers cases to federal prosecutors, recognizing their ability to seek greater sanctions and their skill at trying cases"). R

189. About a year prior to the "pivotal" Weinstein allegations, key Twenty-First Century Fox employees Roger Ailes, CEO of Fox News, and Bill O'Reilly, a popular television host at Fox News, were publicly accused of committing sexual misconduct. *See* Emily Steel & Michael S. Schmidt, *Bill O'Reilly Settled New Harassment Claim, Then Fox Renewed His Contract*, N.Y. TIMES (Oct. 21, 2017), https://www.nytimes.com/2017/10/21/business/media/bill-oreilly-sexual-harassment.html [https://perma.cc/NZL2-NL8Y]. Twenty-First Century Fox was also accused of hiding numerous sexual misconduct accusations and settlements from the public. *Id.* Almost immediately, it was reported that a federal inquiry by the U.S. Attorney's Office Southern District of New York was looking into, among other things, whether sexual misconduct settlement payments were masked as salary or compensation to skirt rules compelling public disclosure of the payments. *See, e.g.*, Jim Dwyer & William K. Rashbaum, *Federal Inquiry of Fox News Moves to a Grand Jury, but Without Preet Bharara*, N.Y. TIMES (Mar. 13, 2017), https://www.nytimes.com/2017/

In addition to potential federal criminal scrutiny, companies should also recognize the risks posed by offices of state attorneys general that enforce their own states' securities statutes. Because they are often elected, state attorneys general are generally viewed as more susceptible to political influence.[190] They may be more inclined, therefore, to "cater to the public by aggressively pursuing unpopular companies,"[191] such as those accused of covering up sexual misconduct. For example, following the accusations against Harvey Weinstein, the New York Attorney General's Office rapidly and publicly pursued sexual harassment and civil rights violations charges against the Weinstein Company.[192]

2. "Private" Enforcement

The plaintiffs' bar (private enforcement) has brought, and will continue to bring, sexual misconduct disclosure liability actions against public corporations.[193] This is due to a confluence of factors including an aggressive plaintiffs' bar, an increase in the impact of sexual misconduct allegations, a general rise in securities class actions, and the copycat nature of private enforcement. In fact, public

03/13/nyregion/federal-inquiry-of-fox-news-moves-to-a-grand-jury-but-without-preet-bharara.html [https://perma.cc/67JY-DPM7] (reporting that a grand jury was convened and looking into Fox News business practices, focusing in part on sexual harassment settlement payments); Emily Steel & John Koblin, *Fox News's Harassment Payments Are Under Investigation, Lawyer Says*, N.Y. TIMES (Feb. 15, 2017), https://www.nytimes.com/2017/02/15/business/media/fox-news-sexual-harassment-payments.html?_r=0 [https://perma.cc/NL8D-JJHG] (reporting that the U.S. Attorney's office was possibly looking into the ways Fox News handled payments related to sexual misconduct to determine whether the company violated securities laws). While experts at the time were unsure whether the settlements were material enough to mandate disclosure, the inquiry illustrates how sexual misconduct issues can draw the attention of federal prosecutors. *See* Fountain & Folkenflik, *supra* note 156 (stating that while Fox News probably should have disclosed the settlement payments, it is ambiguous whether they were significant enough to warrant disclosure). R

190. Park, *supra* note 31, at 158. R

191. *Id.* at 158–59. *But see id.* at 159 (noting that politics can influence both ways, and if the company in question is politically powerful then a state attorney general may decide not to target it).

192. *See, e.g.*, Fritz et al., *supra* note 16 (reporting that New York Attorney General filed a lawsuit only four months after Harvey Weinstein's firing at The Weinstein Company). The New York Attorney General's Office has also requested information from CBS regarding allegations of sexual harassment by CEO Leslie Moonves and others. Joe Flint, *CBS Says It Got Subpoenas From Prosecutors Over Moonves Allegations*, WALL ST. J. (Sept. 28, 2018 6:45 PM), https://www.wsj.com/articles/cbs-says-it-got-subpoenas-from-prosecutors-over-moonves-allegations-1538174744 [https://perma.cc/M74H-A6MD]. R

193. *See, e.g.*, CBS Complaint, *supra* note 18; Wynn Complaint, *supra* note 18. R

corporations may have more reason to fear private enforcement than public enforcement.

Private enforcers are aggressive in pursuing securities class actions.[194] They can be unrelenting in their pursuit of innovative theories of wrongdoing.[195] They are also highly profit-motivated and dogged when seeking new clients.[196] Private enforcers are particularly motivated when there is a large stock price drop following public disclosure of information, and securities litigation often follows stock price declines.[197] That is because a stock price drop is often, although not always, seen as evidence of materiality when there is a failure to disclose.[198] Additionally, a bigger stock drop can mean larger damages penalties,[199] which results in bigger attorneys' fees and therefore an increased incentive for profit-motivated private enforcers to bring securities actions.[200] In the #MeToo environ-

194. For instance, the median time to file a securities class action fell to a record low of 10 days in 2017. Stefan Boettrich and Svetlana Starykh, *Recent Trends in Securities Class Action Litigation: 2017 Full-Year Review*, NERA ECON. CONSULTING 17 (Jan. 29, 2018), http://www.nera.com/content/dam/nera/publications/2018/PUB_Year_End_Trends_Report_0118_final.pdf [https://perma.cc/23CL-LCCP].

195. *See, e.g.*, Matthew C. Stephenson, *Public Regulation of Private Enforcement: The Case for Expanding the Role of Administrative Agencies*, 91 VA. L. REV. 93, 112–13 (2005) (citing several examples of innovative private enforcement).

196. *See, e.g.*, Park, *supra* note 31, at 159–60 ("[C]lass action attorneys are notorious for racing to the courthouse in search of the next case."). R

197. *Compare* Irene Kim & Douglas J. Skinner, *Measuring Securities Litigation Risk* 7–8 (Univ. of Chi. Booth Sch. of Bus., Working Paper No. 10-23, 2012), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=1632638 [https://perma.cc/2SNM-QCLF] (stating that there is a body of research that believes that damages in Rule 10b-5 litigation depends on price decline, and that larger potential damages attract private litigation), *with* Seonghee Han, Murali Jagannathan, & Srinivasan Krishnamurthy, *When Does Insider Selling Increase Litigation Risk?* (Sep. 12, 2014) (unpublished paper) (available at SSRN: https://ssrn.com/abstract=2495595) ("We find that it is insider selling prior to large price drops, not insider selling in general, that increases the likelihood of [securities class action] litigation.").

198. *See, e.g.*, *In re* Merck & Co. Sec. Litig., 432 F.3d 261, 269 (3d Cir. 2005) (materiality of omissions may by measured after the fact by looking at the movement of the company's stock price in the period immediately following full disclosure).

199. *See* CORNERSTONE RESEARCH, ESTIMATING RECOVERABLE DAMAGES IN RULE 10B-5 SECURITIES CLASS ACTIONS 2 (2014) (explaining that one way to determine damages is by looking at "actual share price declines attributable to revelation of the relevant truth regarding a misrepresentation made prior to the purchase of that share").

