

**SECOND REPORT OF THE SPECIAL LITIGATION COMMITTEE  
OF THE BOARD OF DIRECTORS OF  
AFLAC INCORPORATED**

**FEBRUARY 9, 2018**

## TABLE OF CONTENTS

|  | Page |
|--|------|
| I. EXECUTIVE SUMMARY .....   | 1    |
| II. BACKGROUND .....   | 8    |
| A. The Company, Its Board Of Directors, And The Defendants.....  | 8    |
| 1. Daniel P. Amos .....  | 9    |
| 2. Paul S. Amos, II .....  | 9    |
| 3. Douglas W. Johnson .....  | 10   |
| 4. W. Paul Bowers .....  | 10   |
| 5. Barbara K. Rimer .....  | 10   |
| 6. Charles B. Knapp .....  | 11   |
| 7. Elizabeth J. Hudson .....   | 11   |
| B. Aflac Trust And The Company’s Anti-Fraud Policies .....   | 11   |
| C. The Alleged Material, Nonpublic Information .....   | 12   |
| D. The Allegations Of The Complaint.....   | 17   |
| III. THE SPECIAL COMMITTEE’S FORMATION, COMPOSITION, AND<br>INDEPENDENCE .....   | 18   |
| A. The Special Committee Is Authorized To Investigate, Evaluate, And<br>Determine Whether To Prosecute The Demanded Action. .... | 18   |
| B. The Special Committee Members Are Independent And Disinterested. ....   | 20   |
| C. The Special Committee Retained Independent Counsel.....   | 24   |
| IV. THE SCOPE OF THE SPECIAL COMMITTEE’S INVESTIGATION .....   | 25   |
| A. The Special Committee’s Investigation Included Extensive Document<br>Review. ....   | 25   |
| B. The Special Committee Interviewed Twenty-Four Witnesses .....   | 27   |
| 1. W. Paul Bowers .....  | 27   |
| 2. Melvin T. Stith.....  | 27   |
| 3. Joseph L. Moskowitz .....   | 27   |
| 4. Douglas W. Johnson .....  | 28   |
| 5. Barbara K. Rimer .....  | 28   |
| 6. Charles B. Knapp .....  | 28   |
| 7. Elizabeth J. Hudson .....   | 29   |
| 8. Daniel P. Amos .....  | 29   |



**TABLE OF CONTENTS**  
(continued)

|  | <b>Page</b> |
|--|-------------|
| G. The Special Committee Did Not Find Evidence Of Systemic Fraud Regarding “Sit Codes.” .....  | 52          |
| H. The Earnings Manipulation Allegations Are Factually Inaccurate.....   | 53          |
| I. The Whistleblower Allegations Are Without Merit. ....   | 57          |
| 1. The Evidence Does Not Support Mr. Conroy’s Allegations of Retaliation. ....   | 57          |
| 2. The Evidence Does Not Support Mr. Varela’s Allegations Of Retaliation. ....   | 59          |
| J. The Tax-Related Allegations Do Not Support A Derivative Claim. ....   | 60          |
| 1. The Company Does Not Improperly Classify Its Sales Associates. ....   | 60          |
| 2. Plaintiffs’ Allegations Regarding The Aflac Incentive Fund Are Inaccurate. ....   | 62          |
| 3. Plaintiffs’ Allegations Regarding Violation Of Cafeteria Plan Regulations Lack Merit.....   | 64          |
| VI. THE SPECIAL COMMITTEE’S CONCLUSIONS .....  | 66          |
| A. The Rule 10b-5 Claim Faces Numerous Challenges. ....  | 66          |
| 1. Plaintiffs Fail To Identify Any Materially False Or Misleading Statements. ....   | 69          |
| 2. The Complaint Fails To Allege A Strong Inference of Scienter. ....  | 76          |
| 3. Plaintiffs Have Not Shown Loss Causation Or Economic Loss. ....   | 80          |
| 4. Plaintiffs Cannot Establish Reliance.....   | 83          |
| B. The Special Committee Finds The Section 14(a) Claim To Be Without Merit.....  | 86          |
| 1. Plaintiffs’ Claim That The 2017 Proxy Is False Or Misleading Lacks Merit Because The Company Was Not Required To Disclose Unsubstantiated Allegations of Misconduct. .... | 86          |
| 2. The Company Would Most Likely Be Unable To Show Loss Causation.....   | 90          |
| 3. The Company Would Most Likely Be Unable To Show Transaction Causation.....  | 90          |
| C. The Special Committee Has Previously Rejected The Demand To Bring A 20A Claim And Reiterates That Conclusion Here.....  | 93          |

**TABLE OF CONTENTS**  
(continued)

|   | <b>Page</b> |
|---|-------------|
| D. Any Breach Of Fiduciary Duty Claim By The Company Against The Defendants Would Lack Factual Support And Be Subject To Several Defenses.....  | 93          |
| 1. The Company Would Not Be Able To Show A Breach Of The Duty Of Loyalty Under The Facts Alleged.....   | 95          |
| 2. Any Claim By The Company For Breach Of The Duty Of Care Is Subject To Strong Defenses And Any Monetary Damages Are Likely Exculpated Under the Company’s Articles of Incorporation. .... | 96          |
| 3. The Company Would Most Likely Be Unable To Establish A Claim For Failure to Maintain Adequate Controls. ....   | 100         |
| 4. The Company Would Not Be Likely To Prevail In A Claim Against The Defendants Relating To The Stock Repurchases. ....   | 102         |
| E. The Unjust Enrichment Claim Is Not Supported By The Facts.....   | 102         |
| F. The Special Committee Finds That Pursuing The Claims Raised In The Complaint Is Not In The Best Interests Of The Company.....  | 104         |
| VII. CONCLUSION.....  | 106         |

## LIST OF EXHIBITS TO THE REPORT

|     |  |
|-----|--|
| 1.  | September 21, 2017 Letter from Mary Gill to Dimitry Joffe                          |
| 2.  | Draft Derivative Complaint dated October 25, 2017                                  |
| 3.  | November 10, 2017 Letter from Mary Gill to Dimitry Joffe                           |
| 4.  | Complaint dated December 14, 2017  |
| 5.  | Investor Relations Stock Information Chart   |
| 6.  | 2017 Proxy Statement   |
| 7.  | Aflac's Board of Directors   |
| 8.  | Excerpts of Second Quarter 2017 Form 10-Q  |
| 9.  | June 6, 2017 Form 8-K  |
| 10. | December 10, 2016 Letter from Dimitry Joffe  |
| 11. | Demand Letter dated June 23, 2017  |
| 12. | Martin Conroy's Associate's Agreement  |
| 13. | January 5, 2017 Letter from Catherine Coppedge to Dimitry Joffe                    |
| 14. | March 8, 2017 Letter from Dimitry Joffe to Doug Johnson                            |
| 15. | March 28, 2017 Letter from Dimitry Joffe to Doug Johnson                           |
| 16. | 2012 Corporate Citizenship Report  |
| 17. | Initial Report   |
| 18. | July 12, 2017 Board Resolution   |
| 19. | NYSE Listed Company Manual, Independence Test                                      |
| 20. | Amendment to the Articles of Incorporation dated April 25, 1988                    |
| 21. | April 13, 2010 E-mail from Martin Conroy to Paul Amos                              |
| 22. | Screenshot of Aflac Website, Agent Testimonials                                    |
| 23. | October 20, 2015 Letter  |
| 24. | Updated SBA Guidelines   |
| 25. | E-mail from Trevor Fennell to Martin Conroy dated August 29, 2016                  |
| 26. | E-mail Chain Dated December 2015 re: Univision Details for Shared AP Credit #22082 |
| 27. | Incentive Fund Deduction Authorization   |
| 28. | Excerpt of 2017 Participant/Non-Participant Report                                 |
| 29. | 2016 Q4 Results and Outlook Report dated January 31, 2017                          |
| 30. | 2015 Q4 Results and Outlook Report dated February 1, 2016                          |

## LIST OF EXHIBITS TO THE REPORT

|     |   |
|-----|---|
| 31. | 2014 Q4 Results and Outlook Report dated February 3, 2015                       |
| 32. | Recent Fraud News May Not Have Material Impact on Aflac; Raymond James Upgrades |
| 33. | March 20, 2017 Letter from Doug Johnson to Dimitry Joffe                        |
| 34. | Yahoo Finance, Aflac Incorporated   |
| 35. | Bloomberg Stock Report  |
| 36. | Amended and Restated Bylaws   |
| 37. | Paul S. Amos, II's Separation Agreement   |
| 38. | May 4, 2017 Form 8-K  |
| 39. | E-mail from Capps to Dowless dated June 6, 2016 and attachment                  |
| 40. | Excerpt of 2015 10-K  |
| 41. | Aflac Group Website   |
| 42. | UCI Letter dated November 16, 2015  |
| 43. | Report of Investigation   |
| 44. | SIU Case Summary  |
| 45. | Truth Tour  |
| 46. | February 23, 2017 Letter to the IRS   |
| 47. | Arbitration Decision  |
| 48. | EEOC Dismissals   |
| 49. | Flex One Sample Cafeteria Plan Document Packet                                  |
| 50. | Payroll Account Acknowledgment (M-0138)   |
| 51. | Payroll Account Activation (associate version)                                  |
| 52. | Welcome to Aflac E-mail   |
| 53. | Voluntary Insurance: Go With the Group or Go it Alone                           |
| 54. | 2015 Board Authorization  |
| 55. | 2017 Board Authorization  |
| 56. | Week 39 E-mail  |
| 57. | E-mail from Conroy  |
| 58. | E-mail from Brenan to McDaniel  |
| 59. | Focus on You 2014 Budget Overview Presentation                                  |
| 60. | Excerpt of Q4 2017 FAB Supplement   |

## LIST OF EXHIBITS TO THE REPORT

|     |  |
|-----|--|
| 61. | Aflac Trust 2018: Understanding Insurance Fraud and Prohibited Practices |
| 62. | Code of Conduct  |
| 63. | Aflac Trust 2018: Compliance Fraud Analytics Scheme Information          |
| 64. | Excerpts from 2016 Form 10-K   |
| 65. | 1/22/18 Report of Investigation  |
| 66. | E-mail dated September 26, 2016  |
| 67. | 2014 Production Calendar   |
| 68. | 2015 Production Calendar   |
| 69. | 2016 Production Calendar   |

## **I. EXECUTIVE SUMMARY**

On July 12, 2017, the Board of Directors of Aflac Incorporated (the “Company”) passed a resolution forming a special litigation committee (the “Special Committee”) to investigate and evaluate allegations of wrongdoing set forth in a June 23, 2017 letter from an attorney named Dimitry Joffe on behalf of four purported shareholders<sup>1</sup> of the Company (the “Demand Letter”). The Demand Letter claimed that Paul S. Amos, II “violated his fiduciary duties to the Company and its shareholders, as well as committed securities fraud,” and demanded, pursuant to O.C.G.A. § 14-2-831, that the Company take “suitable action” against Paul Amos for alleged insider trading. The Demand Letter claimed Paul Amos sold shares of Company stock while purportedly in possession of material, nonpublic information, namely, knowledge of alleged fraudulent activities at the Company (and the investigation thereof) as described in several letters sent by Mr. Joffe to members of the Company’s senior management, several members of the Board of Directors, and others in December 2016 and March 2017.

The Special Committee investigated the allegations in the Demand Letter, and, as set forth in its report dated September 21, 2017 (the “Initial Report”), the Special Committee rejected the demand. The Special Committee found that the Company did not have viable federal or state law insider trading claims against Paul Amos. In addition, the Special Committee determined that the Company did not have a viable breach of fiduciary duty claim against Paul Amos relating to his alleged participation in the purported Average Weekly Producer (“AWP”) metric manipulation. Finally, the Special Committee determined, through the

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<sup>1</sup> Mr. Joffe made the demand on behalf of Martin Conroy, Gerard McCarthy, Louis Varela, and Julio Leaty.

exercise of its independent business judgment, that, even if such claims had any factual merit, it was not in the Company's best interests to bring the demanded action against Paul Amos.

On September 21, 2017, counsel for the Company, Mary Gill of Alston & Bird ("A&B"), informed Mr. Joffe of the Special Committee's determination. [Appendix ("App.") 1, September 21, 2017 Letter from Mary Gill].

Subsequently, on October 30, 2017, Mr. Joffe sent the Company a draft derivative complaint. [App. 2, Draft Derivative Complaint dated October 25, 2017]. The draft complaint not only included the allegations in the Demand Letter, but also introduced new allegations and claims exceeding the scope of the Demand Letter and seeking relief from Paul Amos and others. In a letter dated November 10, 2017, A&B advised Mr. Joffe that the draft complaint "constitutes a new demand, under Section 14-2-831 of the Georgia Code," and "[a]ccordingly, pursuant [to] Georgia law, the Special Litigation Committee will consider and determine within 90 days of receipt of your October 30, 2017 letter whether the prosecution of the new claims asserted in the Draft Derivative Complaint is in the best interests of the Company and its shareholders." [App. 3, November 10, 2017 Letter from Mary Gill to Dimitry Joffe].

Prior to the expiration of that 90 day period and before the Special Committee completed its investigation of this new, second demand, Mr. Joffe filed a derivative complaint in the United States District Court for the Southern District of New York (the "Complaint") that closely tracked the draft derivative complaint sent on October 30, 2017. [App. 4, Complaint dated December 14, 2017]. Plaintiffs filed this Complaint a month before the expiration of the 90-day period set forth in O.C.G.A. § 14-2-831.<sup>2</sup>

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<sup>2</sup> On February 2, 2018, Plaintiffs filed an amended complaint, which adds additional claims and defendants. A&B has informed Plaintiffs that the Special Committee considers these new

In the filed Complaint, plaintiffs, Martin Conroy, Gerard McCarthy, and Louis Varela (the “Plaintiffs”), allege they are shareholders. The Complaint names seven individual defendants (collectively, the “Defendants”), two of whom are current or former officers and directors – Dan Amos and Paul Amos – and five of whom are independent directors (collectively, the “Director Defendants”) – Douglas W. Johnson, Charles B. Knapp, Barbara K. Rimer, Elizabeth J. Hudson, and W. Paul Bowers.

The new claims in the Complaint allege that certain operational concerns raised by seven former and current associates – all independent contractors of the Company – give rise to claims for violations of federal securities law, breach of fiduciary duties, and unjust enrichment. [App. 4, Complaint].

Fairly read, Plaintiffs’ allegations of wrongdoing at the Company include seven alleged fraudulent practices. First, as discussed above and in the Initial Report, Plaintiffs allege that the Company fraudulently manipulates the AWP metric. Second, the Company allegedly relies on fraudulent tactics to recruit new sales associates. Third, certain sales associates allegedly enrolled non-sergeants as insureds under an Aflac<sup>3</sup> account for members of the Sergeants Benevolent Association (“SBA”), a union representing sergeants in the New York City police department. Fourth, the Company allegedly “converted” some individual policies to group policies, which, in turn, allegedly harmed certain associates who had sold the individual policies.

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(continued...)

allegations to constitute a third demand, and will respond in the 90-day period set forth under Georgia law.

<sup>3</sup> Plaintiffs’ references to “Aflac” lack specificity because they use the term interchangeably to refer to the Company and to its subsidiaries, American Family Life Assurance Company of Columbus, American Family Life Assurance Company of New York, and Continental American Insurance Company. For purposes of the report, the Special Committee interprets the references to “Aflac” to mean any of these entities.

Fifth, certain sales associates allegedly secured electronic policy applications for Aflac insurance through the improper use of the SmartApp Next Generation (“SNG”) platform and the Everwell system. Sixth, certain sales associates purportedly misled applicants by representing that certain insurance products must be purchased together (*i.e.*, in a bundle), although, in fact, they could have been purchased separately. Seventh, the Company allegedly extended financial periods to record revenue received after the close of those periods.

After completing the current investigation, the Special Committee finds no evidence to support the allegations that several of these practices occurred. In those instances where the investigation revealed the alleged practice had occurred, such instances were episodic, provided no evidence of any systemic wrongdoing, and are already subject to the Company’s remediation procedures. Based on this finding alone, the Special Committee could reject the demand.

Nevertheless, the Special Committee reviewed the Complaint to determine if any of the claims could or should be pursued notwithstanding these factual deficiencies. Based on that review, the Special Committee finds that Plaintiffs’ allegations are missing the necessary link between these alleged wrongful practices and any claim *by the Company against these Defendants*. The absence of such a link is fatal to Plaintiffs’ derivative claims.

Plaintiffs attempt to establish the required link by asserting the activities of certain sales associates went unchecked by Defendants despite warnings by Mr. Joffe and his clients. Stripped of hyperbole, however, the Special Committee finds that Plaintiffs fail to establish the required link. First, Plaintiffs fail to show any actual harm to the Company. Neither the Demand Letter nor the Complaint points to any facts (as opposed to conclusions or suppositions) that show that the alleged wrongful practices led to errors in the Company’s financial statements or that the Company has failed to comply with Generally Accepted Accounting Principles

(“GAAP”). Moreover, Plaintiffs fail to show how the named Defendants were responsible for or profited from the alleged wrongful conduct. In addition to this critical factual deficiency, each of Plaintiffs’ enumerated claims appears legally wanting under applicable law.

The Complaint includes five purported causes of action. First, Plaintiffs assert that all Defendants violated Section 10(b) of the Exchange Act and Rule 10b-5 promulgated thereunder. [App. 4, Complaint, at ¶¶ 104–16]. Second, Plaintiffs’ alleged that all Defendants violated Section 14(a) of the Exchange Act and Rule 14a-9 promulgated thereunder. [*Id.* at ¶¶ 117–25]. Third, Plaintiffs allege that all Defendants breached their fiduciary duties. [*Id.* at ¶¶ 126–33]. Fourth, Plaintiffs assert a claim under Section 20A of the Exchange Act against Paul Amos. [*Id.* at ¶¶ 134–47]. Fifth, Plaintiffs allege a claim for unjust enrichment against Paul Amos. [*Id.* at ¶¶ 148–51]. The two claims asserted against only Paul Amos relate to the allegedly improper stock trades raised in the Demand Letter that the Special Committee investigated and evaluated as discussed in its Initial Report.

First, in regard to the Section 10(b) claim,<sup>4</sup> Plaintiffs allege (1) they made the Company and many directors aware of their allegations; (2) the directors were aware of the investigation into these allegations; (3) the allegations are credible because the Company allegedly adopted several remedial measures designed to address the improper practices; (4) the Company improperly failed to disclose these allegations in their 2016 annual report and 2017 proxy statement; (5) the failure to disclose this adverse information improperly caused inflation in the Company’s stock price above its true value; (6) even though the stock price was inflated, the Defendants caused or authorized the repurchase of Company stock during the summer of 2017; and (7) the repurchase of that inflated stock harmed the Company.

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<sup>4</sup> See *supra*, p. 66.

The Special Committee finds that the Company's pursuit of these claims against Defendants would likely be unsuccessful for numerous reasons. First, there was no duty to disclose the unsubstantiated allegations. Second, the alleged misconduct is likely immaterial given it refers to narrow segments of the Company's operations. Third, the Plaintiffs' challenges to statements in the Company's 2017 proxy statement, such as those attesting to the directors' professional and ethical conduct, fail because the statements are mere statements of opinion. Fourth, Plaintiffs have not pointed to any facts in their letters or pleadings showing that any of the Defendants acted with scienter. Consistent with Plaintiffs' omission of specific facts showing scienter, the Special Committee has seen no evidence that any Defendant believed the challenged statements were untrue when they were made. In fact, each Defendant stated their belief that Plaintiffs' claims had been investigated and found to be immaterial. Finally, Plaintiffs cannot show loss causation or any economic loss suffered by the Company because there was no corrective disclosure and resulting economic loss.

Second, the Special Committee finds that Plaintiffs' Section 14(a) claim<sup>5</sup> faces similar arduous obstacles. Plaintiffs' Section 14(a) claim relies on the same allegations as the Section 10(b) claim and argues that the Company fraudulently represented that the Board of Director candidates had integrity and were qualified to serve as directors. Plaintiffs allege that the failure of the candidates to act on the alleged improper conduct identified by Plaintiffs in their letters confirms their lack of integrity and qualifications to serve as a director. Finally, Plaintiffs allege the Company was harmed by the election of these directors.

In order to establish a Section 14(a) violation, Plaintiffs must show first that the proxy statement contained a material misrepresentation or omission. They cannot. To that end,

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<sup>5</sup> See *supra*, pg. 86.

Plaintiffs allege the Defendants failed to disclose Plaintiffs' allegations, but there was no legal duty to do so, therefore, there was no material omission. Plaintiffs must also allege harm linked to the solicitation itself, not to an alleged defect in the supporting materials. None of the alleged misconduct alleged by Plaintiffs required shareholder approval, and, as a result, this link has neither been alleged nor shown. Finally, Plaintiffs have not shown how the Company was harmed by the election of the Defendants as Directors, which is fatal to their claim.

Third, the Special Committee finds there is not a viable breach of fiduciary duty claim.<sup>6</sup> Plaintiffs allege simply that Dan Amos and Paul Amos had direct knowledge of the alleged wrongdoing, and that the Director Defendants were reckless in failing to monitor the Company's response and failing to disclose the allegations to the public. These actions, Plaintiffs claim, amount to a breach of the Defendants' fiduciary duties. But the Special Committee finds that the Defendants had the right to rely on the investigation performed by the Company. To the extent Plaintiffs claim the Defendants did not insist on additional investigation or remediation, such a claim would, at most, constitute a breach of the duty of care, entitling the Director Defendants to the protections of the business judgment rule and exculpation provisions in the Company's Articles of Incorporation. Moreover, because there is no evidence of any personal gain by any of the Defendants other than receipt of usual director compensation, there is no basis for a breach of a duty of loyalty claim. Finally, the investigation revealed no so-called "red flags" that would give rise to liability under a *Caremark* claim (assuming such a claim is viable under Georgia law).

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<sup>6</sup> See *supra*, at 93.

Fourth and fifth, the Special Committee finds, for the reasons set forth in the Initial Report, the Section 20A claim<sup>7</sup> and the unjust enrichment claim<sup>8</sup> against Paul Amos to be without merit.

As a result of its investigation, the Special Committee finds that the claims in the Complaint are factually and legally unconvincing and face numerous procedural and substantive obstacles and defenses. Therefore, any recovery by the Company likely is remote, at best. Plaintiffs have not demonstrated that there has been any economic loss or harm to the Company as a result of the alleged practices. Thus, even if the claims could survive a motion to dismiss, any potential damages appear to be *de minimis*, if not nonexistent. Accordingly, the Special Committee finds that the costs of pursuing the claims would easily and significantly outweigh any supposed benefits. As such, the Special Committee has determined that it is not in the best interests of the Company to pursue the claims.

In sum, the Special Committee's determination is to reject the second demand.

## **II. BACKGROUND**

### **A. The Company, Its Board Of Directors, And The Defendants**

The Company is a Georgia corporation headquartered in Columbus, Georgia, with net earnings in 2016 of approximately \$2.7 billion. Its stock is traded on the New York Stock Exchange ("NYSE") with a current market capitalization in excess of \$35 billion. [App. 5, Investor Relations Stock Information Chart, <http://investors.aflac.com/stock-information/interactive-chart.aspx> (last accessed Jan. 29, 2018)].

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<sup>7</sup> *See supra*, at 93.

<sup>8</sup> *See supra*, at 102.

The Company's principal business involves voluntary insurance products. In the United States, the Company offers both individual and group insurance. "Most of [the Company's] policies are individually underwritten and marketed through independent agents." [App. 64, Excerpts from 2016 Form 10-K, at 1]. In addition, in the United States, the Company offers group products through its subsidiary, Continental American Insurance Company, which is branded as Aflac Group Insurance. [*Id.*]. The Company's focus is on marketing its insurance products at the worksite. [*Id.* at 6].

Currently, the Company's Board is composed of thirteen directors: twelve independent, outside directors<sup>9</sup> and one Company officer, Dan Amos. Not all directors are named as Defendants. The Defendants are as follows:

**1. Daniel P. Amos**

Dan Amos has been Chief Executive Officer of the Company and its wholly-owned subsidiary, American Family Life Assurance Company of Columbus, since 1990 and has been Chairman since 2001. Mr. Amos has spent 37 years in various positions at the Company. [See App. 6, 2017 Proxy Statement, at 9].

**2. Paul S. Amos, II**

In 2007, Paul Amos became the President of American Family Life Assurance Company of Columbus, and joined the Board of Directors of the Company. [See App. 6, 2017 Proxy

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<sup>9</sup> The outside directors are: W. Paul Bowers, Toshihiko Fukuzawa, Elizabeth J. Hudson, Douglas W. Johnson, Karole F. Lloyd, Robert B. Johnson, Thomas J. Kenny, Charles B. Knapp, Joseph L. Moskowitz, Barbara K. Rimer, Katherine T. Rohrer, and Melvin T. Stith. With the exception of Thomas J. Kenny, due to fees paid for his previous role as a consultant to the Board, the Board has determined that all are "independent" under the NYSE's listing requirements. [App. 6, 2017 Proxy Statement; App. 7, Aflac's Board of Directors, available at, <http://investors.aflac.com/corporate-governance/board-of-directors.aspx> (last accessed Jan. 24, 2018)].