200. A study from two class action data sets covering 1993–2002 reveals that the amount of client recovery is definitively the most important determinant in attorney fee award. Theodore Eisenberg & Geoffrey P. Miller, *Attorney Fees in Class Action Settlements: An Empirical Study*, 1 J. EMPIRICAL LEGAL STUD. 27, 27 (2004).

ment, a single tweet alleging sexual misconduct can create a double-digit stock drop.[201] On February 1, 2018, for example, shares in retailer Guess Inc. fell over 17 percent after a #MeToo tweet by model Kate Upton, who accused co-founder Paul Marciano of sexual misconduct.[202] Thus, the issue is ripe for private enforcement efforts.

Aside from the factors that would make sexual misconduct issues inherently attractive to the plaintiffs' bar, the number of securities class actions, both traditional and untraditional, is rapidly rising. In 1995, Congress enacted the Private Securities Litigation Reform Act (PSLRA) in part to combat plaintiffs' lawyers' abuse of 10b-5 suits.[203] Studies show that the PSLRA has achieved its goals in part,[204] but the number of securities class actions has dramatically risen in recent years.[205] The number of companies faced with these lawsuits has also risen, nearly doubling from 2014 to 2017.[206] Part of

201. *Cf. infra* Appendix B.

202. *See Guess Shares Slump After Model Kate Upton Tweets About Exec*, REUTERS, (Feb. 1, 2018, 2:35 PM), https://www.reuters.com/article/us-guess-stocks/guess-shares-slump-after-model-kate-upton-tweets-about-exec-idUSKBN1FL6BK [https://perma.cc/BDQ2-ZTCP] ("Guess Inc shares fell more than 17 percent on Thursday following a tweet by model and actress Kate Upton accusing the company's co-founder of using his power to harass women."); Kate Upton (@KateUpton), TWITTER (Jan. 31, 2018, 2:09 PM), https://twitter.com/kateupton/status/958824619120693248?lang=en [https://perma.cc/Q8EG-2Y2Q] ("It's disappointing that such an iconic women's brand @GUESS is still empowering Paul Marciano as their creative director #metoo").

203. H.R. REP. NO. 104-369, at 31 (1995), *as reprinted in* 1995 U.S.C.C.A.N. 730, 740 ("Congress has been prompted by significant evidence of abuse in private securities lawsuits to enact reforms to protect investors and maintain confidence in our capital markets.").

204. *See* Stephen Choi, Karen K. Nelson, & Adam C. Pritchard, *The Screening Effect of the Private Securities Litigation Reform Act* 26 (Univ. of Mich. Law Sch. John M. Olin Ctr. for Law & Econ., Working Paper No. 07-008, 2009), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=975301## [https://perma.cc/EM38-YC6M].

205. Plaintiffs filed more federal securities class actions in 2017 than in any year since the enactment of the PSLRA. *See* Boettrich & Starykh, *supra* note 194, at 2. Four hundred thirty-two federal securities class actions were filed in 2017, a 44% increase over 2016 and an 89% increase over 2015. *Id.* Part of this increase can be attributed to a dramatic growth in merger-objection cases, which were historically filed in state courts, but are filed there less often after recent state court rulings. *Id.* at 4–5. However, the probability of a firm being targeted in a securities action with "core" allegations has also increased. *Id.*; *see also* CORNERSTONE RESEARCH, SECURITIES CLASS ACTION FILINGS: 2017 YEAR IN REVIEW 3 (2018) (finding that 2017 was a record year for the percentage of U.S. exchange-listed companies sued under "core filings" (defined as those filings with Rule 10b-5, § 11, or § 12(2) claims)). R

206. *See* Boettrich & Starykh, *supra* note 194, at 3. R

this increase is attributable to the rise of "emerging" law firms that are more likely to bring securities cases based upon "business disruptions or disasters," rather than the more traditional "financial misstatement" rationale.[207] Accordingly, the recent increase in class actions is driven in part by exactly the type of firm that would use a non-traditional issue, such as non-disclosure of sexual misconduct,[208] as a basis for a disclosure liability suit.

Moreover, the future resolution of sexual misconduct disclosure cases has the potential to serve as a blueprint and lure for privately enforced sexual misconduct disclosure litigation. Securities class actions premised on non-disclosure of sexual misconduct have been filed against companies such as Signet Jewelers,[209] Wynn Resorts,[210] and CBS.[211] These cases will serve as a model for other private enforcers to follow in future instances of sexual misconduct non-disclosure. For example, Shira Scheindlin, a former judge in the U.S. District Court for the Southern District of New York, stated that the CBS lawsuit foreshadows a litigation trend.[212] Moreover, a successful settlement or verdict will further entice other profit-motivated private enforcers to file similar suits.[213]

In sum, the above-delineated factors combine to make it more likely that public enforcers and private litigants will pursue public corporations for sexual misconduct disclosure violations. These factors have created an environment where sexual misconduct disclosure liability is a reality that public corporations must face, before it is too late.

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207. Sara Randazzo, *Companies Face Record Number of Shareholder Lawsuits*, WALL ST. J. (Aug. 21, 2017 5:30 AM), https://www.wsj.com/articles/why-lawsuits-targeting-stock-drops-are-on-the-rise-1503307800 [https://perma.cc/ZT69-39NX].

208. *Compare id.* (defining Pomerantz LLP as an "emerging firm"), *with* CBS Complaint, *supra* note 18 (shareholder class action suit, arguing the company misled investors by failing to disclose sexual harassment allegations against CEO Leslie Moonves, filed by Pomerantz LLP). R

209. Fifth Amended Class Action Complaint, *In re* Signet Jewelers Ltd. Sec. Litig., (S.D.N.Y. 2018) (No. 1:16-cv-06728-JMF), 2018 WL 2191300 [hereinafter "Signet Complaint"].

210. Wynn Complaint, *supra* note 18. R

211. CBS Complaint, *supra* note 18. R

212. Kristen Rasmussen, *Does Investor Litigation Over #MeToo Stand a Chance?*, LAW.COM: CORPORATE COUNSEL (Sept. 4, 2018, 3:53 PM), https://www.law.com/corpcounsel/2018/09/04/does-investor-litigation-over-metoo-stand-a-chance/ [https://perma.cc/WM8X-5AVB].

("If they bring this, there will be other firms that use it as a model, and consider bringing it in similar situations. . . . Once you see one, you will see many.").

213. *See, e.g.*, Park, *supra* note 31, at 159–60. R

III.
DISCLOSING SEXUAL MISCONDUCT: WHEN AND WHAT SHOULD BE DISCLOSED

Companies would avoid much, if not all, potential sexual misconduct disclosure liability if they prevented the root problem of sexual misconduct.[214] However, in view of the fact that sexual misconduct is an unfortunate, prevalent phenomenon in the workplace,[215] companies should be prepared to include it in their disclosure discussions. Since much of the disclosure is guided by questions of materiality and a duty to disclose, a discussion of the sexual misconduct facts relevant to that analysis follows.