Statement, at 9]. Paul Amos retained the title of President of American Family Life Assurance Company of Columbus from 2007 until 2017, although his responsibilities changed in 2014 when he moved to Japan to focus on the Company's Japanese operations, which comprises approximately 70 percent of the Company's revenue. [See *id.*; see App. 8, Excerpts of Second Quarter 2017 Form 10-Q, at 9]. Paul Amos resigned as President of American Family Life Assurance Company of Columbus and as a member of the Company's Board of Directors effective July 1, 2017. [App. 9, June 6, 2017 Form 8-K, at 3]. He has since joined a Columbus-based private investment firm, now known as JBA Capital.

**3. Douglas W. Johnson**

Mr. Johnson has served as an independent director of the Company since 2003, and is currently the Lead Non-Management Director and the Chair of the Audit and Risk Committee. Mr. Johnson is a Certified Public Accountant and a retired Ernst & Young LLP audit partner. He began auditing insurance companies in 1972 and spent the majority of his career focusing on companies in that industry. His work experience includes extensive coordination with the audit committees of publicly held companies. [See App. 6, 2017 Proxy Statement, at 8-15, 26].

**4. W. Paul Bowers**

Mr. Bowers is Chairman, President, and Chief Executive Officer of Georgia Power Company, the largest subsidiary of Southern Company. Mr. Bowers has been a director of the Company since 2013, and is a member of the Audit and Risk Committee, the Sustainability Committee, and the Chair of the Corporate Development Committee. [*Id.* at 24].

**5. Barbara K. Rimer**

Dr. Rimer is the Dean of the University of North Carolina Gillings School of Global Public Health. Dr. Rimer has been a member of the Company's Board of Directors since 1995.

She currently serves on the Executive and Sustainability Committees, and is Chair of the Corporate Governance Committee. [*Id.* at 15].

**6. Charles B. Knapp**

Dr. Knapp is the President Emeritus of the University of Georgia. Dr. Knapp was the interim director of the Terry College of Business at the University of Georgia from 2013 to 2014. He has been a member of the Company's Board of Directors since 1990. Currently, Dr. Knapp serves on the Audit and Risk and Corporate Development Committees and as Chair of the Finance and Investment Committee. [*Id.* at 13].

**7. Elizabeth J. Hudson**

Ms. Hudson was the Chief Communications Officer for the National Geographic Society from 2014 to 2015. Ms. Hudson has been a director of the Company since 1990, and currently serves on the Finance and Investment and Corporate Development Committees and as Chair of the Sustainability Committee.

At the Company's May 1, 2017 Annual Meeting of Shareholders, each of the Defendants were re-elected to the Board of Directors. [*Id.* at 11; App. 38, May 4, 2017 Form 8-K, at 2].

**B. Aflac Trust And The Company's Anti-Fraud Policies**

The Company's anti-fraud efforts are led by a department within the Company called Aflac Trust. Aflac Trust's mission is to deter, prevent, detect, and respond to potential fraud and abuse. [App. 16, 2012 Corporate Citizenship Report, at 1]. Aflac Trust furthers this mission by setting standards aligned with regulatory requirements, educating employees through fraud awareness programs, implementing analytical tools to identify trends and patterns, employing effective product, process, and system controls, investigating and settling fraud referrals efficiently and effectively, pursuing violators, and communicating and reporting to appropriate internal and external entities. [*Id.* at 23].

Within Aflac Trust is the Special Investigations Unit (“SIU”). SIU is a team “providing a wide array of compliance-related investigative services for management. The unit investigates the allegations of fraud or inappropriate activities from both internal and external sources, and has programs to actively look for evidence of fraud or inappropriate activity.” [App. 61, Aflac Trust 2018: Understanding Insurance Fraud and Prohibited Practices, at 8]. The unit also “coordinates with the various departments of insurance and law enforcement when fraud is confirmed.” [*Id.*].

In addition, the Company has a fraud hotline, website, and fax number to report any perceived violations anonymously. [App. 62, Code of Conduct]. The Company also has a Field Oversight Enforcement Committee, previously called the Agent Activity Review Committee, to address allegations and remediation, among other things.

Aflac Trust creates training materials for associates selling Aflac insurance. One such example states: “Aflac takes a strong stand against insurance fraud. If we find sufficient evidence to confirm that a person has committed insurance fraud or other prohibited practices, Aflac will take appropriate action, up to and including termination of your contract and/or prosecution.” [App. 61 at 2]. The training materials list numerous examples of “prohibited practices,” including many of the practices alleged by Plaintiffs. [*Id.*].

### **C. The Alleged Material, Nonpublic Information**

As discussed in the Special Committee’s Initial Report, the June 23, 2017 Demand Letter requested the Company take action against Paul Amos for allegedly selling Company shares while purportedly in possession of material, nonpublic Company information. [App. 11, June 23, 2017 Demand Letter]. That alleged information included knowledge of “massive fraud at Aflac” (and the Company’s investigation regarding such allegations) that Mr. Joffe and his co-counsel,

Andrew St. Laurent, previously described in a series of letters sent to the Company, certain of its Board members, and others in December 2016 and March 2017.

Mr. Joffe directed the first letter, dated December 10, 2016 (the “December 2016 Letter”), to Dan Amos, Audrey Tillman (the Company’s General Counsel), and Paul Amos. In the December 2016 Letter, Messrs. Joffe and St. Laurent, on behalf of seven current and former sales associates,<sup>10</sup> described alleged wrongdoing at the Company falling into four general categories: fraudulent recruiting, manipulation of the AWP metric, fraudulent underwriting, and potential earnings manipulation.<sup>11</sup>

In sum, Plaintiffs allege that (1) the practices used to recruit new associates are a “sham” because they set unrealistic earnings expectations (*i.e.*, the “Fraudulent Recruiting Allegations”) [App. 10, December 2016 Letter, at 4]; (2) the Company touts a metric to financial analysts and others called the average weekly producer metric – AWP – that is susceptible to and has been manipulated by falsely assigning one dollar of credit to non-producing associates (*i.e.*, the “AWP Manipulation Allegations”) [*Id.* at 7]; (3) the Company has engaged in “a number of unfair, deceptive and illicit underwriting practices that inflate its other key operational metrics, such as the ‘number of policies in force,’ the ‘annualized premiums in force,’ and the ‘total new annualized premium’” (*i.e.*, the “Fraudulent Underwriting Allegations”) [*Id.* at 8]; and (4) the Company engaged in potential earnings manipulation by holding open reporting periods “past

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<sup>10</sup> As a note, the Company classifies sales associates as independent contractors, not employees. [See, e.g., App. 12, Martin Conroy’s Associate’s Agreement, at 1].

<sup>11</sup> As stated in the December 2016 Letter, Mr. Joffe’s clients include Martin Conroy, Gerard McCarthy, Louis Varela, Debbie Cort, Anibal Alcantara, Jr., Frederick Baker, and Julio Leaty. [App. 10, December 2016 Letter]. Only four of these clients were mentioned in the Demand Letter, presumably because the others are not also shareholders of the Company. [App. 11, June 23, 2017 Demand Letter]. And only three of those clients are listed as Plaintiffs in the Complaint. [App. 4, Complaint].

their calendar close date and improperly booking production revenues from business received in that extra time period.” (*i.e.*, the “Potential Earnings Manipulation Allegations”) [*Id.* at 13].

The Fraudulent Underwriting Allegations encompass several allegations: the purported wrongful enrollment of police officers who do not have the rank of sergeant under the SBA account; the inappropriate use of the SNG enrollment platform and the Company’s new Everwell platform; alleged wrongful bundling of policies; and alleged improper transfer of individual policies to group policies. [*Id.* at 8-12].

In addition, Mr. Joffe challenges the use of situation codes or “sit codes” by regional coordinators to split or reassign commissions. [*Id.* at 12-13]. Also, Mr. Joffe asserts that the Company retaliated against purported whistleblowers bringing these allegations to the Company’s attention (*i.e.*, the “Whistleblower Allegations”). [*Id.* at 14].

The December 2016 Letter fails to allege that Dan Amos or Paul Amos participated in any fraudulent activities. Rather, the letter asserts only that some of Mr. Joffe’s clients had informed them of certain of the alleged “schemes.” The Director Defendants are not mentioned in the December 2016 Letter.

The December 2016 Letter also does not state that Mr. Joffe’s clients, on whose behalf he sent the letter, were Company shareholders or that they sought any derivative relief on behalf of the Company. Instead, the letter requested only that the Company (i) redress the alleged harm to Mr. Joffe’s clients – ***not the Company*** – and (ii) waive an arbitration provision included in Mr. Joffe’s clients’ respective sales associate’s agreements. [*Id.* at 14-16].

Following receipt of the December 2016 Letter, the Company conducted an internal investigation. On January 5, 2017, Catherine Coppedge, a lawyer for the Company, responded that “Aflac unequivocally denies the allegations raised in your December 10, 2016 letter[.]”

[App. 13, January 5, 2017 Letter to Joffe]. She further stated, “[y]our clients’ claims are wholly without merit,” and invoked the arbitration provision in Mr. Joffe’s clients’ associate’s agreements, stating that “Aflac is ready and willing to arbitrate your clients’ disputes[.]” Thus far, neither Mr. Joffe nor Mr. St. Laurent has pursued arbitration on behalf of any of their clients. Additionally, according to Ms. Tillman, her report to the Audit Committee and the Board in executive session was consistent with what Ms. Coppedge told Mr. Joffe.

In March 2017, Mr. Joffe sent letters to Doug Johnson, Chair of the Audit and Risk Committee, as well as several other directors, attaching a series of documents, including (i) a letter that Mr. Joffe previously sent to the Securities and Exchange Commission (“SEC”), dated December 21, 2016; (ii) a complaint filed with the Occupational Safety and Health Administration, dated February 8, 2017; (iii) an Internal Revenue Service (“IRS”) Whistleblower submission, dated February 23, 2017; and (iv) a Supplemental SEC submission, dated March 6, 2017 (together, the “March 2017 Letter”).<sup>12</sup> [See, e.g., App. 14, March 8, 2017 Letter to Doug Johnson].

The March 2017 Letter not only includes many of the same allegations set forth above, but also asserts that the Company failed to withhold employment taxes for associates, maintained an undisclosed slush fund, and violated Section 125 of the Internal Revenue Code (*i.e.*, the “Tax-Related Allegations”). [*Id.*]. Notably, the March 2017 Letter includes no new allegations about Dan Amos and Paul Amos and does not mention any involvement by the Director Defendants. Mr. Joffe also points to what he describes as “remedial measures” by the Company in response to the December 2016 Letter, including his claim that the Company has now “decommissioned”

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<sup>12</sup> Mr. Joffe appears to have sent the same letter, dated March 16, 2017, to each of the following directors: Barbara K. Rimer, Charles B. Knapp, Elizabeth J. Hudson, Melvin T. Stith, W. Paul Bowers, and Joseph L. Moskowitz.

the AWP metric and removed a recruiting video from the Company's website. [*Id.*; App. 15, March 28, 2017 Letter to Johnson]. Mr. Joffe and Plaintiffs contend that these measures are evidence that the Company concluded the allegations in the December 2016 Letter had merit.

Mr. Johnson responded to Mr. Joffe on March 20, 2017, stating that the "Board had previously been advised of the allegations raised in your December letter and of the [C]ompany's due diligence efforts." [App. 33, March 20, 2017 Letter from Johnson to Joffe]. On March 28, 2017, Mr. Joffe sent a response to Mr. Johnson stating that Mr. Joffe believed that the Board of Directors had not been "sufficiently and truthfully apprised of our allegations and of the Company's true financial position by the management." [App. 15, March 28, 2017 Letter to Johnson]. This response, however, does not specifically point to any of his allegations that were concealed from the directors or identify the Company's "true financial position" or how that position differed from that set forth in the Company's publicly-available financial statements. In that letter, Mr. Joffe closed by asking Mr. Johnson and the other non-management members of the Board to "remove the current executive management[.]" [*Id.*].

Prior to receipt of the June 23, 2017 Demand Letter, the Company, through in-house counsel, the internal audit department, Aflac Trust, and outside counsel (A&B) investigated the factual assertions raised by Mr. Joffe.

As noted above, following receipt of the Demand Letter, on July 12, 2017, the Board of Directors created the Special Committee, who retained independent counsel, Jones Day. The Special Committee investigated and determined to reject the demand. During that investigation, Mr. Joffe confirmed with counsel for the Special Committee that the Demand Letter was the only derivative demand made on behalf of his clients. The Demand Letter only requested relief based on Paul Amos's alleged insider trading. [*See* App. 17, Initial Report, at 12-13]. Despite the

limited scope of the Demand Letter, Mr. Joffe filed the Complaint on December 14, 2017, which contains allegations extraneous to the Demand Letter and asserts claims against six additional Defendants who were not the subject of the Demand Letter.

#### **D. The Allegations Of The Complaint**

Plaintiffs allege that each Defendant had actual knowledge of the fraud alleged in the December 2016 and March 2017 Letters, but deliberately concealed this information by failing to reference the allegations and the Company's investigation thereof in the Company's "2017 proxy statement published on March 17, 2017 (the "2017 Proxy"), and its Annual Report on Form 10-K for FY2016, and the Year in Review Report, published on February 24, 2017 (collectively, the "2016 Annual Report")["."] [App. 4, Complaint, at ¶ 2a]. Plaintiffs further allege that each Defendant knew that certain "remedial actions" taken by the Company to address the alleged misconduct were designed to "cover up" the misconduct. [*Id.* at ¶ 2b]. According to Plaintiffs, each Defendant, in turn, caused the publication of the 2017 Proxy and 2016 Annual Report, which allegedly omitted material information. [*Id.* at ¶ 2c]. Additionally, Plaintiffs claim the Director Defendants improperly relied on A&B to conduct the investigation because A&B has a conflict given its long-standing representation of the Company.<sup>13</sup> [*Id.* at ¶ 2d]. The Director Defendants also (allegedly) unreasonably and recklessly recommended the re-election of Dan Amos and Paul Amos despite Plaintiffs' allegations "tying" them to the purported "schemes." [*Id.* at ¶ 2e]. These same Director Defendants then (purportedly) improperly rejected the demand

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<sup>13</sup> An investigation conducted by a company's outside counsel is common and appropriate under many circumstances. *See, e.g.,* Defending Corp. & Indiv. in Gov. Invest. § 3:13 ("In many cases, outside counsel with experience representing the company will be the best choice to conduct an investigation because she is already seen as a trusted advisor by management and is familiar with the company and its key employees.").

in the Demand Letter to investigate and prosecute Paul Amos for alleged insider trading.<sup>14</sup> [*Id.* at ¶ 2f]. The Defendants also allegedly failed to correct the deficient controls that allowed the misconduct to occur. [*Id.* at ¶ 3]. All of the claims are asserted derivatively under Rule 23.1 of the Federal Rules of Civil Procedure.<sup>15</sup>

### **III. THE SPECIAL COMMITTEE’S FORMATION, COMPOSITION, AND INDEPENDENCE**

#### **A. The Special Committee Is Authorized To Investigate, Evaluate, And Determine Whether To Prosecute The Demanded Action.**

Upon receiving the June 23, 2017 Demand Letter, the Board determined that the allegations raised in the Demand Letter should be investigated to determine if they had merit, and, if they did, if the best interests of the Company be served by seeking the relief demanded. On July 12, 2017, the Board voted in favor of creating a special committee comprised of three independent directors for the purpose of investigating the “potential claims (the “Potential Claims”) the Company may have against Mr. Paul Amos, II, in connection with [his] June 12, 2017 sale of Company shares while in possession of alleged material, nonpublic Company information regarding claims asserted in a December 10, 2016 Letter from Joffe Law P.C.” [App. 18, July 12, 2017 Board Resolution].

The Board authorized the Special Committee to “investigate, review, and analyze the facts, allegations, and circumstances that are the subject of the Potential Claims [against Paul

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<sup>14</sup> While Plaintiffs allege that the “very same Director Defendants then rejected the Plaintiffs’ demand to investigate and prosecute Defendant Amos II,” it is worth noting that the decision to reject the demand rested with the Special Committee alone, a decision that was not subject to review by the full Board of Directors.

<sup>15</sup> As discussed above, the December 2016 and March 2017 Letters describe several categories of alleged misconduct, but the Complaint includes specific allegations relating only to the AWP Manipulation Allegations, the Fraudulent Recruiting Allegations, and the Fraudulent Underwriting Allegations, while referencing the December 2016 and March 2017 Letters for the details of the remaining areas of alleged wrongdoing. [*See* App. 4, Complaint, at ¶ 42].

Amos] as well as any additional facts, allegations, and circumstances that may be at issue in any related inquiry, investigation, or proceeding[.]” [*Id.*]. The Board granted the Special Committee broad powers regarding its resources and authority, which include:

the full and exclusive authority to consider and determine whether or not the prosecution of the Potential Claims or any other claims related to the facts, allegations and circumstances of the Potential Claims is in the best interests of the Company and its shareholders, and what action the Company should take with respect to the Potential Claims and any related inquiry, investigation or proceeding[.]

[*Id.*]. The Special Committee’s determinations are final, binding, and not subject to review by the Board. [*Id.*].

To facilitate the Special Committee’s exercise of its duties and powers, the Board authorized the Special Committee to incur expenses on the Company’s behalf in connection with its activities, and to engage and retain such experts and advisors, including counsel and other advisors, as the Special Committee shall deem necessary or appropriate in order to assist it in the discharge of its responsibilities. [*Id.*]. The Board further authorized and directed the Company’s directors, officers, employees, public accountants, and advisors to assist the Special Committee, and to provide it with any and all documents and other information that the Special Committee deems necessary to carry out its duties. [*Id.*].

Following receipt of the draft derivative complaint, the Special Committee reviewed whether the resolution creating the Special Committee authorized it to investigate the claims in the draft complaint and (later) the as-filed Complaint. [*Id.*]. The Special Committee determined that it had the authority because the resolution takes into account the possibility of a continued investigation and authorizes the Special Committee to “investigate, review and analyze the facts, allegations and circumstances that are the subject of the Potential Claims, as well as *any*

*additional facts, allegations and circumstances* that may be at issue *in any related inquiry, investigation or proceeding[.]*” [*Id.* (emphasis added)].

**B. The Special Committee Members Are Independent And Disinterested.**

The Special Committee is comprised of W. Paul Bowers, Joseph L. Moskowitz, and Melvin T. Stith. [See App. 17, Initial Report, at 15-17 for detailed description of each of the committee members]. All members of the Special Committee qualify as independent directors under the NYSE’s listing requirements. [App. 19, NYSE Listed Company Manual, Independence Test, Section 303A.02].

The Special Committee has evaluated the independence of its members under the standards established by the Georgia Business Corporations Code, O.C.G.A. § 14-2-101 *et seq.*, and the Georgia courts.

Georgia law recognizes that a corporation’s board of directors may assert control over derivative claims that a shareholder of the corporation seeks to assert on the corporation’s behalf. O.C.G.A. §§ 14-2-742, 14-2-744. In this regard, a board may delegate its authority to a special committee of two or more independent directors. O.C.G.A. § 14-2-744; *Benfield v. Wells*, 324 Ga. App. 85, 88 (2013). A duly appointed special committee may exercise the full powers of the board to the extent the resolution delegating those powers so provides.

In evaluating a special litigation committee’s exercise of its authority to assert control over derivative claims (*i.e.*, when a corporation moves to dismiss a derivative proceeding filed by a shareholder of the corporation on the basis of a special litigation committee’s determination), the court must examine (a) the independence and (b) the disinterestedness of the special litigation committee’s members. See O.C.G.A. § 14-2-744 cmt. (“The decisions that have examined the qualifications of members of special litigation committees have required that they be both ‘disinterested’ in the sense of not having a personal interest in the transaction . . . and

‘independent’ in the sense of not being influenced in favor of the defendants by reason of personal or other relationships.”) (citing *Aronson v. Lewis*, 473 A.2d 805, 812–16 (Del. 1984), *overruled on other grounds*, *Brehm v. Eisner*, 746 A.2d 244, 253 (Del. 2000)).

O.C.G.A. § 14-2-744(c) provides that a director does not lack independence simply because he or she (i) was nominated or elected by directors who are not independent; (ii) was named in a derivative proceeding; or (iii) approved the act being challenged, provided the director did not receive a personal benefit as a result of the action. Courts have considered whether the special litigation committee members possess a personal interest in the underlying transactions involved in the claim, and whether any personal or other relationship between the committee member and the alleged wrongdoer renders the director to be not independent. *See Millsap v. Am. Family Corp.*, 208 Ga. App. 230, 232 (1993); *Benfield*, 324 Ga. App. at 89.

“An SLC member is independent ‘when he is in a position to base his decision on the merits of the issue rather than being governed by extraneous considerations of [sic] influences.’” *Clifford v. Ghadrnan*, No. 1:12-cv-3683-SCJ, 2014 WL 11829337, at \*2 (N.D. Ga. Mar. 5, 2014) (quoting *Kaplan v. Wyatt*, 499 A.2d 1184, 1189 (Del. 1985)). While a “substantial likelihood of personal liability” may cause a director to lack independence, the mere threat of personal liability is not enough. *See Clifford*, 2014 WL 11829337, at \*5 (quoting *In re Friedman’s, Inc. Derivative Litig.*, 386 F. Supp. 2d 1355, 1363 (N.D. Ga. 2005)).

In addition, generally speaking, allegations of a mere personal friendship or an outside business relationship, without more, will not suffice to raise a reasonable doubt about a special litigation committee’s independence. *See Benfield*, 324 Ga. App. at 89 (finding that tangential outside business relationships between special litigation committee members and defendants did not destroy the independence of the special litigation committee); *Clifford*, 2014 WL 11829337,

at \*5 (finding that occasional social interactions with the defendants do not, by themselves, raise an inference that the special litigation committee member lacks independence). The relationship generally must be such that the special litigation committee member feels that he or she “owes something” to the persons accused of wrongdoing, whether that obligation is financial or otherwise. *See London v. Tyrrell*, No. 3321-CC, 2010 WL 877528, at \*12 (Del. Ch. Mar. 11, 2010).

The Special Committee finds that each of its members is disinterested and independent under Georgia law.

The Special Committee members’ only business or financial relationships with the Company (or its subsidiaries, management or other directors) consist of their service as directors, as members of various Board committees, and ownership of Company stock and stock options. The law is clear, however, that mere stock ownership does not destroy a director’s independence. To the contrary, stock ownership confirms the alignment of the Committee members’ interests with those of the Company and its shareholders. *See Aronson*, 473 A.2d at 812 (distinguishing a personal benefit from a benefit “which devolves upon the corporation or all shareholders generally”).

Plaintiffs argue that the Special Committee is not independent because it is comprised of directors who previously declined to fire Dan Amos and Paul Amos as requested in Mr. Joffe’s March 28, 2017 letter. [App. 4, Complaint, at ¶ 101]. This argument is without merit under Georgia law. The fact that members of the Special Committee, as directors, previously declined to acquiesce to Mr. Joffe’s request does not destroy the Committee’s independence. O.C.G.A. § 14-2-744(c)(3) (“None of the following shall by itself cause a director to be considered not independent for purposes of subsection (b) of this Code section . . . (3) The fact that the director

approved the action being challenged in the derivative proceeding so long as the director did not receive a personal benefit as a result of the action.”).

The fact that one member of the Special Committee, Paul Bowers, is named as a Defendant in the Complaint similarly does not affect his independence as a matter of Georgia law. O.C.G.A. § 14-2-744(c)(2) (“None of the following shall by itself cause a director to be considered not independent for purposes of subsection (b) of this Code section: . . . (2) [t]he naming of the director as a defendant in the derivative proceeding.”). The mere threat of personal liability (as a result of being named as a defendant) does not destroy a director’s independence. *Clifford*, 2014 WL 11829337, at \*5 (holding a director independent where there was no showing that he would have faced a substantial likelihood of personal liability had the SLC determined the claims were meritorious); *In re Friedman’s*, 386 F. Supp. 2d at 1364 (claiming that defendants’ actions expose them to the potential liability is not enough to destroy independence because there is no “allegation in the Complaint . . . asserting, or even suggesting, a substantial likelihood that the Director Defendants are liable for any claim alleged.”). Here, even if the Special Committee were to find Plaintiffs’ claims meritorious, Mr. Bowers still does not face substantial personal liability. Any claim for monetary damages against Mr. Bowers for a breach of the duty of care would be indemnified under the Company’s Articles of Incorporation. [See App. 20, Amendment to the Articles of Incorporation, dated April 25, 1988 (“No director shall be personally liable to the corporation or its stockholders for monetary damages for any breach of duty of care or other duty as a director.”)]. And Plaintiffs do not allege any facts to support a breach of loyalty claims against Mr. Bowers.

Mr. Bowers, Mr. Moskowitz, and Dr. Stith do not possess any interest, financial or otherwise, in the alleged wrongdoing described in the December 2016 and March 2017 Letters.

*See In re Friedman's, Inc. Derivative Litig.*, 386 F. Supp. 2d 1355, 1361 (N.D. Ga. 2005) (“A director is considered interested where he or she will receive a personal financial benefit from a transaction that is not equally shared by the stockholders,” or “where a corporate decision will have a materially detrimental impact on a director, but not on the corporation and the stockholders.”) (quoting *Rales v. Blasband*, 634 A.2d 927, 936 (Del. 1993)); *Staehr v. Miller*, No. 08-20990-CIV, 2010 WL 11030716, at \*5 (S.D. Fla. Mar. 31, 2010) (“A director is considered ‘disinterested’ if ‘he or she lacks a financial stake in the transaction under consideration.’”) (citing *Maldonado v. Flynn*, 597 F.2d 789, 793 (2d Cir. 1979)). In addition, Mr. Bowers, Mr. Moskowitz, and Dr. Stith all lack any close social or personal relationships with Paul Amos, Dan Amos, or the Amos family that would affect their ability independently to assess and make decisions about what is best for the Company. *See Benfield*, 324 Ga. App. at 89.

Accordingly, the Special Committee members remain independent and disinterested.

### **C. The Special Committee Retained Independent Counsel.**

On or about July 24, 2017, pursuant to its power to retain independent legal counsel, the Special Committee retained Jones Day, an international law firm with broad-based experience in litigation matters, enforcement actions, and investigations involving public companies. The principal Jones Day attorneys involved in advising the Special Committee with respect to the investigation are Michael J. McConnell and Janine Cone Metcalf. Mr. McConnell has over 30 years of experience and Ms. Metcalf has over 25 years of experience representing public and private corporations, directors, officers, special committees, or other stakeholders in securities and corporate governance matters and internal investigations.

Jones Day does not represent the Company and is therefore independent of the Company and the Board with respect to the investigation. *See Clifford*, 2014 WL 11829337, at \*3 (finding that the special litigation committee appointment process was not flawed even though counsel

involved in the process represented the Board of Directors as well as one of the Defendants personally at the same time); *Johnson v. Hui*, 811 F. Supp. 479, 487 (N.D. Cal. 1991) (stating that “there is no evidence that the [special litigation committee attorneys] are biased or had any improper interest in the matter” because there is “no evidence that [the attorneys] have had any personal or business contacts with [those involved] other in its role as committee counsel.”).

#### **IV. THE SCOPE OF THE SPECIAL COMMITTEE’S INVESTIGATION**

##### **A. The Special Committee’s Investigation Included Extensive Document Review.**

The Special Committee and its counsel spent approximately two months investigating and evaluating the allegations in the Demand Letter, and approximately an additional three months investigating and evaluating the allegations in the second demand. The Committee met with its counsel multiple times, reviewed materials, and was briefed on the interviews with witnesses. Counsel for the Special Committee devoted over 1600 hours of work in assisting the Special Committee with its investigation regarding the Demand Letter and the Complaint.

The Company provided the Special Committee and its counsel with access to over 600,000 documents and e-mails from numerous sources. The Special Committee and its counsel reviewed the following categories of documents, among others:

1. The Company’s Amended and Restated Articles of Incorporation and Bylaws;
2. Internal corporate governance documents and ethics codes;
3. Minutes of relevant Board of Directors and Audit and Risk Committee meetings;
4. The Company’s records of Paul Amos’s stock transactions from August 2016 through June 2017, including correspondence regarding blackout notices and Paul Amos’s pre-clearance requests;
5. The Company’s Long-Term Incentive plan;

6. The Company's management compensation plans;
7. The Company's document retention policy;
8. Paul Amos's Stock Option Award Certificates, dated March 1, 2016 through July 1, 2017;
9. Paul Amos's 2015 Employment Agreement and 2017 Separation Agreement;
10. Correspondence to and from Messrs. Joffe and St. Laurent between December 10, 2016 and November 10, 2017;
11. The Company's relevant filings with the SEC, including proxy statements, Form 10-Ks, Forms 4 & 5 filings, and 8-Ks;
12. Financial Analysts' Briefing Books and Supplements;
13. Documents generated by Aflac Trust and the Company's internal audit department in connection with their relevant investigations;
14. Documents received by Aflac Trust relating to topics similar to Plaintiffs' allegations;
15. Company communications with Plaintiffs;
16. Documents collected by the Company and A&B during the course of the their investigations related to the claims in the Complaint;
17. E-mails collected from Paul Amos and Dan Amos;
18. An imaged copy of Paul Amos's MacBook computer;
19. The Complaint and relevant pleadings filed in the Southern District of New York;
20. The Company's Ethics, Fraud, and Prohibited Practices training materials;
21. Materials related to the Aflac Incentive Fund;
22. The Company's sales production calendars;
23. Prior decisions the Company has obtained relating to Plaintiffs' allegations;
24. Documents relating to relevant audits by the internal audit department;
25. Documents relating to the Plaintiffs; and

26. Documents relating to cafeteria plans.

**B. The Special Committee Interviewed Twenty-Four Witnesses**

Between August 2017 and January 2018, the Special Committee interviewed all witnesses that it deemed to be material to the investigation. The witnesses interviewed were as follows:

**1. W. Paul Bowers**

On August 23, 2017, the Special Committee's counsel conducted an interview of Paul Bowers. As an independent director and Audit and Risk Committee member, among other things, Mr. Bowers was personally familiar with the discussions among and decisions by the Audit and Risk Committee and the Board relating to the investigation of the allegations in the December 2016 and March 2017 Letters. Mr. Bowers is also personally familiar with the Demand Letter, the Complaint, and the Special Committee's formation and work.

**2. Melvin T. Stith**

On August 24, 2017, the Special Committee's counsel conducted an interview of Melvin Stith. As an independent director, among other things, Dr. Stith was personally familiar with the discussions during executive session of the Board regarding the investigation of and response to Mr. Joffe's December 2016 and March 2017 Letters. Dr. Stith is also personally familiar with the Demand Letter, the Complaint, and the Special Committee's formation and work.

**3. Joseph L. Moskowitz**

On August 24, 2017, the Special Committee's counsel conducted an interview of Joseph Moskowitz. As an independent director and member of the Audit and Risk Committee, among other things, Mr. Moskowitz was personally familiar with the discussions among and decisions by the Audit and Risk Committee and the Board relating to the investigation of the allegations in

the December 2016 and March 2017 Letters. Mr. Moskowitz is also personally familiar with the Demand Letter, the Complaint, and the Special Committee's formation and work.

**4. Douglas W. Johnson**

On September 6, 2017, the Special Committee's counsel conducted an interview of Doug Johnson. As an independent director and Audit Committee Chairman, among other things, Mr. Johnson was personally familiar with the discussions among and decisions by the Audit and Risk Committee and the Board relating to the investigation of the allegations in the December 2016 and March 2017 Letters. Mr. Johnson is also personally familiar with the Demand Letter and the Special Committee's formation.

**5. Barbara K. Rimer**

On January 9, 2018, the Special Committee's counsel conducted an interview of Barbara Rimer. As an independent director and member of the Board, Dr. Rimer was familiar with the allegations contained in Mr. Joffe's December 2016 and March 2017 Letters. Dr. Rimer was personally familiar with the discussions of the Board regarding the investigation of and responses to Mr. Joffe's December 2016 and March 2017 Letters. Dr. Rimer is also familiar with the Demand Letter, the Complaint, and the Special Committee's formation.

**6. Charles B. Knapp**

On January 10, 2018, the Special Committee's counsel conducted an interview of Charles Knapp. As an independent director and member of the Audit and Risk Committee, Dr. Knapp was familiar with the discussions among and decisions by the Audit and Risk Committee and the Board relating to the allegations in the December 2016 and March 2017 Letters. Dr. Knapp is also personally familiar with the Company's share repurchase program, the proxy editing process, the Demand Letter, the Complaint, and the Special Committee's formation.

**7. Elizabeth J. Hudson**

On January 10, 2018, the Special Committee's counsel conducted an interview of Elizabeth Hudson. As an independent director and member of the Board, Ms. Hudson was familiar with the investigation of and response to the allegations contained in Mr. Joffe's December 2016 and March 2017 Letters. Ms. Hudson is also personally familiar with the Demand Letter, the Complaint, and the Special Committee's formation.

**8. Daniel P. Amos**

On September 6, 2017, the Special Committee's counsel conducted an interview of Dan Amos. Dan Amos was a recipient of Mr. Joffe's December 2016 Letter and was given high-level briefings from time to time regarding the Company and A&B's investigation of the allegations in Mr. Joffe's December 2016 and March 2017 Letters.

**9. Paul S. Amos, II**

On September 14, 2017, the Special Committee's counsel conducted an interview of Paul Amos. Paul Amos was a recipient of the December 2016 Letter and is alleged to have sold Company stock with knowledge of material, nonpublic information, including an alleged scheme involving the AWP metric.

**10. Audrey Boone Tillman**

On August 30, 2017, the Special Committee's counsel conducted an interview of Audrey Tillman. Ms. Tillman is the Executive Vice President and General Counsel for the Company, where she directs the Legal division and oversees functions related to Human Resources, Corporate Communications, Compliance, Government Relations, Federal Relations, Global Cyber Security and the office of the Corporate Secretary. Ms. Tillman was a recipient of the

December 2016 Letter and reported to the Audit Committee and the Board of Directors in executive session regarding Mr. Joffe's allegations.

**11. Catherine Coppedge**

On September 1, 2017 and January 8, 2018, the Special Committee's counsel conducted interviews of Catherine Coppedge. Ms. Coppedge is in-house counsel and Assistant Corporate Secretary at the Company, and has a wide range of legal responsibilities, including responsibility for issues relating to the Company's associates. Ms. Coppedge is familiar with Mr. Joffe's December 2016 Letter, actions taken with regard to Plaintiffs, and was involved in responding to Mr. Joffe's allegations.

**12. Peter Sumners**

On September 1, 2017 and January 8, 2018, the Special Committee's counsel interviewed Peter Sumners. Mr. Sumners is in-house counsel at the Company where he handles securities, finance, and corporate governance issues. Mr. Sumners is familiar with Mr. Joffe's allegations, the Company's share repurchase programs, and has responsibilities relating to the Company's public disclosures.

**13. Kenneth Dowless**

On August 30, 2017 and January 8, 2018, the Special Committee's counsel conducted interviews of Ken Dowless. Mr. Dowless has been the Director of Aflac Trust since 2015. Prior to that, Mr. Dowless worked with SIU. Mr. Dowless participated in the Company's investigation of allegations in the December 2016 Letter.

**14. William Capps**

On January 8, 2018, the Special Committee's counsel conducted an interview of Bill Capps, who has served as an SIU investigator for the past twenty years. Mr. Capps participated in the Company's investigation of allegations regarding the SBA account.

**15. Joan Diblasi and Jacob Anderson**

On August 31, 2017, the Special Committee's counsel conducted an interview of Joan Diblasi and Jacob Anderson. Ms. Diblasi is the Director of Shareholder Services, and Mr. Anderson is a manager in the Stock Administration division of Shareholder Services. Both Ms. Diblasi and Mr. Anderson are familiar with federal regulations regarding trading by Section 16 officers and the Company's insider trading policies and procedures. Ms. Diblasi and Mr. Anderson also had knowledge of Paul Amos's pre-clearance to trade on June 12, 2017.

**16. Courtney Ruckert and Lamar Barnett**

On September 1, 2017 and January 8, 2018, the Special Committee's counsel conducted interviews of Courtney Ruckert and Lamar Barnett. Ms. Ruckert is the manager of Internal Control over Financial Reporting and Financial Audit at the Company. Mr. Barnett is Vice President of U.S. Internal Audit at the Company. Both Ms. Ruckert and Mr. Barnett had knowledge of, among other things, the Company's investigation of the allegations in the December 2016 Letter regarding the alleged manipulation of the AWP metric and the alleged potential earnings manipulation.

**17. Trevor Fennell**

On January 12, 2018, the Special Committee's counsel conducted an interview of Trevor Fennell. Mr. Fennell is the Market Director for Aflac's New York Metro/Long Island market. Mr. Fennell has held this role for a little over two years. Previously he was a District Sales Coordinator ("DSC") in New York, a Regional Sales Coordinator ("RSC") in New York, and a

Market Director in Chicago. Mr. Fennell knows one of the Plaintiffs, Mr. Conroy, personally, and has knowledge of Mr. Conroy's allegations stemming from his time in the New York Metro/Long Island market. Mr. Fennell was personally familiar with facts relevant to the subject matter of the allegations in the December 2016 Letter.

**18. Ken Meier**

On January 12, 2018, the Special Committee's counsel conducted an interview of Ken Meier. Mr. Meier is the Territory Vice President of Aflac's Northeast Territory. Mr. Meier has held this role for a little over two years. Previously he was the Market Director for the New York Metro/Long Island market. Mr. Meier has known Mr. Conroy personally for many years and has personal knowledge of facts relevant to the subject matter of Mr. Conroy's allegations stemming from his time in the New York Metro/Long Island market. Mr. Meier was familiar with details regarding the subject matter of the allegations in the December 2016 Letter.

**19. Benito Rotondi**

On January 12, 2018, the Special Committee's counsel conducted an interview of Ben Rotondi. Mr. Rotondi is the Senior Training Manager for the Northeast Territory. He has held this position since September 2015. Previously he has served as a DSC, an RSC, and a State Training Coordinator for New York Metro/Long Island. Plaintiffs identify Mr. Rotondi in connection with the AWP Manipulation Allegations and the Fraudulent Recruiting Allegations described in the December 2016 Letter.

**20. Richard Peterson**

On January 17, 2018, the Special Committee's counsel conducted an interview of Rick Peterson. Mr. Peterson has worked as an Aflac sales associate for 18 years and is currently a RSC. Mr. Peterson is identified by Plaintiffs in connection with the Fraudulent Underwriting

Allegations. He has knowledge of facts relevant to the subject matter of several of the allegations in the December 2016 Letter.

**21. Sean Strickland and Ashley Crosby**

On January 16, 2018, the Special Committee's counsel interviewed Sean Strickland and Ashley Crosby. Mr. Strickland is the Director of U.S. Financial Management and Mr. Crosby is the Senior Manager of Distribution and Advertising. Messrs. Strickland and Crosby are familiar with the Aflac Incentive Fund, including the levels of participation of RSCs, DSCs, and the Market Directors in the Aflac Incentive Fund.

The Company's officers, directors, and employees cooperated with the Special Committee and its counsel. The Company's in-house counsel assisted in scheduling interviews and meetings, and the Company timely responded to the Special Committee's requests for documents. Witnesses made themselves available and provided responsive answers to the Special Committee's questions.<sup>16</sup> The Special Committee considers the documents it received to be complete and sufficient to allow it to investigate thoroughly the allegations raised in the Complaint. There was no document or category of documents sought by the Special Committee that was not provided, if available, and there were no witnesses sought by the Special Committee who refused to speak with the Special Committee's counsel.

The Company, through A&B, provided to the Special Committee's counsel over 30,000 e-mails previously collected from over 25 custodians in connection with the Company's investigation of Mr. Joffe's allegations prior to the creation of the Special Committee. The

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<sup>16</sup> An A&B attorney was present for certain witness interviews. The attorney did not object to any questions or interject in any way that affected the candor of any witness in the opinion of counsel for the Special Committee. An A&B attorney was not present for the interviews with Paul Amos or the members of the Special Committee.

electronic documents Jones Day received from A&B were filtered from a collection of over 1.5 million documents pursuant to a list of search terms that Jones Day reviewed and considered appropriate for the purposes of this investigation. In addition, A&B ran additional search terms requested by Jones Day against the collection of 1.5 million documents. Moreover, the Company provided Jones Day with all of Paul Amos's available e-mails and an imaged copy of his MacBook computer so that Jones Day could filter and apply search terms as Jones Day deemed appropriate. Finally, the Company complied with numerous follow-up requests for documents from Jones Day.

**V. THE SPECIAL COMMITTEE'S FINDINGS OF FACT REGARDING THE ALLEGATIONS OF FRAUD**

**A. The Special Committee Finds That The Allegations In The Complaint Regarding The AWP Metric Lack Merit.**

In his December 2016 Letter, Mr. Joffe alleges that the average weekly producer, AWP, metric has been manipulated to appear as though there are more associates making sales on a weekly basis than are actually making sales. AWP is a metric the Company has used for approximately ten years to gauge sales force activity.<sup>17</sup> Plaintiffs allege this manipulation is accomplished by crediting associates with \$1 of production even though they had no sales. [See App. 10, December 2016 Letter, at 7]. As set forth in sections V. through VI. of the Special Committee's Initial Report, the Special Committee found the evidence did not support Plaintiffs' allegations because Paul Amos's stock sale complied with the Company's insider trading policies, Paul Amos had limited knowledge of Mr. Joffe's allegations and the investigation, and the allegations regarding manipulation of the AWP metric lacked merit. Further, to the extent

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<sup>17</sup> The AWP metric is calculated by taking the weighted average of all associates who produce business each week.

that Mr. Joffe suggests that any manipulation impacted the Company's financial statements, Mr. Joffe is incorrect. AWP is a non-GAAP measure that does not affect the Company's financial statements. [See App. 17, Initial Report, at 38-42]. Finally, even if the AWP metric were manipulated in the way alleged, the result of such manipulation would have been immaterial. [App. 17, Initial Report, at 44-45].

**1. Contrary To Plaintiffs' Assertions, The Special Committee Finds No Evidence That The Company's Investigation Was A "Whitewash."**

Plaintiffs characterize the Company's initial investigation into Plaintiffs' allegations as a "whitewash," especially in regard to their allegations concerning the AWP metric. The Special Committee finds no evidence to support this assertion.

In order to protect the Company's attorney-client privilege and to preserve the independence of the Special Committee, the Company did not share with the Special Committee the Company's counsel's analysis and conclusions following their investigation into the allegations in the December 2016 and March 2017 Letters. However, the Company did provide the Special Committee with access to the documents that the Company gathered in connection with its investigation, which included over 30,000 e-mails.

The Company also made available to Jones Day information gathered by Aflac Trust and the internal audit department in connection with their investigations relating to the allegations in the December 2016 and March 2017 Letters. With regard to the AWP Manipulation Allegations, the Company provided the Special Committee with internal audit's analysis of the number of weekly producers with \$1 or less of production during a sample period. They selected the third quarter of 2016 to sample, which was the last full quarter prior to the receipt of the December

2016 Letter. Using records in the Company’s Report Management System (“RPM”),<sup>18</sup> Ms. Ruckert and Mr. Barnett of the internal audit department calculated that approximately 0.09 percent (or fewer than one in a thousand) of the “producers” had \$1 or less of production credit. [See App. 17, Initial Report, at 44-45]. This one-out-of-a-thousand finding fatally undercuts Plaintiffs claims of “widespread” manipulation. The Special Committee finds the Company relied on this fact in support of its investigation, and the existence of this evidence refutes Plaintiffs’ “whitewash” assertions.

Plaintiffs also argue that the Company’s and A&B’s failure to obtain a copy of an April 2010 e-mail exchange between Mr. Conroy and Paul Amos from Plaintiffs’ counsel supports Plaintiffs’ “whitewash” assertion. [See App. 4, Complaint, at ¶¶ 46, 143]. The Special Committee disagrees.<sup>19</sup>

The Special Committee finds that possession of a physical copy of the e-mail was not essential for the Company to evaluate Plaintiffs’ AWP Manipulation Allegations. In the December 2016 Letter, Mr. Joffe refers to that e-mail exchange only to show that Mr. Conroy ostensibly conveyed to Paul Amos his concern that the AWP metric *could* be manipulated, and that Paul Amos disagreed. The December 2016 Letter states: “Thus, in his email to Mr. Amos II of April 13, 2010, Mr. Conroy expressly stated: ‘*Average Weekly Producers is, with all due respect, a “bull pucky” number. There are too many ways to manipulate the figure.*’

Mr. Amos II responded: ‘*I really like the DSC bonus and I think it aligns.*’” [App. 10, December 2016 Letter, at 8]. Mr. Joffe’s letter did not state that Mr. Conroy identified any

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<sup>18</sup> RPM is a web-based application that consolidates the Company’s sales activity, and is separate from the Company’s financial information system.

<sup>19</sup> The Special Committee searched the Company’s electronic data for the e-mail, but was unable to locate this seven-plus-year-old e-mail. As a result, counsel for the Special Committee reached out to Plaintiffs’ counsel to obtain a copy to review.

instances of manipulation in his e-mail – only that it hypothetically *could* be manipulated.

Therefore, the Company’s counsel did not need a copy of the e-mail to investigate whether the AWP metric had been manipulated and whether any such manipulation materially impacted the Company’s financial statements or any of the Company’s disclosures.

Moreover, the Special Committee reviewed a copy of the e-mail prior to the conclusion of its initial investigation. The Special Committee found that the e-mail did not provide meaningful insight into the alleged manipulation of the AWP metric. It reaffirms that finding here.

The Special Committee found that the actual text of that e-mail did not support Mr. Joffe’s characterization of it. The e-mail shows neither that Paul Amos was “expressly forewarned” by Mr. Conroy that the metric could be easily manipulated nor that Paul Amos acknowledged that he prefers the metric. Mr. Conroy’s e-mail to Paul Amos is quite lengthy – spanning four pages, twenty-one paragraphs, and over 1,700 words – and focuses almost entirely on complaints about upcoming changes to the bonus structure for DSCs, which was the position Mr. Conroy’s held at the time. [See App. 21, April 13, 2010 E-mail from Martin Conroy to Paul Amos]. Only a small portion of the e-mail mentions AWP, and only one sentence (the one quoted in Mr. Joffe’s December 2016 Letter), mentions any potential manipulation of the metric. [Id.]. Mr. Joffe’s December 2016 Letter ignores the fact that the majority of the e-mail had nothing to do with AWP. Further, at no point in the e-mail did Mr. Conroy say whether any manipulation, in fact, had occurred, nor did he explain how it could be manipulated. [See id.; App. 10, December 2016 Letter].

Mr. Joffe asserts that Paul Amos, in his response to Mr. Conroy, acknowledged Mr. Conroy’s complaints about the potential manipulation of AWP and openly disagreed with

them. [App. 10, December 2016 Letter]. But Paul Amos’s response does not address Mr. Conroy’s comment about AWP. [App. 21, April 13, 2010 E-mail]. The portion of the response from which Mr. Joffe pulled his quotation reads, in its entirety “[a]s for DSC income, I really like the DSC bonus and I think it aligns. Slight modifications may be made, but I don’t foresee an overhaul.” [Id.]. Given the vast majority of Mr. Conroy’s e-mail focused on the DSC bonus structure, it is not surprising that Paul Amos’s response addressed only that issue. Paul Amos did not comment on Mr. Conroy’s opinion about potential AWP manipulation. [Id.].

**2. The Special Committee Finds That Plaintiffs’ Argument Based On The Alleged Decommissioning Of The AWP Metric Is Factually Baseless.**

Plaintiffs allege that the Company discontinued the use of the AWP metric following receipt of the December 2016 Letter because the Company concluded their AWP allegations had merit. Plaintiffs’ factual premise, however, is erroneous. The Special Committee finds that the Company did not discontinue its use of the AWP metric. On September 1, 2017, Mr. Barnett and Ms. Ruckert showed counsel for the Special Committee the Company’s internal RPM system and counsel observed that the RPM system, in fact, contained a section for AWP reports, including the reports alleged to be decommissioned. Individuals interviewed who were familiar with the metric also confirmed it was still in use. [See, e.g., App. 17, Initial Report, at 44]. Additionally, the AWP metric is still included in the Company’s financial analyst briefing material. [See App. 60, Excerpt of Q4 2017 FAB Supplement, at 18].

**B. The Special Committee Finds That The Fraudulent Recruiting Allegations Are Factually Unfounded.**

Plaintiffs claim that the Company relies on fraudulent practices to recruit new associates. [See App. 10, December 2016 Letter, at 4-7]. Plaintiffs do not allege that any Defendant had any role in the alleged fraudulent recruiting efforts, or that any Defendant even knew of the alleged

practices prior to the Company's receipt of the December 2016 Letter. Assuming for the sake of argument that Plaintiffs' allegations were accurate (a conclusion that is not supported by the evidence), nothing in the various letters or pleadings communicated by Mr. Joffe and his clients identifies any specific harm these practices have allegedly caused the Company. These alleged activities did not have an impact on the financial statements of the Company; rather, at most, these allegations relate to isolated actions in one of the Company's many sales regions.