A. When is Sexual Misconduct Material?

The core purpose of securities disclosure is empowering and protecting investors.[216] Materiality serves an important purpose in requiring companies to filter irrelevant information and to disclose only information that has a "substantial likelihood" of altering the "total mix" of information available to investors.[217] In other words, companies need only to focus on disclosing information that is pertinent to investors.

In general, material sexual misconduct can be sorted into two main buckets: (1) sexual misconduct implicating a key executive and (2) sexual misconduct implicating a significant number of em-

214. False reports of sexual misconduct are rare. *Cf.* JO LOVETT & LIZ KELLY, LONDON METRO. UNIV., DIFFERENT SYSTEMS, SIMILAR OUTCOMES? TRACKING ATTRITION IN REPORTED RAPE CASES ACROSS EUROPE 1, 112 (2009), http://kunskapsbanken.nck.uu.se/nckkb/nck/publik/fil/visa/197/different [https://perma.cc/NJ9S-GCCV] (indicating European false reporting rates of rape are between 1% and 9%); LIZ KELLY, JO LOVETT & LINDA REGAN, HOME OFFICE RESEARCH STUDY 293: A GAP OR A CHASM? ATTRITION IN REPORTED RAPE CASES 52–53 (U.K.) (2005), https://www.researchgate.net/publication/238713283_Home_Office_Research_Study_293_A_gap_or_a_chasm_Attrition_in_reported_rape_cases [https://perma.cc/ZJ7Q-KQRW] (estimating that only 3% of cases of sexual violence reported to the UK police are found or suspected to be false).

215. *See* Lublin, *supra* note 137 (citing AMA survey that found that about 51% of female executives, managers and professionals say they have been sexually harassed on the job, and a similar proportion say they have witnessed it). **R**

216. *See, e.g.*, White, *supra* note 79 ("The core purpose of disclosure, of course, is to provide investors with the information they need to make informed investment and voting decisions. Such information makes it possible for investors to evaluate companies and have the confidence to invest and, as a result, allow our capital markets to flourish."). **R**

217. TSC Indus. v. Northway, Inc., 426 U.S. 438, 448 (1976); *see also id.* at 448 ("Some information is of such dubious significance that insistence on its disclosure may accomplish more harm than good.").

ployees.[218] Nevertheless, materiality is inherently "fact-specific," and so companies will need to evaluate the individual costs[219] they face from alleged or proven sexual misconduct.[220]

1. Executive Misconduct

The concept of materiality should and does cover executive misconduct.[221] Studies have shown that corporate officer misbehavior often has a significant effect on a corporation's reputation and stock price.[222] David Larcker and Bryan Tayan of the Rock Center for Corporate Governance at Stanford University, recently examined thirty-eight incidents of CEO misconduct and measured the resulting corporate consequences.[223] A number of their findings illustrate why CEO misconduct is typically material to investor

218. *See infra* Section III.A.

219. *See supra* Section II.A.2.

220. The Wynn example illustrates how facts specific to each corporation impact the materiality analysis. The reports on Wynn's alleged sexual misconduct by the *Wall Street Journal* were particularly impactful to Wynn Resorts' reputation because of surrounding circumstances. Wynn was the CEO of Wynn Resorts and was highly identified with the company's brand, given that he was its founder and that it shared his name. *See* Nina Munk, *Steve Wynn's Biggest Gamble*, VANITY FAIR, (June, 2005), https://www.vanityfair.com/news/2005/06/steve-wynn-las-vegas-resort [https://perma.cc/UU3Z-3JAP]. Furthermore, the company was highly regulated by state and international gaming regulators, who had the ability to revoke the company's gambling licenses if they determined that Wynn was "not 'suitable' as a casino operator." Susan Pulliam, John Kamp, Chris Kirkham & Kate O'Keeffe, *Misconduct Allegations Against Steve Wynn Put Big Casino Project at Risk*, WALL ST. J. (Jan. 31, 2018, 7:51 PM), https://www.wsj.com/articles/massachusetts-review-of-wynn-allegations-holds-high-stakes-for-casino-1517400000 [https://perma.cc/6UYU-T344]. Indeed, some of these regulators began investigating the sexual misconduct allegations. Kirkham et al., *supra* note 19. These investigations put massive investments by Wynn Resorts at risk, including a billion-dollar casino investment in Massachusetts. Pulliam et al., *supra* note 220. R R

221. *See, e.g.*, Press Release, SEC, SEC Charges Former Carter's Executive with Fraud and Insider Trading (Dec. 20. 2010), https://www.sec.gov/news/press/2010/2010-252.htm [https://perma.cc/SHZ8-JRSJ] (alleging that Carter's, Inc.'s former Executive Vice President's misconduct caused an understatement of Carter's expenses and a material overstatement of its net income in several financial reporting periods).

222. *See, e.g.*, EDWIN H. SUTHERLAND WITH GILBERT GEIS & COLIN GOFF, WHITE COLLAR CRIME: THE UNCUT VERSION (1983); MARSHALL B. CLINARD & PETER C. YEAGER WITH RUTH BLACKBURN CLINARD, CORPORATE CRIME (1st ed., 1980); Appendix B.

223. They identified thirty-eight incidents where a CEO's behavior garnered a meaningful level of media coverage (defined as more than ten unique news references). 21% of these incidents involved a sexual affairs or relations with a subordinate, contractor, or consultant and 16% involved CEOs engaging in objectionable personal behavior or using abusive language. David Larcker & Brian

decisions. For one thing, CEO misconduct is widely reported[224] and has a long-lasting and significantly detrimental impact on a company.[225] Moreover, CEO misconduct has a widespread effect on a company because it can stimulate additional fall-out and is often indicative of wider company culture.[226] Finally, misbehaving CEOs tend to be recidivists and one incident of misconduct therefore suggests more misconduct will result in the future.[227] Thus, it is no surprise that investors generally react negatively to news of executive misconduct.[228]

Sexual misconduct allegations against corporate executives therefore raise real risks of material misstatements and resulting disclosure liability.[229] Since executive misconduct is profoundly impactful, companies should immediately begin disclosure discussions as soon as proven or alleged executive misconduct is revealed.

Tayan, *We Studied 38 Incidents of CEO Bad Behavior and Measured Their Consequences*, HARV. BUS. REV., June 9, 2016.ERROR! HYPERLINK REFERENCE NOT VALID.

224. "The media widely and actively reports allegations of personal misconduct, and because of their prominence, CEOs who engage in bad behavior are an attractive target for news coverage." David F. Larcker & Brian Tayan, *Scoundrels in the C-Suite*, STAN. CLOSER LOOK SERIES 2 (May 10, 2016), https://www.gsb.stanford.edu/sites/gsb/files/publication-pdf/cgri-closer-look-57-scoundrels-csuite.pdf [https://perma.cc/ZUW6-XQDE].