Plaintiffs premise their Fraudulent Recruiting Allegations on the following assertions: (1) that Company representatives provide potential recruits with an income example that Plaintiffs argue is false and misleading because it sets unrealistic expectations for potential income; (2) that a short video featuring Mr. Fennell, the current New York Market Director (and at the time an RSC), falsely promises potential recruits that "[p]eople want to make money . . . [and] *there is a lot of money to be made at Aflac.*" [*Id.* at 4]; and (3) that the Company is responsible for the actions taken by RSCs and DSCs (like Mr. Conroy) during the recruiting process. The Special Committee finds Plaintiffs' premises are flawed.

The alleged false income example that Mr. Joffe described in his December 2016 Letter does not convey a guarantee of earnings success. Messrs. Fennell and Meier explained that such examples illustrate an associate's earning potential *if* certain production levels are achieved. The potential income described in these examples depended upon an associate's ability to generate the assumed production levels. These witnesses also explained that, depending on the associate's efforts and skills, the production levels in the examples they used were achievable. Messrs. Fennell, Meier, and Peterson further explained that, even though they do not recall the specific example referenced by Mr. Joffe, this example and others like it show an attainable

scenario, especially in a large market such as the New York Metro/Long Island market where this example was allegedly used.

Plaintiffs argue that this practice must be fraudulent because the Company has allegedly “revamped its recruiting program,” following receipt of the December 2016 Letter to now promise \$64,000 in first year commission rather than \$125,000. [App. 4, Complaint, at ¶ 53]. The Special Committee finds this argument lacks merit. Although Plaintiffs focus on two illustrative earnings examples in their Complaint, the evidence confirms that these are not the only two examples used. Rather, RSCs and DSCs have used several different illustrative examples of earnings estimates that provide first-year-income projections based on different assumed levels of production. The Company is not – and by virtue of the associates’ status as independent contractors cannot be – in a position to predict an associate’s income. These illustrations do not guarantee that any particular sales associate will generate the production specified in the example, and none of these examples is authored or sponsored by the Company. The Company does convey to associates that they are independent contractors, and are free to work as much or as little as they see fit subject to a minimum productivity requirement.<sup>20</sup> [See, e.g., App. 12, Martin Conroy’s Associate’s Agreement]. The Company does not control the hours an associate works, the intensity of their efforts, or the amount of money they make. [See *id.*].

Second, Plaintiffs also point to a video that they claim the Company removed from its website ostensibly in response to Plaintiffs’ allegations. Plaintiffs assert that removing the video confirmed that their allegations have merit. The Special Committee finds that the video is not

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<sup>20</sup> According to Ms. Coppedge, the Company has a general policy to terminate a sales associate’s contract if that associate does not produce any business for a twelve-month period.

misleading, and, contrary to Plaintiffs' assertion, has not been removed. This video consists of a very short testimonial by Mr. Fennell commenting on his experience as a sales associate for the Company. The Company included the testimonial in a commercial created and aired several years ago. The Company also placed a portion of the commercial on its website around 2011 along with several other video testimonials. Mr. Fennell's video remains available for viewing on the Company's website. [App. 22, Screenshot of Aflac Website, Agent Testimonials, Join our Sales Team/Testimonials/Trevor F. *available at*: <https://www.aflac.com/sales-jobs/testimonials/default.aspx>, last accessed Jan. 23, 2018].

Although Plaintiffs' Fraudulent Recruiting Allegations are factually deficient and contrary to the evidence collected, the claims further miss the mark because independent contractors, not the Company, engaged in the alleged and unsubstantiated improper recruiting practices. While the Company does not condone anyone misleading aspiring associates, ultimately the activities about which Plaintiffs complain are activities by independent contractors over whom the Company does not exert day-to-day control.

Plaintiffs attempt to connect the alleged wrongful conduct to the Company by alleging that the Company benefits from the alleged fraudulent recruiting because recruiting is an important driver of the Company's sales growth. [App. 10, December 2016 Letter, at 4]. The Special Committee saw no evidence of any effort by the Company to encourage the misrepresentation of earnings potential to new associates, and Plaintiffs fail to quantify how many new associates saw or were misled by the alleged fraudulent income example. As such, the Special Committee finds there is insufficient evidence to conclude that the income example in the recruiting materials has led to sales growth that would have a material impact on the

Company's financial statements. In any event, Plaintiffs fail to allege how the named Defendants have any culpability relating to these allegations.

**C. The Special Committee Does Not Find Evidence Of Systematic Fraud Relating To The Sergeants Benevolent Association Allegations.**

Throughout the relevant time period, the Company has offered various insurance policies to sergeants of the New York City Police Department through an account for the SBA, a union for sergeants in the New York City Police Department. Mr. Conroy asserts that associates in the New York area are selling policies under the SBA account to New York City police personnel who are not sergeants. [*See* App. 23, October 20, 2015 Letter]. Although the Special Committee finds that there have been policies sold to individuals who are not sergeants, these sales have not caused harm to the Company, and the Company has implemented appropriate measures to mitigate the reoccurrence of sales to non-sergeant New York City Police personnel.

Mr. Conroy first made these allegations known by a letter dated October 20, 2015, addressed to Dan Amos. [*Id.*]. Dan Amos then referred the letter to the Company's Chief Compliance Officer, Tom McDaniel, who assigned the matter to the Director of Aflac Trust, Ken Dowless. Mr. Dowless assigned an experienced investigator, Bill Capps of SIU, to investigate. Mr. Capps spent several months investigating the allegations. As part of the investigation, Mr. Capps reviewed the rank and status of policyholders who purchased policies through the SBA account. The investigation did reveal instances where sales associates sold policies to police personnel who were not sergeants under the SBA account. Ironically, Mr. Conroy appears to have been one of the associates who erroneously signed up a non-sergeant for a policy under that account. [App. 39, E-mail from Capps to Dowless dated June 6, 2016 and attachment].

These policies were issued to non-sergeants for several reasons. Some associates reported that they simply assumed the police personnel were sergeants if they asked about

enrollment for coverage through the SBA account. Some associates also reported their belief that the New York City payroll department, which handles the payroll deductions for the SBA (as well as other Aflac policies sold to other City of New York employees) would correct any errors in enrollment. However, neither the City nor the SBA corrected the errors. Ultimately, Aflac Trust concluded there was confusion regarding the issuance of some policies under the SBA account, but there was no evidence of improper or intentional misconduct – *i.e.*, the applications did not falsely state that non-sergeants were sergeants. Rather, the erroneous applications listed as “occupation” such titles as “police officer” or “patrolman.” [*Id.*].

As a result of the Company’s investigation, the region took affirmative steps to mitigate a reoccurrence of the erroneous issuance of policies under the SBA account to non-sergeants. Following the Company’s investigation, Mr. Fennell, the Market Director for the New York City area, spoke with each of the associates selling policies under the SBA account and warned that the practice of enrolling non-sergeants would not be tolerated. In addition, Mr. Peterson, the RSC and one of the associates who originated the SBA account, circulated updated guidelines for issuing policies under the SBA account to associates in his region. These guidelines plainly admonish associates to confirm that all applicants for the SBA account are sergeants, stating: “You MAY NOT sign up anyone other than a Sergeant. IT WILL BE DISCOVERED IF YOU SIGN UP ANYONE WHO IS NOT A SERGEANT. THIS WILL RESULT IN YOUR IMMEDIATE TERMINATION.” [App. 24, Updated SBA Guidelines, at 4 (emphasis in original)]. Additionally, guidelines require the applicant to sign a “Statement of Attestation” confirming their membership in a respective union before a sales associate places them on a union-related account. [*Id.* at 9].

The Company conducted a follow-up investigation beginning in January 2017 to ensure implementation of the remedial actions. The investigation confirmed that the number of policies issued to non-sergeants had dramatically decreased and, according to Ms. Coppedge and Mr. Dowless, the Company has made disciplinary determinations regarding those associates who failed to follow the guidelines.

In January 2018, the Company again reviewed the SBA account. This third review confirmed that, for the period from January 1, 2017 through December 31, 2017, only sergeants were enrolled under the SBA account. [App. 65, 1/22/18 Report of Investigation].

In sum, although some insurance policies were issued to non-sergeants prior to 2017, none of the various letters and pleadings sent on behalf of the Plaintiffs identifies any harm to the Company. In regard to past conduct, the Special Committee finds that the sales activities at issue were episodic and concerned one account. Looking at the entire SBA account, including policies for individuals who were in fact sergeants, the total amount of annualized premium generated by all of the policies in 2015, as estimated by Aflac Trust, was approximately \$389,405. [App. 39, E-mail from Capps to Dowless dated June 6, 2016 and attachment]. Meanwhile, the total amount of annualized premiums in force for all policies in the United States in 2015 for the Company was approximately \$5.67 billion. [App. 40, Excerpt of 2015 10-K, at 2]. In other words, the entire SBA account represents less than 0.007% of the Company's 2015 annualized premiums in force. The annualized premiums for the SBA account as a whole (and the erroneously issued policies as a subset) are quantitatively immaterial. In regard to future conduct, the Company has bolstered its controls to mitigate the reoccurrence of the harm in question, which are working as shown by the third review.

Additionally, none of the Defendants is alleged to have been involved in the sale of the erroneously-issued policies under the SBA account, and only Dan Amos is alleged to have been informed of this activity prior to the receipt of Mr. Joffe's December 2016 Letter. Accordingly, Plaintiffs have not identified how the SBA allegations give rise to a claim against the named Defendants.

**D. The Individual To Group Conversion Allegations Lack Merit.**

According to the Company's website, "over 465,000 companies make Aflac available to their employees." [App. 41, Aflac Group Website]. The Company focuses on marketing insurance products at the worksite. [App. 64, 2016 10-K, at 6]. The Company offers policies on both an individual and a group basis. Group plans are underwritten through Continental American Insurance Company ("CAIC"), which the Company acquired in 2009. "Aflac Group" is the marketing name for CAIC.

The Company sells policies both through independent associates and brokers. The associates generally sell *individual* policies to employees of small employers. The brokers focus on selling the *group* products to midsize and larger employers. [*Id.* at 50].

Employers can decide if they want to offer their employees policies through a group plan, or, in the alternative, they can choose to support their employees' purchase of individual policies by allowing premiums to be paid through payroll deduction.

Individual and group insurance products have different characteristics. Individual policies are individually underwritten with premiums generally paid for by the employee. [*Id.* at 6]. These policies are portable, which means that individuals can maintain their insurance coverage even if they leave their employer, generally at the same premium. [*Id.*]. Individual policies are unique to each employee, and may be issued and priced based on personal factors such as age and medical history. Group plans, on the other hand, supply the same coverage to all

employees enrolled under that plan regardless of age or health factors. [App. 53, Voluntary Insurance: Go With the Group or Go it Alone]. With group plans, the employee only receives a certificate of coverage; the employer essentially owns the policy. That means that the employer can cancel the group plan, thereby terminating the employee's policy. The premiums for group plans are generally lower than the premiums for individual policies, especially for older employees or those with health issues. [*Id.*].

Plaintiffs allege that the Company improperly converted individual policies to group policies to artificially boost the "new annualized premium sales" metric, which they contend "is the key indicator of the Company's growth rates and earnings prospects." [App. 4, Complaint, at ¶ 40]. They claim that the Company includes these allegedly converted policies in the new annualized premium numbers "without disclosing that [the Company's] 'new' premium is in fact the result of cannibalizing [the Company's] own pre-existing business." [*Id.*]. Moreover, Plaintiffs contend that, because group policies generally cost less than individual policies, the claimed conversion actually causes a loss to the Company. [*Id.*]. After reviewing the facts, the Special Committee finds Plaintiffs' allegations are erroneous.

Plaintiffs offer an example involving Plaintiff Gerard McCarthy. Mr. McCarthy claims the Company wrongfully converted one of his long-standing accounts to a group account. He alleges that the Company assisted a broker (Aon) to provide a group plan to Univision Communications, Inc. ("UCI"), which had been one of Mr. McCarthy's accounts. Further, he asserts that Aon told UCI employees during the open enrollment period they could not keep their existing Aflac individual policies, but rather had to purchase group insurance. He claims, "they also forced [UCI] to discontinue all payroll deductions effective . . . January 1, 2016." [*Id.* ¶ 39]. While Mr. McCarthy suggests that this alleged "conversion" is not a good business practice from

the viewpoint of a shareholder, the main thrust of his allegations concern his complaints regarding the loss of his personal commissions.

But the evidence made available to the Special Committee confirms that Mr. McCarthy's allegations are erroneous. That evidence confirms that it was UCI's decision, not the Company's, to switch to a group plan. In 2015, UCI sent a letter to the Company stating that UCI "will no longer support existing individual Aflac plans at the end of this year and would like to cancel payroll deduction on all individual [Aflac] plans effective 12/31/2015. Employees may continue old plans on a direct basis but no new individual plans will be supported." [App. 42, UCI Letter dated November 16, 2015]. The letter confirms that UCI elected to change from supporting individual policies through payroll deduction (from which Mr. McCarthy received commissions) to a group plan (from which he would not receive commissions).

Ms. Coppedge confirmed that there have been many examples of employers preferring to offer a group plan rather than simply to support their employees' decision to enroll in Aflac individual policies through payroll deduction. If an employer requests to change to the group product, the Company will accommodate the employer. Associates are not always happy with that decision because they may lose the commissions on renewals of the prior individual policies if the employees choose to cancel the individual policies they have in place and switch to a group policy. Ultimately, the customers' decisions prevail. First, it is the employers' choice if they want to offer a group plan rather than simply to support payroll deduction for employees' individual policies. Second, it is also the employee-policyholders' choice (if their employer chooses to switch to a group plan) if they want to keep their previously-purchased individual policies and pay for them directly (as opposed to through payroll deduction) or if they instead opt to cancel their individual policies and sign up for the employer group plan.

In Mr. McCarthy's situation, the broker, Aon, received the commissions for the UCI account following UCI's decision to convert to a group plan. According to Ms. Coppedge, as an accommodation, but not a requirement, the Company offered to provide Mr. McCarthy with compensation in the form of a finder's fee. The Company could only award that fee to Mr. McCarthy if he had received Aflac Group certification. At the relevant time, however, Mr. McCarthy's certification had lapsed. The Company notified him that he needed to complete coursework required by Aflac Group to become certified so that he could receive a finder's fee. [App. 26, E-mail chain re: Univision Details for Shared AP Credit # 22082]. Ms. Coppedge explained that Mr. McCarthy had ample time to complete the coursework, but failed to do so. As a result, the Company did not pay him the finder's fee.

The Special Committee did not find any improper or inappropriate conduct in regard to the UCI issue. While Plaintiffs offer no other examples in the Complaint, Mr. Joffe mentions that a similar situation occurred in connection with one of Mr. Conroy's accounts in 2010 and generally assert that Plaintiff Varela also witnessed such "conversions." In sum, Plaintiffs offer examples of, at most, a handful from among the over 465,000 employers who offer Aflac's insurance to their employees. The alleged instances are not material (approximately 0.00043%).

**E. The Special Committee Did Not Find Evidence Of Systemic Fraud Through The Use Of SNG Or Everwell.**

Plaintiffs contend that the use of electronic policy applications has "facilitate[d] fraudulent express enrollment" because associates "enroll customers into policies without their knowledge, consent, or authorization, by using their personal information and by forging their signatures." [App. 10, December 2016 Letter, at 9-10].

Associates can electronically enroll an applicant using SNG, a type of application software, which an agent fills out while sitting with an applicant. After the agent and applicant complete the application form, the applicant signs an electronic signature pad.

Plaintiffs allege that associates conduct “informational sessions” during which they ask employees to “indicate, on paper forms and with signatures, which Aflac policies” they want. [*Id.* at 10]. According to Plaintiffs, the associates then collect the forms with the promise that they will return for enrollment, but instead take the forms and input the information into the SNG application themselves and forge the individuals’ signatures.

Plaintiffs offer no concrete examples of any fraud using SNG. Rather, they describe how the alleged fraud *could* happen, and then summarily assert that “the SNG/Express Enrollment fraud is widespread.” [*Id.*]. They do not say who the “unscrupulous associates” are, at what companies these false enrollments occurred, when the false enrollments occurred, and how many insureds were impacted by this alleged fraud.

The Special Committee reviewed documents relating to alleged application fraud. The Special Committee finds that there have been instances where associates have enrolled insureds without the insureds’ authorization. The Special Committee also finds that the Company routinely investigates these practices, and disciplines wrongdoers, up to termination of their contracts. [*See* App. 43, Report of Investigation; App. 44, SIU Case Summary].

Mr. Dowless described various controls SIU and Aflac Trust rely upon to prevent abuse of electronic applications. With regard to SNG, Mr. Dowless explained that, while it is possible that a sales associate could complete an application using the SNG application to falsify a purported policyholder’s signature, the risks of this practice occurring are not significantly different from the risk of fraudulent enrollment through paper applications. Therefore, Aflac

Trust uses the same monitoring techniques for both paper and SNG applications. [See App. 43, Report of Investigation; App. 44, SIU Case Summary]. Some of the controls in place include monitoring by Aflac Trust's Compliance Fraud Analytics Team. This team monitors for and investigates potential abuse by looking for policies falling into multiple categories including, among others, policies with insureds sharing the same address as the sales associate, and policies sharing the same e-mail as the sales associate. [See App. 63, Aflac Trust 2018: Compliance Fraud Analytics Scheme Information]. Multiple policies with the same address or e-mail information (particularly if the information matches an associates' information) would raise a red flag for the team to review further.

Moreover, the Company is transitioning to a new online electronic application system called Everwell that will eventually replace SNG. According to Mr. Dowless, with Everwell, the policyholder can log in and complete their own application. Some of the information in Everwell will be pre-populated by an employer through the employer's human resources department to make the online application process simpler and faster. Mr. Dowless explained that the Everwell system requires verification upon sign-in through a text message, e-mail confirmation code, or the policyholder's social security number. The Company also monitors Everwell accounts for certain red flags. For example, they look for multiple Everwell accounts with the same passwords, or multiple accounts submitted by the same sales associate in which the policyholders select the same security questions and the same answers. Additionally, the Company sends out relevant reminders regarding prohibited practices and communications regarding training to the associates.

While Plaintiffs reference the Everwell system as a source of fraud in the December 2016 Letter, they fail to provide an example of how that system has been used in connection with any alleged “scheme.”

In sum, the Special Committee finds the Company has appropriate controls in place to detect, combat, and address potential fraud regarding the electronic enrollment process.

**F. The Special Committee Did Not Find Evidence Of Systemic Fraud Regarding Bundling.**

Plaintiffs allege that certain sales associates wrongfully sold policies in bundles by telling potential policyholders they could not buy a particular policy if they did not buy others with it. [See App. 10, December 2016 Letter, at 10]. Plaintiffs sometimes refer to these “bundling” schemes as “Mommy packages.” They allege the Company relied on “bundling” to achieve “increased account penetration” and “increased policies per policyholder.” [*Id.*]. Plaintiffs do not allege that any of the Defendants participated in this purported fraudulent behavior.

Plaintiffs make no specific allegations related to bundling in the Complaint, and in the December 2016 and March 2017 Letters they do not identify the associates who purportedly sold the alleged “Mommy packages,” the names of the policyholders who purchased the bundled policies, the dates these bundling incidents occurred, or the specific region or district where this practice occurred. The only detail they provide is that Mr. Peterson supposedly “utilize[d] the ‘Aflac Triple Play’ packages in New York.”

According to all witnesses interviewed who were familiar with the Company’s sales practices, the Company neither encourages nor condones forcing any customer to buy bundled policies. Mr. Fennell explained that it would be illogical for an associate to risk losing a sale by tying it to the sale of a second policy. Additionally, Mr. Peterson denies ever selling these policies at a discount or suggesting to customers that they had to buy three types of Aflac

insurance if the customer only wanted one or two. The Special Committee saw no evidence of any Company *policy* encouraging forced bundling or discounts for bundling. Mr. Dowless explained that Aflac Trust reviewed the New York market for evidence of bundling, which consisted of reviewing all the accounts in the market to see if there were accounts where each policyholder on the account had the same three policies (*e.g.*, accident, cancer, and hospital policies). Aflac Trust did not find evidence of bundling. Rather, according to Mr. Dowless, Aflac Trust found no accounts where all policyholders in the account had all three of the same policies. It did occasionally detect that some of the policyholders purchased one or two or those policies, but it is not unusual for some policyholders on an account to have one or two of the same policies as others on the same account. Thus, there is no indication that there was a practice of forced bundling policies in the market. Even if the bundling practice has occurred, there is no evidence to suggest that the practice is widespread. As such, there is no reason to believe such activity would have a material impact on the Company's financial statements.

**G. The Special Committee Did Not Find Evidence Of Systemic Fraud Regarding "Sit Codes."**

In the December 2016 Letter, Plaintiffs allege that RSCs and Market Directors used "situation codes" or "sit codes" to "split the commission credits and reassign them at will and without the associates' knowledge and consent" resulting in associates "being cheated out of commission they would have been otherwise entitled to." [*Id.* at 12]. Plaintiffs do not include any specific allegations relating to "sit codes" in the Complaint. Nor do they point to any involvement by any Defendant in the alleged improper use of these codes.

The Special Committee's investigation confirmed that RSCs rely on "sit codes" to divide the commission for a sale among the individuals responsible, both directly and indirectly, for that sale. The Company publicly reports in its Annual Report that sales associates are paid on

commission based on both first-year and renewal premiums from the sales of insurance products, and that district and regional sales coordinators also receive override commissions. [App. 64, 2016 10-K, at 6]. These override commissions are assigned through the use of “sit codes.”

In the December 2016 and March 2017 Letters, Mr. Joffe claims the Company manipulates these codes to increase the number of associates counted as producers by giving one dollar of credit to non-producing associates, thereby artificially boosting the AWP metric. As discussed in detail in the Initial Report, the Special Committee did not find evidence supporting this manipulation claim. As discussed above and in the Initial Report, the Company’s records show that for the quarter prior to the receipt of the December 2016 Letter, fewer than one-in-one-thousand producers had one dollar or less of credit. Therefore, to the extent that there was any manipulation of codes to split commissions to create a \$1 producer, the evidence of any systemic manipulation of sit codes was lacking.

Other than references to one dollar producers, Plaintiffs point to no other manner in which the situation codes are manipulated, other than vague references to the ability of RSCs and Market Directors to change the codes in ways associates dislike. Such concerns amount to compensation disputes. Plaintiffs fail to explain how such commission disputes by independent contractors injured the Company or how the named Defendants were in any way involved.

#### **H. The Earnings Manipulation Allegations Are Factually Inaccurate.**

Plaintiffs assert in the December 2016 Letter that their “allegations . . . raise[] the specter of earnings manipulation achieved by keeping the reporting periods ‘open’ past their calendar close date and improperly booking revenues from business received in that extra time period.” [App. 10, December 2016 Letter, at 13]. Plaintiffs reach this conclusion by interpreting e-mails that they did not write, and admit that they are “not aware how [the Company] books revenue for

accounting purposes[.]” [*Id.* at 14]. A review of the facts show that Plaintiffs’ speculative conclusion is erroneous and contrary to the relevant facts.

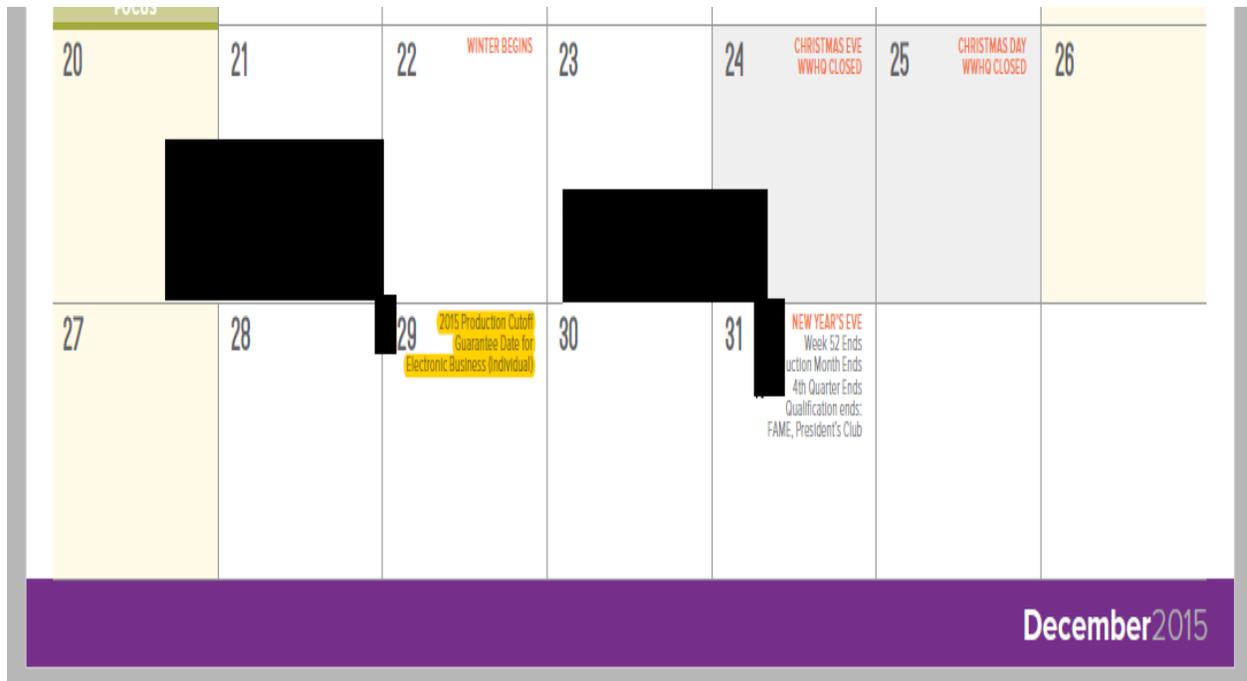
First, Plaintiffs are simply incorrect in their assumption that the e-mail references to “holding open” days means that the Company is improperly booking revenues. As Plaintiffs’ concede, they do not understand how the Company recognizes revenues. The Company does not recognize revenue at the time of policy enrollment. Instead, generally, the Company recognizes revenue when premium payments are due. [*See, e.g.*, 2016 10-K at 37 (“Insurance premiums for most of the Company’s health and life policies . . . are recognized as revenue over the premium-paying periods of the contracts when due from policyholders.”)]. Plaintiffs fail to point to any evidence that the Company has failed to recognize revenue in accordance with its stated policy.

Second, a review of the e-mails that Plaintiffs reference to support their argument that the Company is improperly “holding open” reporting periods reveals that Plaintiffs are mistaken. These e-mails do not refer to financial reporting periods; rather, the referenced time periods are the periods for “production” used by the sales organization. Those “production” time periods are set forth in pre-printed calendars each year. [*See, e.g.*, Apps. 67-69, 2014, 2015, and 2016 Production Calendars].

Plaintiffs conclude from their interpretation of e-mails that the Company had a 53-week year in 2015. [App. 10, December 2016 Letter, at 13]. That is not the case. Plaintiffs misinterpret how the production calendars work.

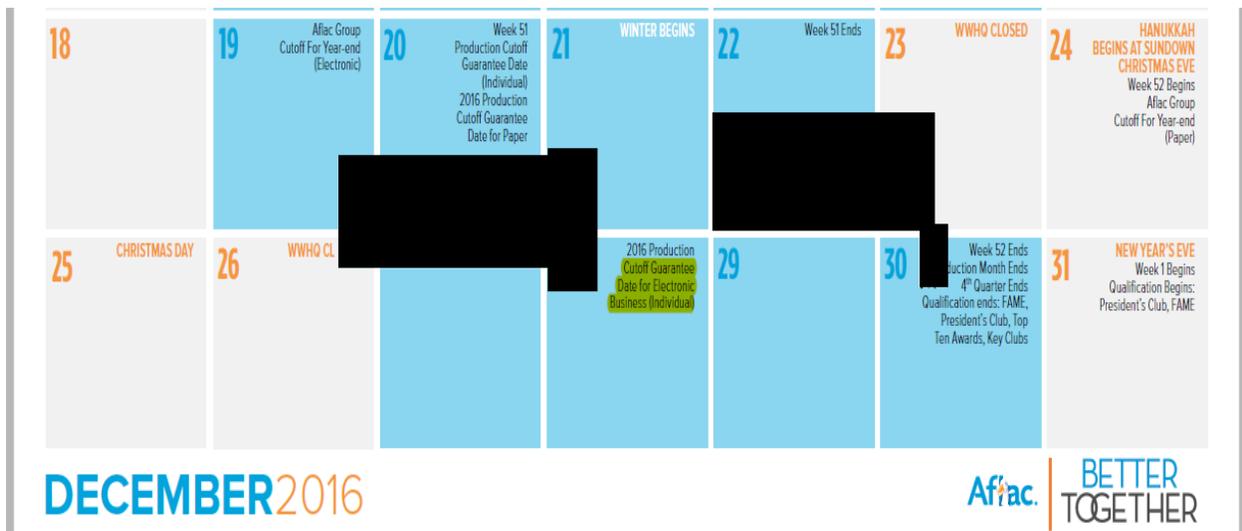
The production calendar is based on a 52-week year with every week beginning on a Saturday. In some years, given holidays, week 52 ends prior to December 31 (for example, 2014 ended on December 24) as can be seen from the screen shot below:





[See, e.g., App. 68, 2015 Production Calendar].

By 2016, the calendar was reset, and week 1 began on Saturday, January 2, 2016. (January 1, 2016 was a holiday). And, as shown below, week 52 ended on Friday, December 30, 2016. The Special Committee confirmed with Ms. Ruckert that the production calendar for any given year ends no later than December 31.



[See, e.g., App. 69, 2016 Production Calendar].

## **I. The Whistleblower Allegations Are Without Merit.**

Plaintiffs allege that the Company retaliated against Messrs. Conroy and Varela in response to their complaints of alleged misconduct. The Special Committee does not find evidence of retaliation.

### **1. The Evidence Does Not Support Mr. Conroy's Allegations of Retaliation.**

Mr. Conroy claims that the Company retaliated against him for raising concerns about the SBA account. He claims he was “stripped of all his accounts and then locked out of Aflac’s Manhattan offices.” [App. 10, December 2016 Letter, at 14]. The Special Committee finds that these allegations are erroneous because (i) Mr. Conroy forfeited his accounts by moving offices and positions multiple times and (ii) he was denied access to the Manhattan office after failing to pay rent for over half a year.

First, as to Mr. Conroy’s accounts, he moved among several different market regions, starting in New Jersey, then moving to Queens, New York, and then to Manhattan from approximately 2015-2016. As Mr. Meier explained, when a coordinator leaves a district for another they can no longer earn commission on the accounts and associates they oversaw. According to Mr. Meier, after Mr. Conroy left New Jersey to take a position as a DSC in Queens, Mr. Conroy informed Mr. Meier that he wanted an RSC position. To accommodate Mr. Conroy’s request, Mr. Meier created a new region in Manhattan, and offered Mr. Conroy the RSC position for that new region. Mr. Conroy accepted the RSC position for this newly-created region, and notified his RSC in Queens (Mr. Peterson) that he would be leaving Queens. Mr. Conroy subsequently changed his mind, claiming he did not want to make the financial commitment required for an RSC, and withdrew his acceptance of the Manhattan RSC position. Unfortunately, in the intervening time, Mr. Peterson filled Mr. Conroy’s former Queens DSC

position with another associate. Mr. Meier again accommodated Mr. Conroy by creating a new DSC position in Manhattan for him, which Mr. Conroy accepted. By virtue of leaving his DSC position in Queens, however, he left behind the associates and accounts assigned to his prior district.

In November 2015, shortly after Mr. Conroy sent his letter to Dan Amos complaining about the SBA account, Mr. Conroy sent an e-mail informing the Company of his decision to resign as a DSC in Manhattan effective January 1, 2016. [App. 57, E-mail from Conroy]. His resignation as a DSC in Manhattan meant he, again, relinquished his right to associates and accounts, this time in Manhattan. Rather than being “stripped of his accounts,” he simply gave them up.

Second, regarding Mr. Conroy’s claim that he was denied access to the Manhattan office, Mr. Fennell, Mr. Meier, and Ms. Coppedge (as well as documents reviewed by the Special Committee) confirmed that Mr. Conroy failed to pay the required rent. As an independent contractor, Mr. Conroy was responsible for paying rent for his own office space. He failed to do so after December 2015.

Nevertheless, the Manhattan RSCs from whom he rented the space did not ask him to leave immediately. He was ultimately denied access on August 17, 2016. [App. 25, E-mail from Trevor Fennell to Martin Conroy dated Aug. 29, 2016 (“We have confirmed that the RSCs have chosen to no longer allow you entry. Since they have control of the premises, there is nothing that Aflac can do.”)]. According to witnesses interviewed, by that time, Mr. Conroy’s behavior had become alarmingly erratic. Such behavior included numerous Facebook posts seemingly of a threatening nature against individuals associated with the Company. [See App. 45, Truth Tour]. These posts raised concerns for RSCs, DSCs, and sales associates in the Manhattan office, who

interpreted these posts as threatening. [App. 25, E-mail from Trevor Fennell to Martin Conroy dated Aug. 29, 2016]. Despite his exclusion from the office space, however, Mr. Conroy remains a sales associate and can sell Aflac insurance.

**2. The Evidence Does Not Support Mr. Varela's Allegations Of Retaliation.**

Louis Varela also claims retaliation as a result of his reporting alleged SNG fraud. [App. 4, Complaint, at ¶ 41]. Plaintiffs allege the Company requested he return his “SNG laptop within hours of his demonstrating [the alleged SNG fraud] for the New York City Comptroller’s Office investigators” and termination a few months later. [*Id.*].

First, no one the Special Committee interviewed was aware of Mr. Varela’s claimed demonstration to the New York City Comptroller’s Office. Mr. Dowless, as Director of Aflac Trust, explained that if Mr. Varela went to the Comptroller’s Office, notice would have been sent to the Company, and subsequently to Aflac Trust. Therefore Mr. Dowless would have been aware of such a meeting or demonstration. But Mr. Dowless found no record of such notice.

Regarding Mr. Varela’s claim that the Company took his SNG laptop, Mr. Dowless explained that, as the Director of Aflac Trust, he would have a record of such a request, but that he had no record of it, and was unaware of a request for Mr. Varela to return his laptop. He also explained that generally associates, as independent contractors, purchase their own laptops so he did not know why anyone would ask him to return his. From time to time, however, the Company may ask for associates’ laptops in order to run forensics if the Company thinks it may include information relevant to a compliance issue under review. Mr. Dowless stated that there was no record in the Aflac Trust database showing that anyone requested Mr. Varela’s laptop.

Finally, the Special Committee finds Mr. Varela’s termination was unrelated to his allegations. Rather, Ms. Coppedge explained and the Company confirmed that Mr. Varela was

terminated due to non-production of business in 2017, which, according to Ms. Coppedge, happens automatically if an associate does not produce business after a rolling 12-month period.

**J. The Tax-Related Allegations Do Not Support A Derivative Claim.**

In a February 2017 letter to the IRS, Mr. Joffe asserts that the Company (a) misclassifies sales associates as independent contractors, (b) maintains an undisclosed slush fund called the Aflac Incentive Fund that is allegedly invisible on the Company's "tax books," and (c) engages in practices that violate Section 125 of the IRS code relating to Cafeteria Plans. [App. 46, February 23, 2017 Letter to the IRS]. Ms. Coppedge has advised counsel for the Special Committee that the IRS has not contacted the Company about these allegations.

**1. The Company Does Not Improperly Classify Its Sales Associates.**

Mr. Joffe alleges that the Company misclassifies sales associates as "independent contractors (1099 Form) rather than employees (W-2)." [*Id.* at 1]. Mr. Joffe alleges that the "degree of control exercised by Aflac over its sales associates, as well as other factors . . . strongly suggest that Aflac sales associates should be treated as W-2 employees for tax purposes rather than as 1099 independent contractors." [*Id.* at 2].

This issue has been litigated frequently by the Company and other insurance companies. Numerous decisions by courts and regulatory agencies support the classification of sales associates as independent contractors. *See, e.g., Brown v. Am. Family Life Assurance. Co. of Columbus*, No. CV 80-39448, 1982 WL 20023, at \*2 (C.D. Cal. Apr. 15, 1982), *rev'd on other grounds*, 709 F.2d 1514 (9th Cir. 1983); [*See also* App. 47, Arbitration Decision; App. 48, EEOC Dismissals (stating "No employee/employer relationship" and "Charging Party was an Independent Contractor")]. Indeed, it is a general practice in the insurance industry to classify sales agents as independent contractors, and courts have upheld that designation for decades. *See, e.g., Weary v. Cochran*, 377 F.3d 522, 524 (6th Cir. 2004) ("As a general matter, this Court has

repeatedly held that insurance agents are independent contractors, rather than employees, in a variety of contexts.”) (citations omitted); *Schwieger v. Farm Bureau Ins. Co. of Neb.*, 207 F.3d 480 (8th Cir. 2000); *Murray v. Principal Fin. Group, Inc.*, 613 F.3d 943 (9th Cir. 2010); *Nationwide Mut. Ins. Co. v. Mortensen*, 606 F.3d 22 (2d Cir. 2010); *Oestman v. Nat’l Farmers Union Ins. Co.*, 958 F.2d 303 (10th Cir. 1992); *Butts v. C.I.R.*, 66 T.C.M. (CCH) 1041 (1993), *aff’d*, 49 F.3d 713 (11th Cir. 1995).

In one recent decision from August 2017, a district court in Ohio disagreed with the accepted wisdom in the industry, but even then that court acknowledged that it was plowing new ground and authorized an immediate interlocutory appeal on the basis that “prior case law has been nearly unanimous in finding that insurance agents generally are to be classified as independent contractors” and the “repercussions of this finding are so far-reaching[.]” *Cf. Jammal v. Am. Family Ins. Co.*, No. 1:13-cv-437, 2017 WL 3268032, at \*20 (N.D. Ohio Aug. 1, 2017). *Jammal* is on appeal, and several amici curiae have filed briefs pointing out that the district court’s decision has turned years of precedent on its head. *See* Brief of Amicus Curiae of the American Council of Life Insurers In Support of Am. Family Life Ins. Co. and Reversal of the District Court’s Certified Opinion, *Jammal v. Am. Family Life Ins. Co.*, 2017 WL 3268032 (No. 1:13-cv-437) (Jan. 24, 2018); Amicus Curiae Brief of the Chamber of Commerce of the United States in Support of Appellants, *Jammal v. Am. Family Life Ins. Co.*, 2017 WL 3268032 (No. 1:13-cv-437) (Jan. 24, 2018); Brief as Amicus Curiae of the Property Casualty Insurers Association of America, et al. in Support of American Family Ins. Co. and Reversal of the District Court’s Certified Opinion, *Jammal v. Am. Family Life Ins. Co.*, 2017 WL 3268032 (No. 1:13-cv-437) (Jan. 24, 2018).

The Special Committee finds no evidence to suggest that the Defendants had any reason to doubt the long-accepted wisdom confirming that associates are independent contractors when presented with Mr. Joffe's March 2017 letter to the IRS. *See, e.g., Brown*, No. CV 80-3948, 1982 WL 20023, at \*2; [App. 47, Arbitration Decision; App. 48, EEOC Dismissals].

**2. Plaintiffs' Allegations Regarding The Aflac Incentive Fund Are Inaccurate.**

Mr. Joffe claims that the Company has an "undisclosed slush fund" known as the Aflac Incentive Fund. [App. 46, February 23, 2017 Letter to the IRS, at 1, 14]. He states that the Company "requires" RSCs and DSCs to contribute a part of their gross commissions to the Aflac Incentive Fund, but the Company "does not recognize contributions to the Fund by the coordinators as its income, nor does it recognize reimbursements from the Fund (which it approves) as its expenses." [*Id.* at 16]. He further argues that the Company includes the contributing coordinators' full commissions on their Form 1099s, but "does not deduct contributions to the Incentive Fund from the contributing [coordinators'] 1099s" [*Id.*].

The Aflac Incentive Fund is a voluntary fund comprised of contributions from the Company's Market Directors, as well as the RSCs, and DSCs for each of the Company's markets.<sup>21</sup> Although Mr. Joffe refers to all associates, only a subset of those associates (Market Directors, RSCs, and DSCs) contribute to the Fund. The Company funds the Market Directors' contributions because they are Company employees. [App. 59, Focus on You 2014 Budget Overview Presentation, at 4]. The Company does not make contributions on behalf of

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<sup>21</sup> The position of Market Director was created on October 1, 2014. Prior to that, the job title closest to that of Market Director was State Sales Coordinator ("SSC"). SSCs were classified as independent contractors. The position of SSC no longer exists. Market Directors, however, are W-2 employees of the Company.

independent contractors, such as RSCs and DSCs. Those who contributed to the Fund may use the Incentive Fund for marketing and growth opportunities.

The Special Committee's investigation revealed that, contrary to Plaintiffs' assertion that the Company requires RSCs and DSCs to contribute to the Incentive Fund, contributions are voluntary. The deduction authorization form confirms this fact. [App. 27, Incentive Fund Deduction Authorization (“[C]ontributions to the Fund are strictly voluntary and may be terminated by me upon written notice to Aflac to cease such deductions.”)]. Ms. Coppedge explained to counsel for the Special Committee that she is familiar with coordinators who have chosen not to participate. Moreover, the Special Committee has reviewed records showing a list of DSCs and RSCs who are participating in the Fund. The records confirm many instances where RSCs and/or DSCs chose not to participate. [See, e.g., App. 28, Excerpt of 2017 Participant/Non-Participant Report].

Additionally, Plaintiffs allege the Company “does not deduct contributions to the Incentive Fund from the contributing [coordinators’] 1099s.” [App. 46, February 23, 2017 Letter to the IRS, at 16]. That is true because, as Messrs. Strickland and Crosby explained, the Company does not seek to provide tax advice to DSCs or RSCs (who are independent contractors) regarding the tax deductibility of contributions to the Incentive Fund. Further, they explained the Company does, however, provide the RSCs and DSCs with documentation regarding their contributions for purposes of preparing their tax returns.

Further, Mr. Joffe alleges the Company's “tax books” fail properly to account for the Fund. [*Id.*]. As Messrs. Strickland and Crosby explained, the Company's accounts for contributions to the Incentive Fund on the balance sheet under “Other Liabilities.” Further, they explained this does not show up as a separate line item because of its minimal size in relation to

other liabilities of the Company. Additionally, the Company's tax department confirmed that Aflac does not take a corporate income tax deduction for reimbursements from the RSC/DSC portion of the Incentive Fund.

Therefore, the Special Committee finds that there is no evidence that the Company improperly handled the Incentive Fund.

### **3. Plaintiffs' Allegations Regarding Violation Of Cafeteria Plan Regulations Lack Merit.**

Plaintiffs allege that the Company violated Section 125 of the Internal Revenue Code relating to cafeteria plans by cancelling policies outside the open enrollment period. [*See* App. 46, February 23, 2017 Letter to IRS, at 16]. Plaintiffs claim the Company allowed election changes in response to employee complaints that they were enrolled without his or her authorization. Plaintiffs state that cafeteria plan rules preclude these "out-of-period" adjustments because they are not due to a "change in status" event. [*Id.* at 18].<sup>22</sup>

A cafeteria plan is an employer-sponsored employee benefit plan through which an employee may elect to forgo taxable cash compensation and use those funds on a pre-tax basis to pay the required employee contribution for certain benefits, such as coverage under the medical plan sponsored by the employer. By paying on a pre-tax basis through a cafeteria plan, the employee avoids income and employment tax on the amount paid for the chosen benefits. In order to secure this tax benefit, the cafeteria plan, both in form and administration, must adhere to the requirements of the IRS cafeteria plan rules. These requirements include, among other things, that the plan be in writing, that non-taxable benefit options are only those specified in the

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<sup>22</sup> As an initial matter, the alleged cafeteria plan violation is only relevant for coverage that is paid for on a pre-tax basis, and many Aflac policies issued through employer programs were paid for on a post-tax basis.

cafeteria plan rules, and that employees may only change their elections under the cafeteria plan at certain times and under certain circumstances.

The Special Committee finds the Plaintiffs' assertions regarding the cafeteria plan violations lack merit. First, direct liability for a violation of the cafeteria plan rules belongs with the sponsoring employer and participating employees, and not with insurers such as the Company. Prop. Treas. Reg. § 1.125-1(c)(6) and (7); Code §§ 3101, 3012(b), and 3403. This comes in the form of liability for income and employment taxes on the amount paid through the plan, including employer withholding for such taxes. *Id.* The Company consistently communicates to employers that legal compliance with respect to these plans is the responsibility of the employer and not the Company. [*See, e.g.,* App. 49, Flex One Sample Cafeteria Plan Document Packet (“You, as sponsoring employer, bear sole responsibility for amending your plan (as necessary) to comply with existing tax law and future changes, for meeting all reporting and disclosure requirements imposed by applicable law, and for the daily administration of your plan.”)]. In fact, employers who use the Company’s cafeteria plan services are required to agree that they retain all responsibility and liability for the plan. [*See* App. 50, Payroll Account Acknowledgment (M-0138)].

Second, the Company has not expressly assumed liability for these plans. It is possible for a vendor to assume the employer’s liability related to income and employment taxes, but only where the vendor actually pays wages directly to employees on behalf of the employer. Code §§ 3504, 3505; *see also* Treas. Reg. § 31.3504-2(e)(6). An insurer who is performing administrative functions related to a cafeteria plan does not become liable for employer

withholding and employment tax obligations without an express assumption of liability or indemnification of the employer.<sup>23</sup> The Company has done neither.

Third, Plaintiffs' suggestion that election changes can never be made outside the period is incorrect. Informal IRS guidance indicates that correction of actual mistakes is permitted. The IRS has informally indicated, in a series of letters, that changes can be made mid-year when the employer determines that a mistake has been made. These letters provide that an error regarding a participant's election may be corrected where there is "clear and convincing evidence" that a mistake has been made.<sup>24</sup> Therefore, even if the Company were responsible for any cafeteria plan violations by employers – which it is not – changes caused by errors in issuing a policy by an insurer may well be considered a mistake under the IRS's informal guidance.

## **VI. THE SPECIAL COMMITTEE'S CONCLUSIONS**

### **A. The Rule 10b-5 Claim Faces Numerous Challenges.**

Plaintiffs claim that, in connection with the Company's repurchases of its shares, the Defendants knowingly disseminated or approved materially false or misleading statements in the Company's 2016 Annual Report and the 2017 Proxy. Plaintiffs allege the following were false or misleading statements:

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<sup>23</sup> While the Company's documents do include an indemnification obligation, it is limited to disagreements between an employee and the Company regarding coverage under the insurance policy and specifically excludes disputes caused by violations of the employer's responsibility under state or federal law. [See App. 51, Payroll Account Activation (account representative version); App. 52, Welcome to Aflac e-mail; App. 50, Payroll Account Acknowledgment]. Instead, the documents consistently provide that it is the employer's responsibility to comply with the law.

<sup>24</sup> See, e.g., IRS Information Letter from Harry Beker, Chief, Office of the Associate Chief Counsel, IRS, dated May 2, 1997; IRS Information Letter from Harry Beker, Chief, Office of the Associate Chief Counsel, IRS, dated March 26, 1998; IRS Information Letter from Harry Beker, Chief, Office of the Associate Chief Counsel, IRS, dated July 7, 1998; IRS Information Letter from Harry Beker, Chief, Office of the Associate Chief Counsel, IRS, addressed to National Plan Administrators dated January 19, 1999.

1. Defendants failed to include in the 2017 Proxy the allegations of fraud set forth in the December 2016 and March 2017 Letters rendering affirmative statements in those documents to be misleading. [*See* App. 4, Complaint, at ¶ 63].
2. The Lead Director, in his letter to shareholders that was included in the 2017 Proxy, encouraged shareholders to vote for a slate of directors that included Dan Amos and Paul Amos despite the allegations raised in the December 2016 and March 2017 Letters. [*Id.* at ¶ 58].
3. The 2017 Proxy included purported assurances by the Corporate Governance Committee that all the director nominees, including Dan Amos and Paul Amos, were selected based on their reputations for honest and ethical conduct in their professional and personal activities, despite alleged “red flags” raised by the December 2016 and March 2017 Letters, which the Director Defendants purportedly ignored. [*Id.* at ¶ 64].
4. The 2017 Proxy stated that the director nominees, including Dan Amos and Paul Amos, were willing and able to serve until the next annual meeting of shareholders or until successors are selected or qualified. Further, the 2017 Proxy stated that the Board had no reason to believe any nominee would be unwilling or unable to serve, despite the allegations in the December 2016 and March 2017 Letters. In addition, the Plaintiffs speculate that Paul Amos’s resignation announced in June 2017 was the result of their allegations. [*Id.* at ¶¶ 65-68].
5. The Proxy purportedly assured shareholders that the Board oversees an enterprise-wide approach to risk management and that the Board is integral to the process of setting the Company’s business strategy, while allegedly being “asleep at the switch” regarding the issues that Plaintiffs speculate led to Paul Amos’s resignation – *i.e.*, the allegations in the December 2016 and March 2017 Letters. [*Id.* at ¶¶ 69-70].
6. The 2017 Proxy included an Audit and Risk Committee report recommending the Board approve the Company’s financial statements to be included in the 2016 SEC Form 10-K despite the alleged knowledge of Defendants Johnson, Bowers, and Knapp – all members of the Audit and Risk Committee – of the allegations in the December 2016 and March 2017 Letters. [*Id.* at ¶ 71].
7. Dan Amos, in his letter to shareholders included in the 2017 Proxy, “encouraged the shareholders to ‘review the enclosed proxy materials and the 2016 Annual Report to learn more about the [C]ompany and the latest achievements’” despite the fact that these documents did not mention the alleged fraud asserted in the December 2016 and March 2017 Letters. [*Id.* at ¶ 72].
8. The 2016 Annual Report failed to mention the allegations set forth in the December 2016 and March 2017 Letters and the Company’s purported investigation of the allegations. [*Id.* at ¶ 73].