225. For example, news stories today continue to reference former American Apparel CEO Dov Charney's odd behavior of walking around the company's offices in his underwear, even though it was first reported over ten years ago. *See* Larcker & Tayan, *supra* note 223. R

226. "Forty-five percent of companies in the sample experienced a significant unrelated governance issue following the event, such as an accounting restatement, unrelated lawsuit, shareholder action, or bankruptcy." *Id.* Debra Katz, a lawyer specializing in sexual harassment explains, "If you have a company with an abuser on the top, they typically surround themselves with people like them, who engage in similar behavior. . . . It can put a set of enablers in place, who protect powerful people when they get challenged for misconduct, and who work to discredit and manage out women who come forward with allegations." Farrow, *supra* note 13. R

227. "21 percent of individuals in the sample were reported to have engaged in previous or subsequent questionable behavior, including allegations of sexual harassment, insider trading, and other infractions, felonies, or misdemeanors." Larcker & Tayan, *supra* note 224. R

228. Among the companies in the sample, share prices declined by a market-adjusted 3.1% (1.1% median) over the three-day trading period after the initial news story of CEO misconduct. Larcker & Tayan, *supra* note 223; *see also* Appendix B. R

229. For example, securities class actions filed against Wynn Resorts and CBS Corporation argue that these companies materially mislead investors by failing to disclose sexual harassment allegations against their CEOs. *See, e.g.*, CBS Complaint, *supra* note 18; Wynn Complaint, *supra* note 18. R

2. Widespread Misconduct

In contrast to CEO misconduct, a different situation arises when only a few lower-level employees commit or are accused of sexual improprieties.[230] Investors do not pay attention to every allegation of sexual misconduct against a public company's employees.[231] Isolated instances of sexual misconduct by low-level employees do not rise to the level of materiality.

On the other hand, allegations that a significant number of employees have committed sexual misconduct will often be material information to investors.[232] For one thing, widespread corporate sexual misconduct can contribute to an executive's firing even when the executive was not directly involved in the conduct.[233] It

230. *Cf.* White, *supra* note 79 ("When disclosure gets to be 'too much' or strays from its core purpose, it could lead to what some have called 'information overload.'"). For example, investors knew there was were sexual harassment complaints against Signet Jewelers, but only instituted a securities class action after its widespread nature was revealed. *Compare* Signet Complaint, *supra* note 209, at 57, *with* Harwell, *supra* note 15.

231. *Cf.* TSC Indus. v. Northway, Inc., 426 U.S. at 448 ("Some information is of such dubious significance that insistence on its disclosure may accomplish more harm than good.").

232. For example, a currently pending class action complaint against Signet Jewelers argues that the company materially misled investors by failing to disclose the alleged company culture of sexual harassment. Signet Complaint, *supra* note 209. Signet, like many public companies, has forced all employees to agree to arbitration for labor disputes. *See* Harwell, *supra* note 15; *see also* Alexander J.S. Colvin, *The Growing Use of Mandatory Arbitration*, Econ. Policy Inst. 1–2 (Sept. 27, 2017), https://www.epi.org/files/pdf/135056.pdf [https://perma.cc/JZH7-4C2D] (reporting, among other things, that more than half of nonunion private-sector employers have mandatory arbitration procedures). As a result, hundreds of allegations of sexual misconduct, including those against key executives, were hidden from the public until they were revealed by the *Washington Post*. Harwell, *supra* note 15. The class action alleges, among other things, that Signet Jewelers did not adequately disclose the extent of a gender-related discrimination class action filed against the company, including its size, its likelihood of success, and the importance to the company of some of the accused. *See* Signet Complaint, *supra* note 209, at 57–83. In fact, as the *Washington Post* report revealed, the sex discrimination class action included 249 signed affidavits and had swollen to 69,000 class members. *See* Harwell, *supra* note 15. Additionally, the accusations were significant enough to have brand implications, as evidenced by the article's impact on brand score. *See* Marzilli, *supra* note 151. Over the course of the year, Signet's stock lost more than one-third of its value. Mamta Badkar, *Signet Jewelers is S&P 500's Worst Performer So Far This Year*, Fin. Times (Mar. 7, 2017), https://www.ft.com/content/96def5f8-9525-3d92-b434-df1a9ebfb03d [https://perma.cc/Q8P5-HCCP].

233. Eric Newcomer & Brad Stone, *The Fall of Travis Kalanick Was a Lot Weirder and Darker Than You Thought*, Bloomberg Businessweek (Jan. 18, 2018, 5:00 AM), https://www.bloomberg.com/news/features/2018-01-18/the-fall-of-travis-kalanick-was-a-lot-weirder-and-darker-than-you-thought [https://perma.cc/SYP2-NH5E]

can also result in negative media attention,[234] which leads to public and private enforcement efforts.[235] Widespread misconduct further has negative brand consequences, which will affect consumer decisions,[236] while also harming the corporation in other ways.[237] Pervasive misconduct can even lead to other lawsuits,[238] which can result in a material amount of financial penalties.[239] In sum, when a company uncovers increasing amounts of proven or alleged sexual misconduct, its disclosure discussions should be increasing as well.

B. Disclosure of Material Sexual Misconduct

As required by the 34 Act and subsequent regulations imposed by the SEC,[240] public companies have affirmative duties to disclose certain information as it relates to material sexual misconduct.[241] Outside of these affirmative duties, companies should remain mindful of the statements they make regarding sexual misconduct.[242] Statements made prior to the detection of sexual misconduct will generally not lead to direct liability, but could potentially create a "duty to correct" or "update" under Rule 10b-5.[243] Moreover, while Rule 10b-5 imposes no *per se* duty to reveal even material wrongdoing,[244] it does impose a duty to not be misleading.[245] Therefore, a company must decide between speaking truthfully or not at all in order to avoid securities liability following a material corporate sexual misconduct event.

1. Pre-Detection Statements

As long as they are careful, public companies need not fear disclosure liability due to statements made prior to sexual misconduct. Public companies may have a "duty to correct" disclosures

(stating that corporate sexual harassment was a contributing factor in Uber CEO Travis Kalanick's forced sabbatical and ultimately his firing).

234. *See, e.g.*, *id.*

235. *See supra* Section II.B.

236. *See, e.g.*, Sierra et al., *supra* note 20, at 187; Marzilli, *supra* note 151. R

237. *See* Kim et al., *supra* note 136, at 21–22. R

238. *See, e.g.*, Flaherty, *supra* note 17. R

239. *Compare* 17 C.F.R. § 229.103 (2019) (lawsuits can rise to a material level), *with* Signet Complaint, *supra* note 209, at 57–83 (attempting to claim that sexual misconduct lawsuits will result in a material financial penalty). R

240. *See SEC*, *supra* note 22. R

241. *See infra* Section III.B.

242. *See id.*

243. *See infra* notes 246–249 and accompanying text. R

244. *See* Matrixx Initiatives, Inc. v. Siracusano, 563 U.S. 27, 44 (2011).

245. 17 C.F.R. § 240.10b-5(b) (2019).

that were materially false at the time they were made.[246] And public companies may be subject to a "duty to update" in some—but not all—jurisdictions, which is triggered when a disclosure becomes materially false as a result of new developments.[247] On the other hand, there will not be a direct finding of disclosure liability for pre-detection sexual misconduct statements because the scienter requirement[248] of disclosure liability will not be satisfied.[249]

Many corporate statements regarding sexual misconduct will naturally be made in the context of ethics programs. In that context, "It is well-established that general statements about reputation, integrity, and compliance with ethical norms are inactionable 'puffery,' meaning that they are 'too general to cause a reasonable investor to rely upon them.'"[250] Accordingly, recent court decisions, discussed below, indicate that actions and statements contradictory to a company's ethics code will generally not trigger a duty to correct or update. However, public companies should be particularly vigilant in avoiding repeated ethical lapses, especially if the company has indicated that the conduct had ceased.

In *Retail Wholesale & Department Store Union Local 338 Retirement Fund v. Hewlett-Packard Co.* (*Retail Wholesale*),[251] for example, the

246. Bruce Mendelsohn and Jesse Brush, *The Duties to Correct and Update: A Web of Conflicting Case Law and Principles*, 43 SEC. REG. L.J. 43, 72–74 (2015).

247. *See id.* at 74–80.

248. The Supreme Court held, in *Ernst & Ernst v. Hochfelder*, that a civil damage action under Rule l0b-5 requires a showing of scienter. 425 U.S. 185, 193 (1976). Four years later, the Supreme Court said that the SEC also had to prove scienter in its Rule 10b-5 cases, explaining that "the rationale of *Hochfelder* ineluctably leads to the conclusion that scienter is an element of a violation of § 10(b) and Rule 10b-5, regardless of the identity of the plaintiff or the nature of the relief sought." Aaron v. SEC, 446 U.S. 680, 691 (1980).

249. There are some commentators who believe that a lack of scienter precludes a duty to correct as well. *See* J. ROBERT BROWN, JR., REGULATION OF CORPORATE DISCLOSURE § 10.04[C] (Allison Herren Lee ed., Wolters Kluwer 4th ed. Supp. 2019-1) ("There is no inherent reason why, under the federal securities laws, a statement must be corrected if false at the time issued. As long as the incorrect statement was made without scienter, no violations of the antifraud rules occurred. Thereafter, the statement is no different in practice from one that became false as a result of subsequent developments. The basis for requiring the correction of one but not the other remains obscure.").

250. Pontiac Policemen's & Firemen's Ret. Sys. v. UBS AG, 752 F.3d 173, 183 (2d Cir. 2014).

251. The facts of the case are as follows. In 2006, a whistleblower informed the government that HP had hired detectives to monitor phone records and email accounts of HP employees. 845 F.3d 1268, 1272 (9th Cir. 2017). Criminal charges were brought against the then-Chair and General Counsel of HP. *Id.* Following the charges, HP took every opportunity it could to convince the public that it had improved its company code of ethics. *Id.* And despite the scandal, the CEO of HP,

Ninth Circuit held that alleged inappropriate sexual behavior by a corporate executive need not be disclosed simply because it may have violated an "aspirational" company code of ethics.[252] A plaintiff class had sued Hewlett Packard (HP), alleging: "(1) HP and [CEO] Hurd actively promoted the [company code of ethics ('SBC')] and stated that HP had zero tolerance for SBC violations; (2) Hurd's SBC violations led to his resignation; and (3) Hurd's resignation caused HP's stock price to drop."[253] The Ninth Circuit upheld the district court's dismissal of the complaint and found that HP's touting of their ethics program was effectively immaterial "puffing," because ethics codes are "inherently aspirational" and not capable of "objective verification."[254] Hurd's sexual misconduct itself may very well have been material to investors since it predictably led to his resignation. But because § 10(b) and Rule 10b-5(b) do not create an affirmative duty to disclose any and all material information,[255] the court found that a duty to disclose was missing and Hurd's failure to comply with a company's ethics program did not trigger a corrective disclosure duty.[256]

Retail Wholesale could have had a different outcome if HP had instead made unequivocal ethics statements. For example, if the company had said, "Hurd has not violated our code of conduct" but later found out he had, then a failure to make a corrective disclo-

Mark Hurd, remained highly respected. *Id.* ("HP, its stockholders, and Wall Street insiders viewed Hurd as one of HP's most valuable assets, seeing his leadership as the 2006 scandal's silver lining."). This changed when HP's Board of Directors received a letter from attorney Gloria Allred alleging that Hurd had, among other things, sexually harassed her client, Jodie Fisher. *Id.* The HP Board promptly launched an internal investigation, which found that Hurd falsified expense reports and lied about his relationship with Fisher. *Id.* at 1273. Hurd immediately resigned from his position at HP and the price of HP stock fell 10% in one day. Ashlee Vance, *Boss's Stumble May Also Trip Hewlett-Packard*, N.Y. TIMES (Aug. 8, 2010), http://www.nytimes.com/2010/08/09/technology/09hp.html [https://perma.cc/S7N3-Z9BF] (reporting that "H.P.'s share price tumbled 10 percent on Friday as word of Mr. Hurd's departure rippled through Wall Street").

252. 845 F.3d 1268, 1278 (9th Cir. 2017).

253. *Id.* at 1275.

254. *Id.* at 1275–77 ("It simply cannot be that a reasonable investor's decision would conceivably have been affected by HP's compliance with SEC regulations requiring publication of ethics standards.").

255. Matrixx Initiatives, Inc. v. Siracusano, 563 U.S. 27, 44 (2011).

256. To the contrary, the court observed that "it appears that HP's ethics and compliance policies worked. Hurd did not live up to HP's standards; HP became aware of Hurd's ostensible misconduct; HP quickly launched an investigation, confirming the misconduct; and Hurd resigned." *Retail Wholesale*, 845 F.3d at 1277 n.3. Accordingly, *Retail Wholesale* suggests that public companies can implement and act on ethics programs without resulting disclosure liability.

sure would have been a material omission.[257] The unequivocal statement distinction is also shown in *In re Omnicare, Inc. Securities Litigation* (*Omnicare*).[258] In *Omnicare*, the company received key information, namely audit results revealing "substantial fraud" and "billing irregularities,"[259] but failed to correct previous unequivocal statements.[260] While the *Omnicare* court did not find scienter existed, they did find a "material omission."[261]

Public companies should also be particularly vigilant in avoiding repeated ethical lapses because courts in such scenarios may be more likely to find a material misstatement or omission.[262] For example, the Ninth Circuit, in *Retail Wholesale*, noted it "would likely be different if HP had continued the conduct that gave rise to [a] 2006 scandal while claiming that it had learned a valuable lesson in ethics."[263] In fact, the Sixth Circuit, in *Omnicare*, found that the company in question had a recent history of non-compliance issues

257. There is an important difference between a company's announcing rules forbidding conduct and its factual representation that that no officer has engaged in such forbidden conduct. *See In re* PetroChina Co. Sec. Litig., 120 F. Supp. 3d 340, 360 (S.D.N.Y. 2015) ("Although the Company's codes of ethics prohibit bribery and other forms of fraudulent conduct, they do not claim that PetroChina's officers are abiding by them. Since the [complaint] does not challenge the actual existence of these rules, nor PetroChina's description of them, Plaintiffs have not demonstrated that the Company's statements were false or misleading.").