9. Dan Amos certified that the financial statements in the 2016 Annual Report fairly represent the financial condition of the Company in all material respects and that he disclosed to the auditors all significant deficiencies and materials weaknesses in controls and any fraud (whether material or not) involving management, despite knowledge of the allegations in the December 2016 and March 2017 Letters. [*Id.* at ¶¶ 74-75].

Plaintiffs further allege that the above purported misstatements or omissions artificially inflated the price of the Company stock, and that the Company repurchased shares of stock while at an inflated price. Those purchases of “inflated” stock allegedly injured the Company. [*Id.* at ¶¶ 109-112, 115-116].

To prevail in a Section 10(b) civil action for violation of Rule 10b-5(b), a plaintiff must prove: “(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.” *Ledford v. Peebles*, 657 F.3d 1222, 1248 (11th Cir. 2011) (citing *Stoneridge Inv. Partners, LLC v. Scientific-Atlanta*, 552 U.S. 148, 157 (2008)); *see also GE Inv’rs v. Gen. Elec. Co.*, 447 F. App’x 229, 231 (2d Cir. 2011). A complaint under Section 10(b) of the Exchange Act must contain more than legal conclusions. “[A] complaint alleging securities fraud must plead ‘enough facts to state a claim to relief that is plausible on its face.’” *Dempsey v. Vieau*, 130 F. Supp. 3d 809, 814 (S.D.N.Y. 2015) (quoting *Bell Atlantic Corp. v. Twombly*, 550 U.S. 544, 570 (2007)). This plausibility standard demands “more than a sheer possibility that a defendant has acted unlawfully.” *Ashcroft v. Iqbal*, 556 U.S. 662, 678 (2009). While factual allegations are construed in the light most favorable to plaintiffs, that tenet does not apply to legal conclusions. *See In re Lions Gate Entm’t Corp. Sec. Litig.*, 165 F. Supp. 3d 1, 5 (S.D.N.Y. 2016), *appeal withdrawn* (June 7, 2016) (citing *Iqbal*, 556 U.S. at 678).

A claim under Section 10(b) must meet the heightened pleading standards of the Federal Rules of Civil Procedure 9(b), and the requirements of the Private Securities Litigation Reform Act (“PSLRA”). See *Dempsey*, 130 F. Supp. at 814; *S. Cherry St., LLC v. Hennesee Grp. LLC*, 573 F.3d 98, 110 (2d Cir. 2009). “The PSLRA expanded on the Rule 9(b) standard, requiring that securities fraud complaints specify each misleading statement; that they set forth the facts on which a belief that a statement is misleading was formed; and that they state with particularity facts giving rise to a strong inference that the defendant acted with the required state of mind.” *City of Taylor Gen. Emps. Ret. Sys. v. Magna Int’l Inc.*, 967 F. Supp. 2d 771, 777-78 (S.D.N.Y. 2013) (quoting *Anschutz Corp. v. Merrill Lynch & Co.*, 690 F.3d 98, 108 (2d Cir. 2012)).

The Special Committee finds that Plaintiffs’ Section 10(b) allegations will likely fail to meet these standards.

**1. Plaintiffs Fail To Identify Any Materially False Or Misleading Statements.**

The alleged false statements fall into three general categories. First, Plaintiffs allege that the omission in the 2017 Proxy Statement of the allegations set forth in the December 2016 and March 2017 Letters (and the related investigation) renders certain statements in that Proxy to be materially false and misleading. [App. 4, Complaint ¶¶ 6, 63, 65-72 (items 1-7 above)]. Second, Plaintiffs allege that the 2016 Annual Report made a similar improper omission. [*Id.* at ¶ 73 (item 8 above)]. Third, Plaintiffs allege that Dan Amos improperly certified the 2016 financial statement due to the existence of Plaintiffs’ allegations set forth in their letters. [*Id.* at ¶¶ 74-75 (item 9 above)]. The Special Committee finds none of these arguments is likely to survive a motion to dismiss.

In order to survive a motion to dismiss with regard to a claimed omission, a Plaintiff must establish that there was a “duty to disclose” the omitted information. See *Basic Inc. v. Levinson*,

485 U.S. 224, 239, n.17 (1988); *Chiarella v. United States*, 445 U.S. 222, 229 (1980) (“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”); *see also In re Enron Corp. Sec. Litig.*, 258 F. Supp. 2d 576, 589 (S.D. Texas 2003) (“Rule 10b-5 does not impose on a corporation an affirmative duty to disclose all non-public material information that it has about a corporation, and where a material omission is alleged, there is no liability under the federal securities laws unless the corporation has a duty to disclose such information.”) (citation omitted); 17 C.F.R. § 240.10b-5 (“It shall be unlawful for any person . . . [t]o make any untrue statement of a material fact or to omit or to state a material fact[.]”) (emphasis added).

Additionally, a Company has no duty to disclose “unsubstantiated allegations.” *Bolger v. First State Financial Services*, 759 F. Supp. 182, 194 (D.N.J. 1991); *see Lebhar Friedman, Inc. v. Movielab, Inc.*, No. 86 Civ. 9965 (SWC), 1987 WL 5793, at \*4 n.5 (S.D.N.Y. Jan. 13, 1987) (“Defendants were not required to disclose . . . mere allegations.”) (citing *Markewich v. Adikes*, 422 F. Supp. 1144, 1146 (E.D.N.Y. 1976)). The mere fact that someone alleges misconduct does not establish that the allegations are material. *See, e.g., SEC v. Reyes*, 491 F. Supp. 2d 906, 912 n.6 (N.D. Cal. 2007) (stating that simply alleging that misstatements were made “is a woefully insufficient basis for finding that the misrepresentations are ‘material’ as a matter of law. If a misrepresentation is deemed material simply because it is a misrepresentation, then the law’s materiality requirement is altogether meaningless”); *see also In re Westinghouse Sec. Litig.*, 90 F.3d 696, 714 (3d Cir. 1996) (holding that when the financial import of alleged misstatements is *de minimis* those alleged misstatements are immaterial as a matter of law). Information is material if there is a substantial likelihood that a reasonable shareholder would consider it

important in making an investment decision. *TSC Indus., Inc. v. Northway, Inc.*, 426 U.S. 438, 449 (1976).

The Special Committee finds that the allegations in the December 2016 and March 2017 Letters were not substantiated by the materials provided by Plaintiffs and remain unsubstantiated following several investigations. The evidence collected as a result of these investigations confirms the alleged practices did not occur or, in the instances where they had occurred, they were isolated events and subject to remediation by the Company. The Special Committee concludes a court is unlikely to find that the Company had a duty to disclose these unsubstantiated allegations.

Plaintiffs claim that miscellaneous complaints by a few independent contractors (and the investigation of those complaints) are material. Numerous cases, however, undercut that assertion. *See Day v. Staples, Inc.*, 555 F. 3d 42, 56 (1st Cir. 2009) (stating that “a disagreement with management about an internal tracking system, which is not reported to shareholders is not actionable” because it does not meet the elements of a securities fraud claim); *In re Sanofi Sec. Litig.*, 155 F. Supp. 3d 386, 407 (S.N.D.Y. 2016) (stating that an argument that defendants misrepresented material facts by failing to disclose an internal investigation was not compelling because “whatever internal investigation took place – if any – did not uncover any unlawful activity of a material proportion”). As the United States Supreme Court set forth in *Basic*, to fulfill the materiality requirement “there must be a substantial likelihood that the disclosure of the omitted fact would have been viewed by the reasonable investor as having significantly altered the ‘total mix’ of information made available.” 485 U.S. at 231–32 (internal citation omitted).

Many of Plaintiffs' allegations describe episodic issues, some occurring several years ago. First, although Plaintiffs refer to fraudulent recruiting activities, the investigation detected no support for the alleged activities.<sup>25</sup> The income example referenced by Plaintiffs is not proof of misconduct, rather it is only one of several examples used by various RSCs and DSCs in the New York area to provide information regarding potential sales associate compensation based on certain assumed levels of production. Nothing on the face of these examples represents that the prospective associate would achieve the assumed level of production and each person interviewed with knowledge regarding recruiting confirmed that they were unaware of any potential sales associate being told they would necessarily achieve these possible levels of production. In any event, Plaintiffs fail to explain how the alleged use of these income examples rendered any affirmative statements made by the Company to be misleading, the name of the person who made any misstatement, or the timing of that misstatement.

Second, in regard to the SBA account, the Special Committee found that there were individuals enrolled under this account who were not sergeants.<sup>26</sup> As a result of the Company's investigation, however the Company adopted remedial measures to address these enrollment issues. The Market Director for the New York City area warned associates that the Company prohibits enrolling non-sergeants in the SBA account. The RSC for the region also distributed updated guidelines requiring sales associates to confirm an applicant's membership in the SBA before issuing a policy under that account. [App. 24, Updated SBA Guidelines, at 4]. Additionally, applicants are now required to sign a "Statement of Attestation" confirming their membership in the SBA. [*Id.* at 9]. Moreover, the Company has conducted two follow-up audits

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<sup>25</sup> *See supra*, at 38.

<sup>26</sup> *See supra*, at 42.

and the latest showed that, as of January 2018, there were no mistaken enrollments under the SBA account.

Third, the individual to group “conversion” complaint regarding UCI arises from a customer’s decision, not misconduct.<sup>27</sup>

Fourth, with regard to the bundling accusations, the Special Committee did not find any systemic or Company-approved example of forced bundling.<sup>28</sup> Rather, the witnesses interviewed understood that Company policy disallowed any attempt to require an applicant to buy any unnecessary policies.

Fifth, Plaintiffs’ allegations regarding “sit codes” were also factually inaccurate. Sit codes are codes used for dividing commissions.<sup>29</sup> The Special Committee found no systematic manipulation of the codes.

Sixth, with regard to the alleged earnings manipulation, Plaintiffs are comparing apples with oranges.<sup>30</sup> The Plaintiffs’ claim that the Company is holding open a reporting period to record revenue earned after the close of that period is simply factually incorrect. The Special Committee saw no evidence that the time period used for financial reporting was held open or treated in any way contrary to GAAP. Instead, the referenced “holding open” practice relates strictly to the sales production calendar and is unrelated to the timing of revenue recognition, which is a function of the timing of when premiums are due under a particular policy.

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<sup>27</sup> *See supra*, at 45.

<sup>28</sup> *See supra*, at 51.

<sup>29</sup> *See supra*, at 52.

<sup>30</sup> *See supra*, at 53.

Seventh, Plaintiffs' tax-related allegations are contrary to law.<sup>31</sup> Courts have consistently held insurance sales associates to be independent contractors. The Special Committee found that the Incentive Fund is indeed voluntary, and the tax reporting is appropriate. And the Company is not responsible for the cafeteria plans of employers who offer Aflac insurance.

Finally, as discussed in detail in the Initial Report, the allegations related to the alleged manipulation of the AWP metric are erroneous, and, in any event, are immaterial.<sup>32</sup>

In light of the foregoing, the Special Committee concludes that it is unlikely that the Company could show that a reasonable investor would consider the facts found by the Special Committee material. Indeed, the Company itself did not consider the facts relevant to these allegations to be material, as evidenced by the fact that neither Paul Amos nor any other member of the Board or executive management was subject to a blackout related to the allegations in the December 2016 and March 2017 Letters when Paul Amos traded on June 12, 2017. [See App. 17, Initial Report, at 58-62].

Plaintiffs also argue that statements in the 2017 Proxy regarding the character and qualifications of the director-nominees are misleading because Defendants omitted information regarding Plaintiffs' allegations. For example, Plaintiffs contend the statement in the 2017 Proxy that all the director nominees were selected based on their reputations for honest and ethical conduct was misleading because the Company did not also disclose the Plaintiffs' allegations or the purported failure of Dan Amos and Paul Amos to act upon them. [App. 4, Complaint ¶ 64]. But statements relating to ethical and professional character are generally not actionable. *See, e.g., Southland Sec. Corp. v. Inspire Ins. Solutions, Inc.*, 365 F. 3d 353, 372 (5th Cir. 2004)

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<sup>31</sup> *See supra*, at 60.

<sup>32</sup> *See supra*, at 34.

(stating that, because analysts rely on facts in determining the value of a security, statements of the vague and optimistic type cannot support a securities fraud action). The law considers a statement that is “too vague, too generalized, or mere corporate puffery [to be] immaterial because a reasonable investor would not base [an] investment decision on the basis of [such] statements.” *Waterford Twp. Gen. Emps. Ret. Sys. v. Bank United Fin. Corp.*, No. 08-CIV-22572, 2010 WL 1332574, at \*8 (S.D. Fla. Mar. 30, 2010); *see also, e.g., Philadelphia Fin. Mgmt. of San Francisco, LLC v. DJSP Enters., Inc.*, 572 F. App’x 713, 717 (11th Cir. 2014). Plaintiffs “must look beyond optimistic characterizations to the specific, verifiable statements made by Defendants if they are to successfully allege a violation of the federal securities laws.” *Waterford Twp.*, 2010 WL 1332574 at \*8; *ECA, Local 134 IBEW Joint Pension Trust of Chicago v. J.P. Morgan Chase Co.*, 553 F.3d 187, 205 (2d Cir. 2009) (remarks by defendants that Company had “risk management processes [that] are highly disciplined” were unactionable puffery); *Southland Sec. Corp.*, 365 F.3d at 372 (“[G]eneralized positive statements about the Company’s competitive strengths, experienced management, and future prospects are not actionable because they are immaterial.”). The Special Committee finds the challenged statements regarding the character and qualifications of the director nominees to be vague and generalized statements that do not support a Section 10(b) claim.

Plaintiffs also challenge statements in the 2017 Proxy and 2016 Annual Report regarding the veracity of the Company’s financial statements. But Plaintiffs have neither alleged nor pointed to any specific facts supporting an inference that the alleged fraudulent activity impacted the Company’s financial statements. Indeed, during a September 2017 telephone conference with counsel for the Special Committee, Mr. Joffe acknowledged that the alleged fraudulent activity did not impact the Company’s financial statements. And, as discussed above, the

Special Committee finds the alleged misconduct could not have any material impact on the Company's financial statements. Additionally, despite Plaintiffs' allegations to the contrary, the Company did in fact speak with its auditor, KPMG, about the allegations. [See App. 58, E-mail from Brenan to McDaniel]. Therefore, the Special Committee does not believe Plaintiffs' challenges to the accuracy of the financial statements have merit. *Cf. Alaska Elec. Pension Fund v. Adecco S.A.*, 434 F. Supp. 2d 815, 822 (S.D. Cal. 2006) (holding that, in the absence of any allegations quantifying the financial impact, plaintiff failed to "allege enough to allow a court to discern whether the alleged GAAP violations were minor or technical in nature, or whether they constituted widespread and significant inflation of revenue") (quoting *In re Daou Sys., Inc. Sec. Litig.*, 411 F.3d 1006, 1017 (9th Cir. 2005)).<sup>33</sup>

## **2. The Complaint Fails To Allege A Strong Inference of Scienter.**

Plaintiffs allege that Defendants acted with scienter solely because they had knowledge of the allegations in the December 2016 and March 2017 Letters. This allegation does not meet

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<sup>33</sup> Furthermore, since this is a derivative demand, the Company must consider if the Defendants have a defense to any claim by the Company against the Defendants. The Defendants have a valid defense to any argument that Plaintiffs' allegations were material based on the doctrine of estoppel. *Fey v. Walston & Co., Inc.*, 493 F.2d 1036, 1049 (7th Cir. 1974) (stating that the affirmative defense of estoppel is "available under the Securities Exchange Act upon sufficient showing"). A party may be entitled to a defense based on the doctrine of estoppel "when the representations or conduct of a party cause another party to act 'in reliance thereon to the latter's detriment.'" *Arrow Exterminators, Inc. v. Zurich Am. Ins. Co.*, 136 F. Supp. 2d 1340, 1351 (N.D. Ga. 2001) (applying Georgia law) (quoting *Carter v. Digby*, 244 Ga. App. 217, 219 n.8 (2000)). This defense prevents a party "with full knowledge of the facts, who accepts the benefits of a transaction, contract, statute, regulation or order" from subsequently taking "an inconsistent position to avoid the corresponding obligations or effects." *DeShong v. Seaboard Coast Line R.R. Co.*, 737 F.2d 1520, 1522 (11th Cir. 1984). Here, the only knowledge that the Directors had regarding the allegations at the time of the alleged misstatements or omissions in the 2017 Proxy or 2016 Annual Report was that the Company had investigated those allegations and found them to be immaterial. [See App. 13, Jan. 5, 2017 Letter; App. 33, Mar. 20, 2017 Letter]. The Special Committee has found no indication that the Defendants had any additional knowledge that would put them on notice of further inquiry and, as such, are able to rely on the Company's assurance that the allegations were immaterial.

the pleading requirements established by the PSLRA. Rather the PSLRA requires Plaintiffs to state with particularity facts giving rise to a strong inference that each Defendant acted with the requisite state of mind, *i.e.*, “a showing of either an ‘intent to deceive, manipulate, or defraud,’ or ‘severe recklessness.’” *Thompson v. Relationserve Media, Inc.*, 610 F.3d 628, 633 (11th Cir. 2010) (quoting *Mizzaro v. Home Depot, Inc.*, 544 F.3d 1230, 1238 (11th Cir. 2008)).<sup>34</sup> A securities fraud complaint will survive only if the “inference of scienter [is] more than merely ‘reasonable’ or ‘permissible’ – it must be cogent and . . . at least as compelling as any opposing inference one could draw from the facts alleged.” *Tellabs v. Makor Issues & Rights, Ltd.*, 551 U.S. 308, 324 (2007). The Court must consider plausible explanations for the Defendants’ conduct, and draw inferences favoring the Plaintiffs. *Id.* A “strong inference” must be present as to “*each* defendant” and “*each* alleged violation[.]” *See City of St. Clair Shores Gen. Emp. Ret. Sys. v. Lender Processing Serv. Inc.*, No. 3:10-CV-1073-J-32JBT, 2012 WL 1080953, at \*4 (M.D. Fla. Mar. 30, 2012) (emphasis added). And Plaintiffs must show that Defendants were aware of – or were severely reckless in not knowing – facts that made their statements false or misleading *when made*. *See Mizzaro*, 544 F.3d at 1245.

To plead strong circumstantial evidence of scienter, the Complaint must allege that the Defendants (a) “engaged in deliberately illegal behavior;” (b) “knew facts or had access to information suggesting that their public statements were not accurate;” or (c) “failed to check information they had a duty to monitor[.]” *S. Cherry St.*, 573 F.3d at 110 (quoting *Novak v.*

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<sup>34</sup> “Severe recklessness is limited to those highly unreasonable omissions or misrepresentations that involve not merely simple or even inexcusable negligence, but an extreme departure from the standards of ordinary care, and that present a danger of misleading buyers or sellers which is either known to the defendant or so obvious that the defendant must have been aware of it.” *Thompson*, 610 F.3d at 634 (quoting *Bryant v. Avado Brands, Inc.*, 187 F.3d 1271, 1282 n.18 (11th Cir. 1999)).

*Kasaks*, 216 F.3d 300, 311 (2d Cir. 2000)). Here, the Complaint does not allege deliberately illegal behavior. While the Complaint does allege a failure to monitor, that allegation is based on the incorrect assumption that the Company's investigation was a "whitewash." Finally, Plaintiffs attempt to plead scienter by pointing to Defendants' purported knowledge of facts or access to information. [App. 4, Complaint ¶ 111]. These conclusory allegations do not satisfy the requirement for scienter. *See Hart v. Internet Wire, Inc.*, 145 F. Supp. 2d 360, 366 (S.D.N.Y. 2001). For each allegedly false statement, Plaintiffs made no attempt to establish each Defendants' then-existing knowledge of contrary facts. *Id.*; *see also Mogensen v. Body Cent. Corp.*, 15 F. Supp. 3d 1191, 1220 (M.D. Fla. 2014). Rather, at most, Plaintiffs state that the Director Defendants knew of allegations, but knowledge of allegations is not the same thing as knowledge of facts. *See Mogensen*, 15 F. Supp. 3d at 1221 (refusing to "strongly infer" scienter without demonstration that "on or about a certain date, Defendants were directly confronted with specific information that actually contradicted – or cast serious doubt upon – their public statements"); *Fidel v. Rampell*, No. 02-61258-CIV, 2005 WL 5587454, at \*4, \*7 (S.D. Fla. Mar. 29, 2005) (refusing to infer scienter because the complaint failed to allege that defendants were directly told specific information that contradicted their public disclosures); *Kinnett v. Strayer Educ., Inc.*, Nos. 8:10-cv-2317-T-23MAP, 8:10-cv-2728-T-23MAP, 2012 WL 933285, at \*12-13 (M.D. Fla. Jan. 3, 2012) (refusing to infer scienter when plaintiff failed to allege that any of the defendants were informed that fraud was actually occurring or that the defendants discussed the alleged fraud). Plaintiffs say nothing about any direct knowledge any specific Director Defendant had about any of the alleged wrongdoing.

With regard to Dan Amos and Paul Amos, Plaintiffs have not shown that they were personally aware of facts supporting the allegations. In evaluating scienter, a court will look to

see if there is a plausible explanation for the Defendants' actions. Here, it is certainly just as plausible to conclude that Defendants believed the allegations to be without merit and rejected them for that reason (as opposed to reaching Plaintiffs' conclusion of fraudulent intent).

In sum, the Special Committee finds that the absence of these required allegations is not surprising. After considering the evidence collected as part of the investigation, the Special Committee finds that none of the Defendants was aware of facts that made their statements false or misleading when made.

Scienter may also be shown if defendants had the motive and opportunity to commit fraud or if there is strong circumstantial evidence of conscious misbehavior or recklessness. *ECA, Local 134 IBEW Joint Pension Tr. Of Chicago*, 553 F.3d at 198-99. The Complaint shows neither.

First, to establish motive and opportunity, the Complaint must allege that the Defendants "benefitted in some concrete and personal way from the purported fraud." *Id.* Plaintiffs argue Defendants' were motivated to inflate artificially the Company's stock price in order to increase the value of their own shares. Plaintiffs allege only that Paul Amos sold shares and that Doug Johnson received options. [App. 4, Complaint ¶ 85]. But receipt of options or sale of stock alone is not evidence of motive and opportunity. *See In re Magnum Hunter Res. Corp. Sec. Litig.*, 616 F. App'x 445, 445 n.2 (plaintiff must plead that the sales are "unusual") (citing *Acito v. IMCERA Grp. Inc.*, 47 F.3d 47, 54 (2d Cir. 1995)). Rather, Plaintiffs must show that any sales or receipt of options were unusual such that they appear "calculated to maximize personal benefit from inside information." *Ressler v. Liz Claiborne, Inc.*, 75 F. Supp. 2d 43, 60 (E.D.N.Y. 1998) (quoting *In re Apple Computer Sec. Litig.*, 886 F.2d 1109, 1117 (9th Cir. 1989) *aff'd sub nom.* *Fishbaum v. Liz Claiborne, Inc.*, 189 F.3d 460 (2d Cir. 1999)); *see also In re Travelzoo Inc. Sec.*

*Litig.*, Nos. 11 Civ. 5531 GBD, 11 Civ. 6845 GBD, 2013 WL 1287342, at \*9-10 (S.D.N.Y. Mar. 29, 2013) (finding an absence of scienter where a defendant sold 95% of her stock because “Plaintiffs fail[ed] to adequately plead that her sale was inconsistent with her prior trading practices”). The Complaint does not suggest that Mr. Johnson did anything out of the ordinary. With regard to Paul Amos, as discussed in the Initial Report, the timing of his sales corresponded with the expiration of his options by virtue of his Separation Agreement. [See App. 17, Initial Report, at 32]. Therefore, there is a plausible explanation for his sales. See *Ressler*, 75 F. Supp. 2d at 60. The Special Committee thus finds that this motive and opportunity argument would likely be unsuccessful. Moreover, the Complaint is silent regarding the other five Defendants and their potential motive.