258. *In re* Omnicare, Inc. Sec. Litig., 769 F.3d 455 (6th Cir. 2014).

259. *Id.* at 479.

260. Omnicare's material-compliance statements in its 10-K forms stated, "We believe that our billing practices materially comply with applicable state and federal requirements." They also stated, "[W]e believe that we are in compliance in all material respects with federal, state and local laws." *Id.* at 477–78.

261. *Id.* at 480–81.

262. *See In re* Petrobras Sec. Litig., 116 F. Supp. 3d 368, 380 (S.D.N.Y. 2015). In this case, the court held that a company's statements about its "general integrity and ethical soundness" were not immaterial as a matter of law. *Id.* at 380. The court said that although statements "viewed in isolation, may be mere puffery," the defendant had repeatedly used the statements "in an effort to reassure the investing public about the Company's integrity," so as to cause "a reasonable investor [to] rely on them as reflective of the true state of affairs at the Company." *Id.* at 381. Therefore, "[w]hether a representation is 'mere puffery' depends, in part on the context in which it is made." *Id.*

263. Retail Wholesale, 845 F.3d at 1278. The court commented that the context of statements is only relevant to the materiality prong and not to the misrepresentation prong of disclosure liability. *Id.* (citing to Matrixx Initiatives, Inc. v. Siracusano, 563 U.S. 27, 43–47 (2011)). The court then ignored the context of the HP's previous ethics scandal and determined that the statements were not material. However, the court seemed to imply that context would matter if the conduct had been more similar to that of the 2006 scandal. *Id.*

and therefore the subsequent non-compliance was material information to investors.[264]

As a general rule, then, public companies should avoid making unequivocal statements related to ethics, including issues pertaining to sexual misconduct. Further, companies should make an extra effort to avoid statements related to previous ethical lapses, since these incidents could contribute to the statements' materiality.

2. Post-Detection Affirmative Duties to Disclose

Federal securities laws, and the rules[265] and regulations[266] promulgated thereunder, affirmatively require the disclosure of certain information. Public companies have an ongoing obligation to disclose information,[267] but only in rare circumstances will a company have a duty to disclose sexual misconduct. Additionally, some corporate actions trigger an immediate duty to disclose material information,[268] including sexual misconduct that is material.

Item 103 of Regulation S-K, entitled "Legal proceedings," is particularly relevant to potential sexual misconduct disclosure liability.[269] Naturally, it mandates disclosure of "any material pending legal proceedings."[270] Item 103 also states, however, that "[n]o information need be given with respect to any proceeding that involves primarily a claim for damages if the amount involved . . . does not exceed 10 percent of the current assets of the

264. *In re Omnicare*, 769 F.3d 455 at 478.

265. *See, e.g.*, 17 C.F.R. § 240.10b-5 (2019).

266. *See, e.g.*, 17 C.F.R. §§ 243.100-243.103 (2019).

267. *See, e.g.*, 17 C.F.R. § 229.103 (2019); 17 C.F.R. § 229.303 (2019). Hemel and Lund argue that sexual misconduct may also trigger a duty to disclose under Item 402, which requires public companies to publish details on compensation paid to its CEO, CFO, and the three other most highly paid employees. *See* Hemel & Lund, *supra* note 33, at 42; *see also* 17 C.F.R. § 229.402 (2019). They argue that "if the company—in effect—allows its CEO to seek sexual pleasure through the harassment of employees and then pays to clean up the resulting legal mess," this could arguably constitute a "perquisite" that must be disclosed under Item 402. *Id.* at 53. R

268. *See, e.g.*, 17 C.F.R. §§ 243.100-243.103 (2019).

269. Many legal proceedings are typically publicly filed, which can simplify a company's disclosure decision. However, as the Signet Complaint reveals, sexual misconduct litigation is often obscured by arbitration provisions, which could potentially tempt a company to hide the extent of the litigation from the public. Signet Complaint, *supra* note 209, 82–83. R

270. 17 C.F.R. § 229.103 (2019).

registrant and its subsidiaries on a consolidated basis."[271] Item 103 further requires companies to describe any legal proceedings "known to be contemplated by government authorities,"[272] although it is doubtful that the term "legal proceedings" would pertain to many internal or government investigations of sexual misconduct. For example, in *In re Lions Gate Entertainment Corp. Securities Litigation*, the U.S. District Court for the Southern District of New York held that an SEC investigation, or even the receipt of a Wells Notice, is not *per se* material to investors and therefore need not always be disclosed.[273] The court held that the mere "possibility of materiality" is not enough to support a securities fraud claim.[274] In other words, the court found that while a public investigation may prompt the beginning of a disclosure conversation, companies need not disclose investigations under Item 103 until legal proceedings have begun. In essence, the affirmative disclosure duties imposed by Item 103 are actually rather limited.

Item 303 of Regulation S-K, entitled "Management's discussion and analysis of financial condition and results of operations," requires public companies to disclose "any known trends or uncertainties that have had or that the company reasonably expects will have a material favorable or unfavorable impact on net sales or rev-

271. 17 C.F.R. § 229.103(2) (2019). Because the materiality standard is often assessed relative to the size of a company, there are times it does not apply to large companies that fail to disclose information that would rise to the level of materiality at smaller companies, thereby leading to "materiality blindspots." *See* George S. Georgiev, *Too Big to Disclose: Firm Size and Materiality Blindspots in Securities Regulation*, 64 UCLA L. Rev. 602, 633 (2017). For example, Twenty-First Century Fox's sexual misconduct-related settlement payments, while large, were relatively small compared to the total size of the company. *Compare* Fountain & Folkenflik, *supra* note 156 (reporting that Gretchen Carlson's settlement was for $20 million and experts said it was ambiguous whether the settlement payments were significant enough on a financial basis to warrant disclosure), *with* Press Release, The Walt Disney Co., The Walt Disney Company to Acquire Twenty-First Century Fox, Inc., After Spinoff of Certain Businesses, for $52.4 Billion in Stock (Dec. 14. 2017), https://thewaltdisneycompany.com/walt-disney-company-acquire-twenty-first-century-fox-inc-spinoff-certain-businesses-52-4-billion-stock-2/ [https://perma.cc/ECM3-4ZA8] (revealing that Twenty-First Century Fox was worth many multiples of $20 million). R

272. 17 C.F.R. § 229.103 (2019).

273. 165 F. Supp. 3d 1, 12 (S.D.N.Y. 2016) ("[T]he defendants did not have a duty to disclose the SEC investigation and Wells Notices because the securities laws do not impose an obligation on a company to predict the outcome of investigations. There is no duty to disclose litigation that is not 'substantially certain to occur.'").

274. *Id.* at 14.

enues or income from continuing operations."[275] The Supreme Court is currently considering whether there is a disclosure duty under Item 303 that is actionable under § 10(b) of the 34 Act.[276] If the court finds that there is, Item 303 may require companies to disclose information related to sexual misconduct in order to avoid disclosure liability.[277] For instance, the SEC issued Item 303 "cyber-attack" guidance which states, "If it is reasonably likely that the attack will lead to reduced revenues, an increase in cybersecurity protection costs, including related to litigation, the registrant should discuss these possible outcomes, including the amount and duration of the expected costs, if material."[278] By analogy, if a sexual misconduct allegation leads to a material amount of reduced revenues or increased compliance and litigation costs, a public company presumably should conduct Item 303 disclosure.

Additionally, as the Supreme Court emphasized in *Chiarella v. United States*, certain corporate actions trigger a duty to disclose material non-public information (MNPI).[279] Under insider trading doctrine, for example, companies and corporate insiders have a duty to disclose all material facts before buying or selling the company's securities.[280] Furthermore, Regulation FD mandates that when public companies disclose MNPI, they do so to all investors at

275. 17 C.F.R. § 229.303 (2019).

276. *See* Leidos, Inc. v. Ind. Pub. Ret. Sys., 137 S. Ct. 1395 (2017). *Compare* Ind. Pub. Ret. Sys. v. SAIC, Inc., 818 F.3d 85, 95 (2d Cir. 2016) (supporting the contention that there is a disclosure duty under Item 303 that is actionable under 10(b)), *with* Oran v. Stafford, 226 F.3d 275, 288 (3d Cir. 2000) (rejecting that contention).

277. In *Indiana Public Retirement System v. SAIC, Inc.*, investors alleged that the corporation was aware of employee wrongdoing in connection with a city contract and the corporation's potential liability to that city but still did not disclose it on the corporation's 10-K. 818 F.3d 85, 85 (2d Cir. 2016). An analogous sexual misconduct scenario would arise if a company knows of sexual misconduct and its potential liability but fails to disclose it.

278. SEC, *supra* note 88. R

279. 445 U.S. 222, 228 (1980) ("[O]ne who fails to disclose material information prior to the consummation of a transaction commits fraud only when he is under a duty to do so. And the duty to disclose arises when one party has information that the other [party] is entitled to know because of a fiduciary or other similar relation of trust and confidence between them.") (internal citations omitted).

280. *Id.* ("Application of a duty to disclose prior to trading guarantees that corporate insiders, who have an obligation to place the shareholder's welfare before their own, will not benefit personally through fraudulent use of material, nonpublic information."); *see also*, United States v. O'Hagan, 521 U.S. 642, 651–53 (1997) (explaining the "classical" and "misappropriation" theory of insider trading liability).

the same time;[281] if a company unintentionally discloses MNPI to only a few people, it must cure the problem by promptly disclosing that information to the rest of the public.[282] In another example, public companies have certain disclosure obligations while they are undergoing a merger or acquisition.[283] Therefore, to the extent that a company knows of material sexual misconduct, they must disclose it when there is a triggering event, such as insider trading or partial disclosure.

Furthermore, under § 10(b) and Rule 10b-5, public companies must not make any misleading statements concerning material sexual misconduct.[284] Accordingly, companies must be complete when publicly discussing such issues. "Complete" does not necessarily mean disclosing all information related to the incident—for example, companies should avoid disclosing the names of victims or any facts that would make those victims easily identifiable.[285] However, when a company makes a misleadingly incomplete disclosure regarding material sexual misconduct, they have a duty to disclose all information necessary to make that statement not misleading. Therefore, public companies can control their duty to disclose material sexual misconduct under Rule 10b-5, in part, by limiting their public statements.[286] Even so, it may be unrealistic to expect that public companies will be able to remain silent about material sexual misconduct. As explained below, the longer a company holds onto a material fact without disclosure, the more it risks being accused of making a misleading statement.

Otherwise innocuous comments can trigger 10b-5 liability when a company holds onto information related to material misconduct. A recent case in the Southern District of New York, *In re*

281. 17 C.F.R. §§ 243.100-243.103 (2019).

282. *Id.*

283. *See, e.g.*, Article 11 of Regulation S-X, 17 CFR § 210.11-01 (2014) (generally requiring the provision of pro forma financial information where a significant acquisition or disposition "has occurred or is probable"); Item 14 of Schedule 14A, 17 CFR § 240.14a-101 (requiring Article 11 pro forma financial information and extensive other information about certain extraordinary transactions if shareholder action is to be taken with respect to such a transaction).

284. *See supra* notes 25, 87–91, 116, 117 and accompanying text. R

285. The EEOC found "reasonable cause" to believe that an employer violated Title VII when it revealed the name of a former employee with a pending sexual harassment claim against the company and characterized the claim as "meritless"; the Seventh Circuit agreed that the disclosure "constituted a material adverse employment action" because it "might be negatively viewed by future employers." Greengrass v. Int'l Monetary Sys., Ltd., 776 F.3d 481, 484 (7th Cir. 2015).

286. *See* analysis *supra* Section I.D.

VEON Ltd. Securities Litigation, is an apt example.[287] VEON entered into a deferred prosecution agreement with the United States Department of Justice, pursuant to which the company pled guilty to Foreign Corrupt Practices Act violations.[288] The company was also promptly sued for disclosure liability and found to have made material misstatements.[289] For example, VEON credited its "sales and marketing efforts" for the growth of its operations in Uzbekistan without mentioning that it had also paid bribes to obtain business.[290] Additionally, VEON's disclosure about owners of telecommunications networks in Uzbekistan enjoying "equal protection guaranteed by law," were found to be misleading since VEON had to pay bribes to operate in the country.[291] Essentially, VEON's statements, although initially appearing to be general business statements, gave rise to disclosure liability following the revelation of FCPA violations and 20/20 hindsight.

Thus, public companies should question whether they can hold onto material information, such as proven or alleged sexual misconduct, without making a material misstatement. For example, many public companies routinely make general statements in their SEC filings that they rely on their senior management to succeed.[292] A court may very well find statements like these to be actionable misstatements when the company has failed to disclose proven or alleged sexual misconduct against an executive.[293] In essence, complete and immediate disclosure is the only option that fully addresses the risk of sexual misconduct disclosure liability.

CONCLUSION

Sexual misconduct has a negative impact on multiple parties. Naturally, the victims of sexual misconduct are often emotionally and physically traumatized. Consequences to the accused stemming from such allegations range from reputational damage to incarceration. In the case of corporate officers or employees, sexual misconduct allegations can also have a materially negative impact on the companies with which the accused are affiliated, which in turn can

287. No. 15-CV-08672 (ALC), 2017 WL 4162342 (S.D.N.Y. Sept. 19, 2017).

288. *Id.* at *1.

289. *Id.* at *8.

290. *Id.* at *6.

291. *Id.* at *7.

292. *See, e.g.*, Wynn Las Vegas, LLC, Annual Report (Form 10-K) at 11 (Feb. 24, 2017) ("Our ability to maintain our competitive position is dependent to a large degree on the efforts, skills and reputation of Stephen A. Wynn.").

293. *See supra* notes 173–175 and accompanying text. R

cause economic harm to investors. In such circumstances, sexual misconduct raises a corporate concern of disclosure liability under federal securities laws.