### **3. Plaintiffs Have Not Shown Loss Causation Or Economic Loss.**

The Company has not made a corrective disclosure. In the absence of a corrective disclosure concerning Plaintiffs’ allegations, Plaintiffs have not properly alleged loss causation. See, e.g., *Dura Pharm., Inc. v. Broudo*, 544 U.S. 336, 338 (2005) (“A private plaintiff who claims securities fraud must prove that the defendant’s fraud caused an economic loss.”); *In re Scientific Atlanta, Inc. Sec. Litig.*, 754 F. Supp. 2d 1339, 1372 (N.D. Ga. 2010) (in the absence of any “correction of the alleged fraud” plaintiffs failed to demonstrate that the defendant’s misrepresentation played any role in the loss when no information revealing the misrepresentation came to light during the class period).

Plaintiffs could conceivably argue that two events put the public on notice that something was amiss: (1) the resignation of Paul Amos announced shortly after the May 2017 Annual Meeting and (2) the stock drop as a result of a January 11, 2018 article in The Intercept regarding the Plaintiffs’ allegations. But neither event would suffice to establish Plaintiffs’ claim. See *In*

*re Verisign, Inc., Derivative Litig.*, 531 F. Supp. 2d 1173, 1207–08 (N.D. Cal. 2007) (plaintiff must establish loss causation, or economic loss).

As Plaintiffs did here, the *Verisign* plaintiffs claimed that the corporation repurchased its shares at inflated prices and thus suffered harm. The *Verisign* plaintiffs argued that it was not a requirement to prove that there was an actual corrective disclosure. Rather, the plaintiffs claimed that the market could learn the “truth” through a variety of sources. The court, however, rejected plaintiff’s argument, reasoning:

In order to plead loss causation, a plaintiff need only allege that the loss resulted from a stock price drop caused by revelation of the “relevant truth” – that is, true facts about the Company’s financial condition or performance that defendants had concealed. *Dura*, 544 U.S. at 342–46, 125 S.Ct. 1627. Plaintiffs assert, however, that it is not necessary that there be a true “corrective disclosure,” but rather that the market could learn about the possible fraud through a number of sources spread out through a period of time, during an investigation or because of resignations. Plaintiffs claim that the allegations of market knowledge through the resignation of key directors, followed by a drop in the price of the stock, are sufficient to adequately allege economic loss.

The court finds that the [the plaintiffs] fail[ed] to plead facts showing economic loss or loss causation. Indeed, as defendants have pointed out, it is questionable whether plaintiffs will ever be able to allege loss causation, because VeriSign’s stock price went up, not down, after the June 27, 2006, announcement of the grand jury subpoena, the inquiry from the SEC, and the announcement of the internal review of stock option practices by VeriSign’s board of directors. Similarly, the stock price went up, not down, after VeriSign’s November 21 and 22, 2006, announcements of the preliminary results of the directors’ review of the stock option grants, and its statement of its intent to restate its 2001–2005 financial statements to record \$250 million in non-cash, stock-based compensation expense.

*Id.* at 1208.

The facts in *Verisign* align with the facts here. First, there was no disclosure made “correcting” any prior misstatements made by the Company. Second, even if Paul Amos’s June 12, 2017 stock sale was deemed to be a corrective disclosure, the price of the Company’s stock has steadily increased since that sale, negating any argument of loss causation. The stock traded

at \$77.4043 per share on June 12, 2017. On January 29, 2018, the stock price opened at \$90.78. Moreover, at market close on June 12, 2017, the Company's market capitalization was \$30.678 billion. On January 25, 2018, the Company's market capitalization was \$35.061 billion, increasing almost \$5 billion since Paul Amos sold his shares. [App. 8, Excerpt of 2017 Second Quarter Form 10-Q (shares outstanding); App. 34, Yahoo Finance, Aflac Incorporated]. The absence of a market decline after Paul Amos's stock sale contradicts any inference that that stock price was improperly inflated at the time of his resignation and stock sale. Also, the Company's market capitalization increase (by nearly \$5 billion) undercuts any inference that it was harmed by the sale. Without any showing of economic harm or loss causation, Plaintiffs' Section 10(b) claim fails.

Any argument that the January 11, 2018 Intercept article describing Plaintiffs' allegations operates as a *de facto* corrective disclosure also fails. First, it is questionable whether such an article constitutes a corrective disclosure. Courts have typically held that the announcement of an investigation without a finding of wrongdoing is not enough to constitute a corrective disclosure. *Meyer v. Greene*, 710 F.3d 1189, 1201 (11th Cir. 2013) ("The announcement of an investigation reveals just that – an investigation – and nothing more."); *see also In re Almost Family, Inc. Sec. Litig.*, No. 3:10-CV-00520-H, 2012 WL 443461, at \*13 (W.D. Ky. Feb. 10, 2012) ("Numerous federal district courts have held that a disclosure of an investigation, absent an actual revelation of fraud, is not a corrective disclosure."); *In re Maxim Integrated Prods., Inc. Sec. Litig.*, 639 F. Supp. 2d 1038, 1047 (N.D. Cal. 2009) (explaining that disclosures of SEC investigations may be "indicators of risk because they reveal the potential existence of future corrective information," but they are not corrective disclosures for purposes of loss causation);

*Rudolph v. UTStarcom*, 560 F. Supp. 2d 880, 887-88 (N.D. Cal. 2008) (holding that the announcement of internal investigation cannot support an allegation of loss causation).

Second, while the stock price dropped to \$84.94 when the article was published, the stock price has since nearly rebounded. The January 10, 2018 price was \$91.69. On January 29, 2018, the Company's stock price was \$90.78. Analysts watching the Company stock have remarked that the stock drop was an overreaction, which was tempered by the public release of the Initial Report. [See App. 32, Recent Fraud News May Not Have Material Impact on Aflac; Raymond James Upgrades].

#### **4. Plaintiffs Cannot Establish Reliance.**

To establish their Section 10(b) claim, Plaintiffs must be able to establish that the Company relied on the absence of the allegedly omitted information – *i.e.*, the allegations of wrongdoing – when the Company repurchased shares. In an attempt to establish reliance, the Plaintiffs allege that, in deciding to repurchase shares, the Company relied on the stock price reflecting all relevant information. But the Company's directors (including the Defendants) authorized the repurchases, and the directors (including the Defendants) knew that they had not disclosed the Plaintiffs' allegations. Therefore, both the Company and the Defendants knew that information about Plaintiffs' allegations was not a factor in determining the market price for the Company's stock and therefore it is impossible for them to have relied on the omitted information.

The plaintiffs in *Verisign* made a similar reliance arguments as the Plaintiffs here, and the Court rejected the argument:

The court finds that plaintiffs fail to plead facts showing reliance. As with loss causation, it may prove impossible for plaintiffs to adequately plead reliance under the facts of the case. Plaintiffs allege that “VeriSign would not have purchased VeriSign common stock at the prices it paid, had the market previously been award [sic] that the market price of VeriSign's stock was artificially and

falsely inflated by defendants' misleading statements.” CAC ¶ 266. However, the CAC does not identify a single VeriSign officer or director who relied on the supposedly false or misleading financial statements in deciding to undertake the stock repurchase on VeriSign's behalf.

*Verisign*, 531 F. Supp. 2d at 1209.

In other words, assuming for the sake of argument that the 2017 Proxy and the 2016 Annual Report were misleading because they did not mention the Plaintiffs’ allegations, the Company, acting through its directors who are also Defendants, could not have relied on the supposedly misleading statements. Indeed, “[a]pproval of stock repurchases by a ‘disinterested majority of the board possessing authority to act and fully informed of all relevant facts will suffice to bar a Rule 10b–5 claim that the corporation or its stockholders were deceived.’” *Staehr*, 2010 WL 11030716, at \*5 (quoting *In re Citigroup Inc., S’holder Derivative Litig.*, No. 07 Civ. 9841, 2009 WL 2610746, at \*10 (S.D.N.Y. Aug. 25, 2009)). “When a disinterested majority of the board approves a transaction, the plaintiff cannot demonstrate that the shareholders were deceived ‘because the knowledge of the disinterested majority in such event must be attributed to the corporation and its stockholders.’” *Id.* (quoting *Maldonado v. Flynn*, 597 F.2d at 793). A director is considered “disinterested” if “he or she lacks a financial stake in the transaction under consideration.” *Id.* In other words, “a plaintiff cannot show a Rule 10b–5 violation where the claim is based on a transaction approved by the board, and there are no allegations (a) that the board members were not informed of the relevant facts and (b) the board members were not personally interested in the transaction, or controlled by an interested party.” *Id.*

Here, the Special Committee has seen no evidence that the Defendants have an interest in the share repurchase. A review of the publicly filed Form 4s shows the Company’s directors both purchased and sold Company stock in the period since the Company’s receipt of the December 2016 Letter. [*See, e.g.*, Form 4 filed February 27, 2017 by Charles Knapp].

Interviews with directors revealed that the 2017 repurchases were consistent with past practice, and that the Company's Board of Directors has authorized share repurchases for over ten years. The Company's share repurchases in 2017 were pursuant to a publicly disclosed share repurchase program similar to the share repurchase programs disclosed in recent years. [App. 29, 2016 Q4 Results and Outlook Report dated Jan. 31, 2017, at 4 ("As we have communicated, absent compelling alternatives, we believe that growing the cash dividend and repurchasing our shares are the most attractive means for deploying capital. We continue to anticipate that we'll repurchase in the range of \$1.3 to \$1.5 billion of our shares in 2017, front-end loaded in the first half of the year."); App. 30, 2015 Q4 Results and Outlook Report dated Feb. 1, 2016, at 4 ("As we have communicated, absent compelling alternatives, we believe that growing the cash dividend and repurchasing our shares are the most attractive means for deploying capital. We continue to anticipate that we'll repurchase \$1.4 billion of our shares in 2016, largely front-end loaded in the first half of the year."); App. 31, 2014 Q4 Results and Outlook Report dated Feb. 3, 2015, at 4 ("As we have said for many years, we believe that growing the cash dividend and repurchasing our shares are the most attractive means for deploying capital . . . We currently plan to repurchase \$1.3 billion of our shares in 2015.")]. As explained by Dr. Knapp, these share repurchases provide a means to return value to the Company's shareholders. The directors typically authorize the Company's management to repurchase a specified amount of shares in August of each year when appropriate as one of the Company's three primary capital deployment options. [See App. 54 2015 Board Authorization; App. 55 2017 Board Authorization]. Management then decides when these shares will be repurchased. In regard to the shares repurchased in June, July, and early August of 2017, the Board authorized those repurchases in the summer of 2015, prior to receipt of any letters sent by Mr. Joffe or any of his clients.

**B. The Special Committee Finds The Section 14(a) Claim To Be Without Merit.**

Plaintiffs allege Defendants violated SEC Rule 14a-9, promulgated pursuant to Rule 14(a) of the Exchange Act, because the Proxy was materially false and misleading regarding the Board recommendation of the re-election of members of the Board, including Dan Amos and Paul Amos, and the approval of the Board members' compensation. [App. 4, Complaint, at ¶¶ 118-121]. In reliance on these alleged misstatements, the Company's shareholders elected the slate of proposed directors and approved the requested compensation. [*Id.* at ¶¶ 122-125].

**1. Plaintiffs' Claim That The 2017 Proxy Is False Or Misleading Lacks Merit Because The Company Was Not Required To Disclose Unsubstantiated Allegations of Misconduct.**

To establish a Section 14(a) violation, a plaintiff must show “(1) a proxy statement contained a material misrepresentation or omission which (2) caused the plaintiff injury and (3) that the proxy solicitation itself, rather than the particular defect in the solicitation materials, was an essential link in the accomplishment of the transaction.” *Land and Bldgs. Inv. Mgmt., LLC, v. Taubman Ctrs., Inc.*, Case No. 12-11576, 2017 WL 3499900, at \*3 (E.D. Mich. Aug. 16, 2017) (quoting *Tracinda Corp. v. DaimlerChrysler AG*, 502 F.3d 212, 228 (3d Cir. 2007)). To impose liability, that misstatement or omission must be “made with the requisite level of culpability,” and such misstatement or omission must be an essential link in the accomplishment of the proposed transaction – here the re-election of the directors at the May 2017 Annual Meeting. *See Desai v. Meyercord*, 223 F.3d 1020, 1022 (9th Cir. 2000) (citing *TSC Indus.*, 426 U.S. at 444 & n.7).

An omitted fact is material under Section 14(a) if there is a substantial likelihood that a reasonable shareholder would consider it important in deciding how to vote. *See TSC Indus.*, 426 U.S. at 449. The standard does not “require proof of a substantial likelihood that disclosure of the omitted fact would have caused the reasonable investor to change his vote.” *Id.* Rather,

the standard requires “a showing of a substantial likelihood that, under all the circumstances, the omitted fact would have assumed actual significance in the deliberations of the reasonable shareholder.” *Id.* In other words, “there must be a substantial likelihood that the disclosure of the omitted fact would have been viewed by the reasonable investor as having significantly altered the ‘total mix’ of information made available.” *Id.*

The Complaint alleges that the 2017 Proxy was misleading because Defendants (1) failed to include Plaintiffs’ allegations, [App. 4, Complaint, at ¶ 63], (2) encouraged shareholders to vote for a slate of directors that included Dan Amos and Paul Amos despite the allegations raised in the December 2016 and March 2017 Letters, [*id.* at ¶ 64], (3) included assurances that all the director nominees, including Dan Amos and Paul Amos, were selected based on their reputations for honest and ethical conduct in their professional and personal activities, [*id.*], (4) stated that the director nominees were willing and able to serve until the next annual meeting of shareholders, [*id.* at ¶ 65], and (5) assured shareholders that the Board oversees an enterprise-wide approach to risk management and the Audit and Risk Committee recommended the Board approve the Company’s financial statements to be included in the 2016 Annual Report, [*id.* at ¶¶ 69-71].

First, Plaintiffs’ reliance on the lack of disclosure of their allegations or related investigation is misplaced. As discussed above, a Company has no duty to disclose to shareholders unsubstantiated allegations. *See, e.g., Bolger*, 759 F. Supp. at 194 (stating that a company has no duty to disclose unsubstantiated allegations); *see also United States v. Matthews*, 787 F. 2d 38, 45 (2d Cir. 1986) (“Liability under Rule 14a–9 is predicated upon a showing that an allegedly omitted fact is true.”) (quoting *Bertoglio v. Texas Int’l Co.*, 488 F. Supp. 630, 649 (D. Del. 1980)); *In re Marsh & McLennan Companies, Inc. Sec. Litig.*, 536 F. Supp. 2d 313, 322

(S.D.N.Y. 2007) (holding that although the director defendants' alleged mismanagement was arguably relevant to their re-election, there was no duty to disclose such information and that "courts in this and other circuits have held that there is no per se rule, under either section 14(a) or Rule 14a-9, requiring the disclosure [of] mere mismanagement[.]"); *Ciresi v. Citicorp*, 782 F. Supp. 819, 823 (S.D.N.Y. 1991) *aff'd*, 956 F.2d 1161 (2d Cir. 1992) (dismissing § 14(a) claim in part because "the law does not impose a duty to disclose uncharged, unadjudicated wrongdoing or mismanagement"); *In re Teledyne Def. Contracting Derivative Litig.*, 849 F. Supp. 1382 (C.D. Cal. 1993) (holding that "[d]irectors and officers simply need not confess guilt to involvement in criminal conduct and breaches of fiduciary duties of care when such charges have not yet been brought, let alone proven"); *Kahn v. Wien*, 842 F. Supp. 667, 678 (E.D.N.Y. 1994) ("The Second Circuit has held that the disclosure of unproven allegations is not required in proxy solicitations.") (citing *Ciresi*, 782 F. Supp. at 823). Therefore, Plaintiffs cannot state a Section 14(a) claim based on the failure to reveal allegations or the Board's subsequent investigation into those allegations. See *In re Browning-Ferris Indus., Inc. S'holder Derivative Litig.*, 830 F. Supp. 361, 368 (S.D. Tex. 1993).

Additionally, the materiality analysis used to analyze the Section 10(b) claim applies in regard to the Section 14(a) claim. As discussed above, the facts found by the Special Committee show that the allegations are not material. Because immaterial information cannot form the basis of a Section 14(a) claim, the failure to reference the allegations in the 2017 Proxy cannot support Plaintiffs' Section 14(a) claim.

Second, because there was no duty to disclose these allegations, Plaintiffs' allegations that the 2017 Proxy was misleading because it encouraged shareholders to vote for a slate of directors, including Dan Amos and Paul Amos, despite their allegations, are similarly misplaced.

“A reasonable [ ] shareholder would not consider . . . baseless allegations to be material in an election of an unopposed slate of director nominees.” *Bolger*, 759 F. Supp. at 194. Indeed, even if such allegations become the subject of a lawsuit, the Company does not necessarily have an obligation to disclose them. *See* 17 C.F.R. § 229.103 (regulation S-K requires disclosure only of non-routine pending litigation); *see also GAF Corp. v. Heyman*, 724 F. 2d 727, 739 (2d Cir. 1983) (“[U]nadjudicated allegations in a pending civil action against a director-nominee should not automatically be deemed material. In a society as litigious as ours, where plaintiffs are permitted great latitude in their pleadings, a reasonable shareholder would not place much stock in the bald, untested allegations in a civil complaint . . .”).

Third, Plaintiffs’ allegations that the 2017 Proxy was misleading because it assured shareholders that the director nominees were honest and ethical is misplaced because, as discussed earlier, statements relating to ethical and professional character are generally not actionable. *See, e.g., Southland Sec. Corp.*, 365 F. 3d at 372 (stating that because analysts rely on facts in determining the value of a security statements of the vague and optimistic type cannot support a securities fraud action).

Fourth, Plaintiffs allege that the statement in the 2017 Proxy that the directors were expected to serve until the next election is false because Paul Amos resigned in June 2017. The Special Committee found no evidence suggesting that the Defendants knew that Paul Amos would resign at the time of the publication of the 2017 Proxy.

Finally, as to the assurance that the Board oversees an “enterprise-wide” approach to risk management and that the Audit Committee approves of the Company’s financial statements, the Special Committee found no evidence suggesting that such assurance was false or misleading. As discussed throughout, the Defendants were informed of the allegations in the December 2016

and March 2017 Letters and were assured that those allegations were immaterial. Thus, there was no reason not to approve the financial statements.

**2. The Company Would Most Likely Be Unable To Show Loss Causation.**

Plaintiffs fail to allege an economic loss arising from alleged misrepresentations and omissions in the 2017 Proxy. This element, called loss causation, is not satisfied by simply alleging that the price of the security was inflated because of an alleged misrepresentation. *Dura Pharm.*, 544 U.S. at 338. In order to satisfy this requirement, a plaintiff must provide the defendant “with notice of what the relevant economic loss might be or of what the causal connection might be between that loss and the misrepresentation.” *Id.* at 347. “[W]ithout an allegation of economic loss, no remedy, equitable or otherwise, is available.” *New York City Emps’ Ret. Sys. v. Jobs*, 593 F.3d 1018, 1024 (9th Cir. 2010), (holding that plaintiffs failed to adequately plead economic loss to satisfy a disclosure claim under § 14(a) and Rule 14a-9), *overruled on other grounds, Lacey v. Maricopa Cty.*, 693 F.3d 896 (9th Cir. 2012). Instead, the only alleged economic loss is a claimed inflated stock price due to the failure to disclose Plaintiffs’ allegations. That allegation does not suffice. *Id.* (citing *Dura Pharm.*, 544 U.S. at 347-48) (noting that alleging an “artificially inflated purchase price” is not itself an economic loss).

**3. The Company Would Most Likely Be Unable To Show Transaction Causation.**

Plaintiffs have also failed to allege the required element of transaction causation – that is, that the misstatement or omission was an essential link in the proposed transaction, here, the election of directors and approval of the requested compensation. *See In re Tenneco Sec. Litig.*, 449 F. Supp. 528, 531 (S.D. Tex. 1978) (citing *Lewis v. Elam*, C.C.H. Fed Sec. L. Rep. P. 96,013 (S.D.N.Y. April 5, 1977)). For there to be liability, the proxy solicitation itself – rather than a

particular defect in the solicitation materials – must be an essential link to the accomplishment of the transaction. *See Mills v. Elec. Auto-Life Co.*, 396 U.S. 375, 385 (1970).

Here, Plaintiffs do not seek to rescind the election of the directors, but rather seek damages presumably as a consequence of that election. But courts have generally rejected claims for damages in situations such as those presented here, where the proxy at issue involves only the election of directors and not some other corporate action for which the Company seeks shareholder approval. The act of electing the directors rarely causes the harm for which plaintiffs seek damages. *See Gen. Elec. Co. by Levit v. Cathcart*, 980 F.2d 927 (3d Cir. 1992) (directors' reelection did not create any cognizable harm because shareholders' votes did not authorize transactions that caused losses); *Rosenbaum v. Klein*, 547 F. Supp. 586 (E.D. Pa. 1982) (dismissing plaintiffs' 14(a) claims because the alleged failure to disclose in an election proxy was not the cause of the act for which they seek damages); *Issen v. GSC Enters., Inc.*, 522 F. Supp. 390, 396 (N.D. Ill. 1981) (holding that the complaint fails to state a claim upon which relief may be granted under section 14(a) because the election of directors was not causally related to the action for which plaintiffs seek damages).

Instead, Plaintiffs seek damages for alleged stock price inflation for failure to disclose their allegations. [App. 4, Complaint, at ¶ 125]. They seek damages based on the 2017 Proxy, which merely elected the directors while the alleged misconduct – virtually all of which were the decisions of employees and independent contractors in the normal course of performing their work – did not require shareholder approval. *See Zilker v. Klein*, 510 F. Supp. 1070, 1074 (N.D. Ill. 1981) (dismissing claim under Section 14 because alleged misconduct did not require shareholder approval). *See United Canso Oil & Gas Ltd v. Catawba Corp.*, 566 F. Supp. 232, 238 (D. Conn 1983) (14(a) claims dismissed on the ground that the allegedly defective proxy

solicitations were not an essential link in the accomplishment of the challenged transactions because the only shareholder involvement was the election of the directors who carried out the transactions); *see id.* at 237 (rejecting plaintiff’s theory of “but for” causation as impractical and overbroad because plaintiff’s theory would hold directors liable under Section 14(a) for failure to disclose improprieties in proxy statements because “but for” this failure they might not have been reelected).

Finally, the claims relating to Paul Amos’s resignation also fail because Plaintiffs have articulated no theory of damage to the Company – not even the flawed inflated stock price theory. While Plaintiffs assert that the Company was harmed by Paul Amos’s resignation shortly after his re-election to the Board, the stock price increased and remains significantly higher than it was on the date that the Company publicly announced his resignation. [*See* App. 35, Bloomberg Stock Report dated January 25, 2018 (stock price at market close on January 24, 2018 was \$88.43 while the stock price at market close on June 6, 2017 was \$74.79)].

In any event, the relief sought for any Section 14(a) claim regarding Paul Amos’s resignation is moot because he has already resigned. *In re Teledyne Def. Contracting Derivative Litig.*, 849 F. Supp. at 379 (stating that without the planned amendment of the complaint, Plaintiff’s Section 14(a) claim would be moot because it is based on proxy statements relating to director terms which expired and “challenges to the election of directors for lapsed terms are moot”) (quoting *Gen. Elec. Co. by Levit*, 980 F.2d at 934); *In re Tenneco Sec. Litig.*, 449 F. Supp. at 531 (denying plaintiffs’ claims for relief because any injunctive relief for alleged improper election of directors had already been accomplished by re-election of the directors under unchallenged proxy statements).

**C. The Special Committee Has Previously Rejected The Demand To Bring A 20A Claim And Reiterates That Conclusion Here.**

Plaintiffs only allege a Section 20A insider trading claim against Paul Amos. They claim first that he sold shares of Company stock in June 2017 while in possession of knowledge of the allegations set forth in the December 2016 and March 2017 Letters. [App. 4, Complaint, at ¶¶ 127-133]. Second, Plaintiffs assert that the Company's share repurchases in July and August 2017 constitute contemporaneous trades. [*Id.*]. Third, Plaintiffs allege that Paul Amos is liable for damage to the Company as a result of the Company's repurchase of shares in June 2017. [*Id.*].

The Special Committee evaluated whether the Company had a viable claim for insider trading under either federal or state law, and determined that the Company did not because it would be unable sufficiently to establish all of the required elements under the relevant federal and state laws, including materiality, scienter, and harm to the Company. [App. 17, Initial Report, at 56-67]. The allegations in the Complaint do not change that analysis.

**D. Any Breach Of Fiduciary Duty Claim By The Company Against The Defendants Would Lack Factual Support And Be Subject To Several Defenses.**

Plaintiffs allege that Defendants knowingly breached the duties of "candor, good faith, loyalty and reasonable inquiry." [App. 4, Complaint, at ¶¶ 135-136]. In regard to Dan Amos and Paul Amos, Plaintiff's claim they (i) knowingly participated in or failed to prevent the alleged misconduct; (ii) allowed retaliation against Messrs. Conroy and Varela; (iii) ignored Mr. McCarthy's complaints; and (iv) "orchestrated the Company's current efforts to whitewash the fraud," in breach of their fiduciary duties. [*Id.* at ¶¶ 137-138]. In regard to the Director Defendants, Plaintiffs claim they breached their duties by (i) failing to investigate Plaintiffs' allegations and (ii) "not knowing that the 'Company's due diligence efforts' in investigating

Plaintiffs’ allegations were a whitewash[.]” [*Id.* at ¶ 143]. Plaintiffs also claim that the Defendants breached their duties by failing to implement a system of internal controls at the Company sufficient to detect and prevent the alleged fraud. [*Id.* at ¶ 146]. Plaintiffs allege these breaches damaged the Company. [*Id.* at ¶ 147]. Each of these arguments is addressed below.

As the Company is a Georgia corporation, pursuant to the internal affairs doctrine, Georgia law applies to Plaintiffs’ breach of fiduciary duty claim. *Edgar v. MITE Corp.*, 457 U.S. 624, 645 (1982); *NAF Holdings, LLC v. Li & Fung (Trading) Ltd.*, 772 F.3d 740, 743 (2d Cir. 2014), *certified question answered*, 118 A.3d 175 (Del. 2015). Georgia law has long recognized that directors and officers of a corporation owe fiduciary duties of care, good faith, and loyalty to the corporation and its shareholders. *See, e.g., Quinn v. Cardiovascular Physicians, P.C.*, 254 Ga. 216, 217 (1985) (“It is settled law that corporate officers and directors occupy a fiduciary relationship to the corporation and its shareholders, and are held to the standard of utmost good faith and loyalty.”) (citing *King Mfg. Co. v. Clay*, 216 Ga. 581 (1961)).<sup>35</sup>

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<sup>35</sup> Plaintiffs allege that Defendants breached a duty of candor to the Company and its shareholders. [App. 4, Complaint, at ¶ 136]. Rather than a standalone duty, the duty of candor is encompassed by other fiduciary duties. Since Georgia law does not directly address the duty of candor in this fashion, a Georgia court may look to Delaware law for guidance. *See, e.g., James & Jackson LLC v. Holyfield*, No. 2006CV124372, 2009 WL 7479360 (Ga. Super. Ct. May 7, 2009) (looking to Delaware law for the scope of recovery for a breach of duty of loyalty); *see also* Questioning Authority: The Critical Link between Board Power and Process, 38 J. Corp. L. 1, 3 (Fall 2012) (Noting that Delaware’s “corporate law enjoys quasi-national authority within the United States”); *Mullen v. Acad. Life Ins. Co.*, 705 F.2d 971, 973 n.3 (8th Cir. 1983) (“[C]ourts of other states commonly look to Delaware law . . . for aid in fashioning rules of corporate law.”). According to the Delaware Supreme Court, the duty of candor “does not import a unique or special rule of disclosure. It represents nothing more than the well-recognized proposition that directors of Delaware corporations are under a fiduciary duty to disclose fully and fairly all material information within the board’s control . . .” *Stroud v. Grace*, 606 A.2d 75, 84 (Del. 1992); *see also In re Orchard Enters., Inc. Stockholder Litig.*, 88 A.3d 1, 29 n.9 (Del. Ch. 2014) (“After *Stroud*, the prevailing Delaware terminology shifted from the “duty of candor” to the “duty of disclosure.”); *Laddin v. Odom*, No. 1:09-cv-01293-ODE (N.D. Ga. June 30, 2010) (dismissing claims for alleged breach of a duty of candor, finding no self-

**1. The Company Would Not Be Able To Show A Breach Of The Duty Of Loyalty Under The Facts Alleged.**

The Complaint does not include any allegations specific to a breach of the fiduciary duty of loyalty. Rather, they allege generally a violation of all fiduciary duties from the fact that (purportedly) Defendants knew of Plaintiffs' allegations of fraud, but, instead of properly investigating, condoned the behavior, did nothing, and (with regard to Dan Amos and Paul Amos) allowed the Company to retaliate against Plaintiffs Conroy and Varela. [App. 4, Complaint, at ¶¶ 137-145].

Under Georgia law, the duty of loyalty prohibits directors and officers from preferring their own interests to the interests of the corporation or using their role as directors or officers to obtain a personal advantage for themselves at the expense of the shareholders. *See* O.C.G.A. §§ 14-2-830; 14-2-842. They cannot engage in direct competition with the corporation, engage in self-dealing, commingle the corporation's assets and records with their own, or usurp "corporate opportunities" belonging to the corporation. *See, e.g., Enchanted Valley RV Resort, Ltd. v. Weese*, 241 Ga. App. 415, 422 (1999) (commingling of funds and records violates the duty of loyalty); *Brewer v. Insight Tech., Inc.*, 301 Ga. App. 694, 697-98 (2009) (explaining corporate opportunity doctrine). Plaintiffs, however, do not allege any self-dealing by the

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(continued...)

standing duties separate from the fiduciary duties of care and loyalty under Minnesota, or by reference Delaware, law); *In re Transkaryotic Therapies, Inc.*, 954 A.2d 346, 357 (Del. Ch. 2008) (stating that the duty of candor is "merely a specific application of the duties of care and loyalty"); *In re Walt Disney Co. Derivative Litig.*, 907 A.2d 693, 745 n.400 (Del. Ch. 2005) ("The Delaware Supreme Court has been clear that outside the recognized fiduciary duties of care and loyalty (and perhaps good faith), there are no other fiduciary duties. In certain circumstances, however, specific applications of the duties of care and loyalty are called for, such as . . . the duty of candor or disclosure.").

Defendants, commingling of the corporation's assets, or any usurpation of corporate opportunities.<sup>36</sup>

The Special Committee finds that neither the correspondence sent on behalf of Plaintiffs nor their Complaint points to any facts to support a breach of loyalty claim against any Defendant. Indeed, there are no specific allegations in the Complaint that any Director Defendant received any benefit deriving from any of the alleged misconduct. Further, the Special Committee's investigation revealed no evidence of any Defendant gaining financially from any of the Defendants resulting from the alleged wrongdoing or failure to disclose the wrongdoing.

**2. Any Claim By The Company For Breach Of The Duty Of Care Is Subject To Strong Defenses And Any Monetary Damages Are Likely Exculpated Under the Company's Articles of Incorporation.**

Under Georgia law, a director or officer is required to perform his duties "in good faith and with the degree of care of an ordinarily prudent person in a like position would exercise under similar circumstances." O.C.G.A. § 14-2-830(a) (directors); O.C.G.A. § 14-2-842(a) (officers). Officers and directors are presumed to make decisions in good faith by following a process pursuant to the exercise of ordinary care; that presumption, however, may be rebutted by evidence that such process constituted gross negligence, meaning a "gross deviation of the standard of care of a [director or officer] in a like position under similar circumstances." O.C.G.A. § 14-2-830(c) (directors); O.C.G.A. § 14-2-842(c) (officers).

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<sup>36</sup> Plaintiffs do not raise any allegation in Count V (the count for breach of fiduciary duty) relating to Paul Amos's stock sale. In any event, in its Initial Report the Special Committee addressed whether Mr. Amos's June 2017 sale of Company stock constituted a breach of fiduciary duty, and found that it did not.

Under Georgia law, an officer or director has a statutory right of reliance. In the performance of duties, an officer may rely upon other officers, employees, or agents of the corporation whom the officer or director “reasonably believes to be reliable and competent in the functions performed.” O.C.G.A. § 14-2-830(b)(1) (directors); O.C.G.A. § 14-2-842 (b)(1) (officers). The officer or director may also rely upon “[i]nformation, data, opinions, or statements provided” by employees of the corporation, legal counsel, public accountants, or others as to “matters involving the skills, expertise, or knowledge reasonably believed to be reliable and within such person’s professional or expert competence.” O.C.G.A. § 14-2-830(b)(2) (directors); O.C.G.A. § 14-2-842 (b)(2) (officers).

Georgia also recognizes the business judgment rule, which protects officers and directors from liability for good faith business decisions made in an informed and deliberate manner. As explained in *Fed. Deposit Ins. Co. v. Loudermilk*, 295 Ga. 579, 585–86 (2014), the business judgment rule:

generally precludes claims against officers and directors for their business decisions that sound in ordinary negligence, except to the extent that those decisions are shown to have been made without deliberation, without the requisite diligence to ascertain and assess the facts and circumstances upon which the decisions are based, or in bad faith. Put another way, the business judgment rule at common law forecloses claims against officers and directors that sound in ordinary negligence when the alleged negligence concerns only the wisdom of their judgment, but it does not absolutely foreclose such claims to the extent that a business decision did not involve ‘judgment’ because it was made in a way that did not comport with the duty to exercise good faith and ordinary care.

In addition, Georgia corporations are permitted to limit or eliminate a director’s personal liability to the corporation or its shareholders in certain circumstances. O.C.G.A. § 14-2-202. Specifically, an exculpatory clause in a corporation’s articles of incorporation enacted pursuant to Section 202 may eliminate a director’s personal liability for a breach of the duty of care to shareholders for money damages. O.C.G.A. § 14-2-202(b)(4). In addition, a Georgia

corporation is authorized to indemnify directors, officers, employees, and agents, subject to similar limitations. *See generally* O.C.G.A. §§ 14-2-851 *et seq.* The Georgia Code also grants directors and officers a statutory right to mandatory indemnification for their obligation to pay judgments, settlements, fines, penalties, and defense costs reasonably incurred if that director or officer is “wholly successful, on the merits or otherwise,” in defending a proceeding. O.C.G.A. § 14-2-852. This right accrues both in litigation brought by or on behalf of the corporation and litigation brought by third parties.<sup>37</sup>

The Company’s Articles of Incorporation mirror the Georgia protections and limitations. Specifically, the Articles state:

No director shall be personally liable to the corporation or its stockholders for monetary damages for any breach of duty of care or other duty as a director. Notwithstanding the foregoing, a director shall be liable to the extent provided by applicable law: (i) for the appropriation in violation of his duties of any business opportunity of the corporation; (ii) for acts or omissions not in good faith or which involve intentional misconduct or a knowing violation of law; (iii) for any action for which the director could be found liable pursuant to Section 14-2-154 of the Official Code of Georgia Annotated, or any amendment thereto or successor provision thereto; and (iv) for any transaction from which the director derived an improper personal benefit.

[App. 20, Amendment to the Articles of Incorporation, dated April 25, 1988].

Article VII of the Company’s Bylaws also provide for indemnification of any director, officer, employee, or agent who:

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<sup>37</sup> But there are exceptions to these protections. A director or officer cannot be exempted from liability arising from (1) misappropriation of corporate opportunities; (2) intentional misconduct and knowing violations of law; (3) unlawful distributions as defined in O.C.G.A. § 14-2-832; or (4) transactions from which he or she received an improper personal benefit. *See id.* §§ 14-2-856 (directors); 14-2-857 (officers). Furthermore, a Georgia corporation cannot attempt to limit a director or officer’s liability, nor indemnify them, for violations of the duty of loyalty as it can for violations of the duty of care. *See id.* §§ 14-2-856 (directors); 14-2-857 (officers) (permitting a corporation to exculpate directors for certain types of conduct, but not for conduct that results in the director obtaining an improper personal benefit). As noted above, the Special Committee did not find evidence of breach of the duty of loyalty.

was or is a party or is threatened to be made a party to any threatened, pending or completed action, suit or proceeding (including, but not limited to, any action, suit, or proceeding by or in the right of the Corporation), whether civil, criminal, administrative or investigative, by reason of the fact that he is or was a director, advisory director, officer, employee or agent of the Corporation or is or was acting at the request of the Corporation.

[App. 36, Amended and Restated Bylaws Article VII, Section 1]. In addition, Article VII provides that the Company “shall advance expenses to such person reasonably incurred in connection therewith, to the fullest extent permitted[.]” [*Id.* at Article VII]. The provisions relating to indemnification and advancement in the Company’s Bylaws generally track the language of the Georgia Code and indicate an intent that the Company be permitted to indemnify its directors and officers to the maximum extent permitted by Georgia law.

In addition to its factual finding that the allegations are without merit, the Special Committee does not believe that there is a viable breach of the duty of care claim here.

In regard to the efficacy of a duty of care claim, the Director Defendants relied on the advice of counsel and others, exercised their business judgment, and, in any event, would be exculpated. There are no allegations that any of the Director Defendants knew anything about the allegations prior to Mr. Joffe sending his letters. With regard to Dan Amos and Paul Amos, at most, the evidence is that they received letters from two of the Plaintiffs prior to the letters from Plaintiffs’ counsel. But both Dan Amos and Paul Amos explained that they receive countless e-mails and letters from sales associates and others about a variety of issues, and that their procedure has been to pass those e-mails and letters to the appropriate personnel in the compliance or legal departments. After that, they rely on the people in those departments to investigate and report to them if there is an issue. They never received any report that these allegations were material or evidenced any systemic problems at the Company. Indeed, the

opposite is the case. Based on the advice of counsel and others in the Company, Defendants exercised their business judgment in deciding not to disclose Plaintiffs' allegations.

In sum, the Special Committee has not seen evidence that would lead to a conclusion that any Defendant breached the duty of care. Further, even if such a claim could be established, it would not lead to the recovery of monetary damages, but would instead obligate the Company to incur significant costs in fulfilling the advancement and indemnification obligations discussed above.

### **3. The Company Would Most Likely Be Unable To Establish A Claim For Failure to Maintain Adequate Controls.**

In Delaware, a director can be liable for failing to implement an adequate system of controls. *In re Caremark Int'l Inc. Derivative Litig.*, 698 A.2d 959 (Del. Ch. 1996). Delaware consistently acknowledges that establishing liability under *Caremark* is a very high hurdle. *See In re Citigroup S'holder Derivative Litig.*, 964 A.2d 106, 125 (Del. Ch. 2009) (“[D]irector liability based on the duty of oversight ‘is possibly the most difficult theory in corporation law upon which a plaintiff might hope to win a judgment.’”) (quoting *In re Caremark Int'l Inc. Derivative Litig.*, 698 A.2d at 967). “To state a claim that directors have not satisfied their oversight duties, a complaint must plausibly allege that directors ‘utterly failed to implement any reporting or information system or controls,’ or that, ‘having implemented such a system or controls, consciously failed to monitor or oversee its operations thus disabling themselves from being informed of risks or problems requiring their attention.’” *In re Bank of Am. Corp. Sec., Derivative, & Emp. Ret. Income Sec. Act (ERISA) Litig.*, Master File No. 09 MD 2058(PKC), 2013 WL 1777766, at \*13 (S.D.N.Y. Apr. 25, 2013) (quoting *Stone v. Ritter*, 911 A.2d 362, 370 (Del. 2006)).

It is not clear whether a Georgia court would follow *Caremark*. See *F.D.I.C. v. Adams*, No. 1:12-cv-00726, 2013 WL 6044111, at \*7 (N.D. Ga. Apr. 10, 2013) (stating that it is unaware of any Georgia decision explicitly recognizing *Caremark*, but assumed, without deciding, that the plaintiff may bring such a claim under Georgia law in order to analyze whether the complaint contained sufficient allegations). Even if *Caremark* were applicable, however, the allegations fall short of what is required under Delaware law.

Here, the Complaint simply states that there was a breakdown in controls, and provides no facts to support that assertion other than the supposition that the Company's investigation was a "whitewash." The Company investigated and advised management and the directors that there were no material issues to be addressed at the Board level. The Company's controls include the services provided by SIU and Aflac Trust, which monitor an ethics hotline and website to address and investigate claims brought to their attention, as well as the internal audit department. In reliance on the investigation performed in accordance with the existing controls, Defendants understood Plaintiff's various allegations to lack merit. The directors rejected the allegations not because there was a breakdown in controls, but because the directors believed the allegations were immaterial or without merit based upon the conclusions reached from the appropriate execution of existing controls.

In addition, the Complaint does not point to any reports received by the Board or the Audit and Risk Committee that internal controls may have been deficient. Conclusory allegations that the Board failed to act on so-called warning signs are not sufficient to state a claim. See *id.*; see also *Guttman v. Huang*, 823 A.2d 492, 506–07 (Del. Ch. 2003) ("In this case, the plaintiffs have not come close to pleading a *Caremark* claim. Their conclusory complaint is empty of the kind of fact pleading that is critical to a *Caremark* claim, such as contentions that

the Company lacked an audit committee, that the Company had an audit committee that met only sporadically and devoted patently inadequate time to its work, or that the audit committee had clear notice of serious accounting irregularities and simply chose to ignore them or, even worse, to encourage their continuation.”). The Complaint fails to plead any facts that the Defendants were made aware of any deficiencies in internal controls, let alone the extreme set of facts required under *Caremark*.

**4. The Company Would Not Be Likely To Prevail In A Claim Against The Defendants Relating To The Stock Repurchases.**

To the extent that Plaintiffs challenge the share repurchase as a breach of fiduciary duty, they make no particularized allegations regarding the Board’s reason for approving a stock repurchase, nor do they allege that the stock repurchase was approved dishonestly or in bad faith. The Special Committee finds that the stock repurchase was motivated, as Dr. Knapp explained, by a desire to return value to shareholders as part of the Company’s three primary capital deployment options. Specifically, Dr. Knapp explained that the Company does three things to increase shareholder value: increase dividends, invest back into the Company (*e.g.*, through IT, cybersecurity, or training), and repurchase its own stock. Plaintiffs advance no particularized allegations to show that the reasons expressed by Dr. Knapp are not valid, and make no effort to show that the Board was not adequately informed in approving any stock repurchase. They have failed to show that the stock repurchases lacked “any rational business purpose.” *See F5 Capital v. Pappas*, 856 F.3d 61, 87 (2d Cir. 2017). Therefore, Plaintiffs cannot show that the Defendants did not authorize the repurchase through the proper exercise of their business judgment.

**E. The Unjust Enrichment Claim Is Not Supported By The Facts.**

Finally, Plaintiffs allege that Paul Amos was unjustly enriched when he purportedly received \$17 million for the sale of shares “in violation of securities laws and in breach of his

fiduciary duties.” [App. 4, Complaint, at ¶ 149]. The Special Committee finds that Plaintiffs’ allegations of unjust enrichment are unfounded.

To plead a claim for unjust enrichment under Georgia law, Plaintiffs must allege: “(1) a benefit has been conferred, (2) compensation has not been given for receipt of the benefit, and (3) the failure to so compensate would be unjust.” *Clark v. Aaron’s, Inc.*, 914 F. Supp. 2d 1301, 1309 (N.D. Ga. 2012); *Crook v. Foster*, 333 Ga. App. 36, 39 (2015) (stating that unjust enrichment is an equitable concept applied when there is no contract in place, and a benefited party ought to return or compensate for the benefit conferred); *see also Engram v. Engram*, 265 Ga. 804, 806 (1995).

Here, Plaintiffs do allege that a benefit has been conferred, specifically that Paul Amos received \$17 million for the sale of his shares. As discussed in the Initial Report, this was an exercise of his options received during his time as an officer and director of the Company. [See, e.g., App. 17 Initial Report, at 32]. Indeed, his options were set to expire if he did not exercise them within three months of his resignation. [App. 37, Paul S. Amos, II’s Separation Agreement, at 2]. Therefore, contrary to the elements of unjust enrichment, compensation *has* been given for this benefit because Paul Amos received his options in exchange for his work as an officer and director of the Company. [See App. 6, 2017 Proxy Statement]. Additionally, the Special Committee does not find that he was in possession of material, nonpublic information when he sold his shares or that this sale was otherwise improper. And, as discussed in the Initial Report and above, Paul Amos followed proper procedures and received clearance from the Company to exercise his options, and thus was not “unjustly” enriched. *See S.E.C. v. Collins*, 2003 WL 21196236 (N.D. Ill. May 21, 2003) (stating that in order to find unjust enrichment there must be evidence that defendants violated securities laws or otherwise acted improperly).

**F. The Special Committee Finds That Pursuing The Claims Raised In The Complaint Is Not In The Best Interests Of The Company.**

The Special Committee’s ultimate task is to determine whether it is in the best interests of the Company to pursue a derivative action against Defendants, or some other remedial action, in light of all circumstances. *See* OCGA § 14-2-744(a) (“The court may dismiss a derivative proceeding if, on motion by the corporation, the court finds that [a special litigation committee] has made a determination in good faith after conducting a reasonable investigation upon which its conclusions are based that the maintenance of the derivative suit is not in the best interests of the corporation.”). In addition to the legal considerations, the Special Committee may also consider any “ethical, commercial, promotional, public relations, employee relations, and fiscal factors[.]” *See Peller v. The Southern Co.*, 707 F. Supp. 525, 530 (N.D. Ga. 1988) (citing *Kaplan v. Wyatt*, 484 A.2d 501, 508–09 (Del. Ch. 1985)). “The rationale to be applied at the second step is that of public policy and the spirit of the law as well as, from a pure business standpoint, the overriding best interests of the corporation and its shareholders when weighing a good faith recommendation of dismissal made by the independent Committee . . . [i]n applying its own independent business judgment to this second-step analysis . . . it is necessary that the Court, in addition to considering matters of law and public policy, consider also such ethical, commercial, promotional, public relations, employee relations and fiscal factors as may be involved in a given situation.” *Kaplan*, 484 A.2d at 508–09 (citing *Zapata Corp. v. Maldonado*, 430 A.2d 779, 788 (Del. 1981)). “We recognize that the final substantive judgment whether a particular lawsuit should be maintained requires a balance of many factors ethical, commercial,

promotional, public relations, employee relations, fiscal as well as legal.” *Zapata Corp.*, 430 A.2d at 788 (quoting *Maldonado v. Flynn*, 485 F. Supp. 274, 285 (1980)).<sup>38</sup>

The Special Committee concludes that the claims referenced in the various letters and the Complaint are without merit. It further finds that the alleged misconduct has not harmed the Company.

Additionally, the Special Committee concludes that, based on a cost-benefit analysis, the pursuit of these claims is not in the best interests of the Company. As an initial matter, the Company would likely incur substantial legal expenses in connection with the pursuit of these claims. *See Abella v. Universal Leaf Tobacco Co.*, 546 F. Supp. 795, 801 n.13 (E.D. Va. 1982) (noting that committee concluded that the benefit to be derived from a successful decision on the merits was outweighed by, *inter alia*, the “[l]arge attorneys’ fees and expenses”); *Mills v. Esmark, Inc.*, 573 F. Supp. 169, 172 n.2 (N.D. Ill. 1983) (noting committee’s recommendation to seek dismissal based on, *inter alia*, the “cost of pursuing the claims”); *Lewis v. Fuqua*, 502 A.2d 962, 971 (Del. Ch. 1985) (observing expense was one of the “decisive factors” in the committee’s recommendation that the Company move for dismissal of the derivative action). Furthermore, the Company would also be obligated to advance expenses on behalf of the Defendants for their legal fees and expenses arising from the defense of the derivative claims. *See id.* (citing possible obligation to indemnify the defendant directors among the “decisive factors” in the committee’s recommendation that the corporation move for dismissal of the derivative litigation).

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<sup>38</sup> Though Georgia law does not outline the exact factors it uses to determine whether an action is in the best interests of a company, it is likely to look to Delaware law for guidance. *See supra*, at 94 n.35.

The Special Committee also finds that the prosecution of these claims would likely be an unnecessary distraction to the officers' and directors' abilities to manage the corporation. *Abella*, 546 F. Supp. at 801 n.13; *see also Stein v. Bailey*, 531 F. Supp. 684, 690 (S.D.N.Y. 1982) (considering, *inter alia*, the cost of litigation in terms of its "disruption of management"); *Lewis*, 502 A.2d at 971 (finding that disruptive effect on corporate management was another one of the "decisive factors" in committee's recommendation that the corporation move for dismissal of the derivative action).

Given the low, if not non-existent, probability of any recovery, the Special Committee concludes the monetary, and other costs that would flow from the prosecution of these claims, far outweighs any potential benefits. *See Lewis*, 502 A.2d at 971 (noting that the low probability of recovery and the possibility of a meager recovery were also among the "decisive factors" in the committee's recommendation that the corporation move for a dismissal of the derivative action); *Mills*, 544 F. Supp. at 1282 n.2 (noting committee's determination that continuation of the litigation would not advance the best interests of the corporation was based on, *inter alia*, the committee's conclusion that the corporation's "chance of succeeding on the merits . . . would be too small to justify the expenditure of substantial legal fees").

For these reasons, the Special Committee concludes that the prosecution of these claims is not in the best interests of the corporation.

## **VII. CONCLUSION**

In light of all circumstances, the Special Committee finds that bringing a derivative action would not be in the best interests of the Company or its shareholders. The Special Committee has determined to reject the demand.

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**On behalf of the**

**SPECIAL COMMITTEE OF THE BOARD  
OF DIRECTORS OF AFLAC INCORPORATED**

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