In the wake of the #MeToo movement, public corporations face a particularly significant, but underestimated, risk of sexual misconduct disclosure liability. The victims of corporate sexual misconduct are more willing to publicly fight back in the #MeToo environment. Their allegations could have a material impact on companies by imposing a variety of costs including decreased productivity, reputational damage, and litigation expenses. Additionally, the increased number of allegations, publicized nature of the sexual misconduct, and an overall increase in securities disclosure cases makes it more likely that companies will face both public and private disclosure liability enforcement efforts.

The core purpose of securities disclosure is protecting investors. Companies therefore generally need only to focus on disclosing information that is material to investors to avoid liability. Material information pertaining to sexual misconduct includes incidents that implicate key executives or a significant number of employees, especially when they are combined with other investor-important factors. As the impact, frequency, and enforcement of corporate sexual misconduct allegations increase in the #MeToo world, however, its material importance to investors will grow as well.

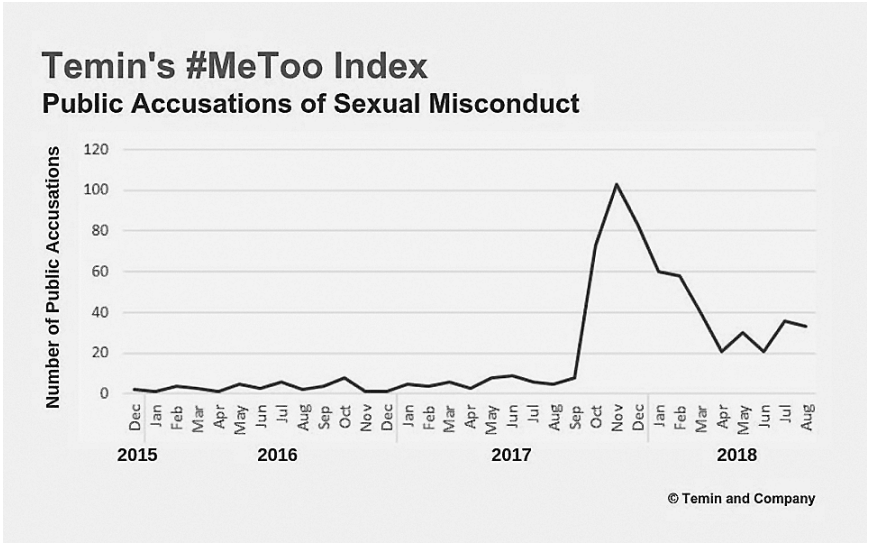
Statements made prior to the detection of sexual misconduct will not lead to direct disclosure liability, but public corporations may have a duty to correct or update previously false material statements once any misconduct is detected. The materiality of those pre-detection statements will depend on their equivocality and whether they referenced an ongoing history of sexual misconduct. Therefore, after misconduct is detected, companies should examine their earlier public statements to determine if additional disclosure is required.

After a company detects material sexual misconduct, they must also comply with affirmative duties that require disclosure of information pertaining to that misconduct. Additionally, Rule 10b-5 requires that public companies must not make any untrue statements concerning material sexual misconduct. It further requires that companies must be complete when publicly discussing material sexual misconduct; a company that makes an incomplete disclosure has a duty to complete it. Since otherwise innocuous comments can trigger Rule 10b-5 liability when a company holds onto material in-

formation, immediate disclosure is the only option that fully addresses the risk of sexual misconduct disclosure liability.

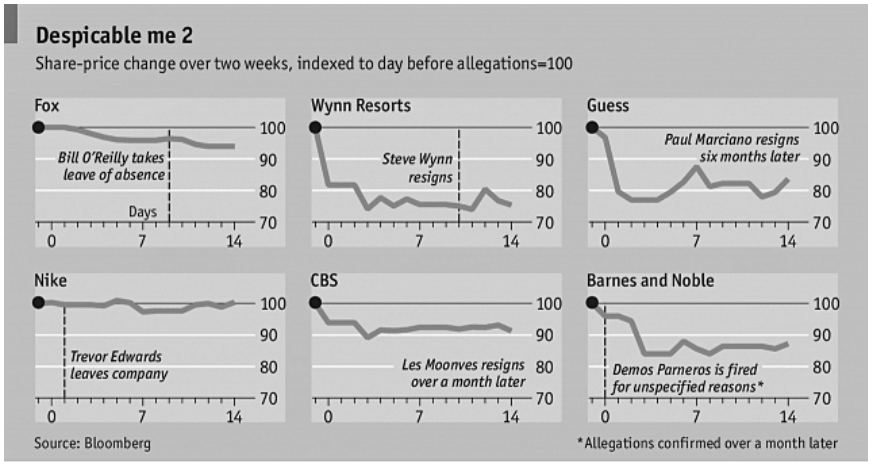
By definition, sexual misconduct can cause profound harm to everyone associated with it. Companies should not add to this harm by attempting to deceive the investing public. Instead, companies should strongly consider fully, truthfully, and immediately disclosing material sexual misconduct to the investing public.

APPENDIX A: "PUBLIC" SEXUAL MISCONDUCT ALLEGATIONS[294]



294. Davia Temin, *Les Moonves Makes No. 700 on the #MeToo Index (And Jeff Fager is 701)*, FORBES (Sept. 12, 2018, 09:58 AM), https://www.forbes.com/sites/daviatemin/2018/09/12/les-moonves-makes-700-lessons-learned-as-number-accused-of-metoo-sexual-harassment-mounts/#647ca5f73d83 [https://perma.cc/T7SZ-ZPBM] (defining a "public accusation" as one that appeared in at least seven major news stories).

APPENDIX B: SHARE-PRICE IMPACT OF ALLEGED SEXUAL MISCONDUCT[295]



The Economist

295. *American Business and #MeToo*, *supra* note 145; *see also* Tiffany Hsu & Alexandra Alter, *Barnes & Noble Says Former C.E.O. Demos Parneros Was Fired for Sexual Harassment*, N.Y. TIMES (Aug. 28, 2018), https://www.nytimes.com/2018/08/28/business/barnes-noble-ceo-sexual-harassment-lawsuit.html [https://perma.cc/X9QS-VGYQ] (describing Barnes & Noble controversy); Farrow, *supra* note 13 (describing CBS controversy); Sara Germano, *Nike Investigates Workplace Complaints, Says No. 2 Executive Resigns*, WALL ST. J. (Mar. 15, 2018, 7:58 PM), https://www.wsj.com/articles/nike-investigates-workplace-complaints-says-no-2-executive-resigns-1521153597 [https://perma.cc/8VSY-A9C4] (describing Nike controversy); Valeriya Safronova, *Paul Marciano Will Leave Guess After Sexual Harassment Settlements*, N.Y. TIMES (June 12, 2018), https://www.nytimes.com/2018/06/12/style/guess-harassment-resignation.html [https://perma.cc/D3CF-2BPE] (describing Guess controversy); Berzon et al., *supra* note 13 (describing Wynn Resorts controversy); Steel & Schmidt, *supra* note 189 (describing Twenty-First Century Fox controversy). R R R R