

A low-angle, upward-looking photograph of several modern skyscrapers with glass facades. The sky is a mix of purple, blue, and orange, suggesting a sunset or sunrise. The buildings are partially illuminated from within, showing warm yellow lights. The perspective creates a sense of height and scale.

Vinson & Elkins

TEN HOT TOPICS & ONE REMINDER:

DEVELOPMENTS IN GOVERNANCE AND DISCLOSURE
SUMMER 2018

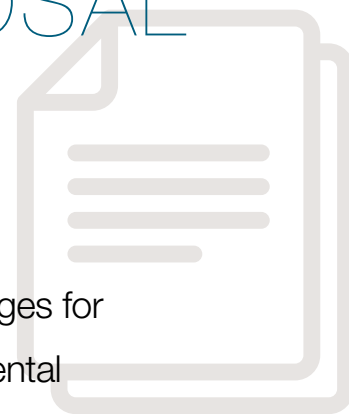
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IN ADDITION TO THE TOPICS COVERED MORE EXTENSIVELY IN THIS ISSUE, HERE ARE A FEW SNAPSHOTS OF OTHER TOP DEVELOPMENTS:

- In April 2018, the Delaware Court of Chancery **permitted claims of waste and bad faith to continue** where the board of CBS Corporation had continued to pay its former chairman compensation, despite his incapacity.
- In April 2018, Institutional Shareholder Services Inc. ("ISS") updated its **U.S. Proxy Voting Research Procedures and Policies FAQs**, including new questions: Can a company get a copy of its ISS proxy report? Can a company send the ISS proxy report to its shareholders or other parties? What happens if the proxy report contains a factual error? How can a company request an engagement with the U.S. research analysts? and Who should I contact with questions on ISS U.S. voting policies?
- In March 2018, **the SEC charged** the former chief information officer of a U.S. business unit of Equifax with insider trading in advance of the company's September 2017 data breach announcement. According to the **SEC's complaint**, despite the fact that the officer was not initially informed of the breach, because he guessed that the company had been involved in a data breach and subsequently sold company securities, he is subject to insider trading liability.
- In April 2018, the National Institute of Standards and Technology published an **updated version** of its voluntary risk management framework consisting of standards, guidelines, and best practices for managing cybersecurity-related risks.

INTRODUCTION: 2018 PROXY AND PROPOSAL SEASON UPDATE



The 2018 proxy and proposal season¹ brought a fresh wave of challenges for companies, but also brought a few small measures of relief. Environmental and social proposals continued to represent approximately 40% of submitted proposals, based on data from Institutional Shareholder Services Inc.

(“ISS”),² with proposals regarding climate change or requesting the adoption of greenhouse gas emissions goals or disclosure and proposals regarding boardroom diversity among the most frequently submitted environmental and social proposals. While a record number of environmental and social proposals received strong investor support, the staff (the “Staff”) of the Securities and Exchange Commission’s (the “SEC”) Division of Corporation Finance (the “Division”) also scaled back the inclusion of a number of such proposals in proxy statements by concurring with exclusion of those proposals on the basis that they related to the company’s “ordinary business.”

¹ The “2018 proxy and proposal season” refers to the period of time beginning October 1, 2017 and ending June 1, 2018, during which most public companies receive shareholder proposals, submit no-action request letters, file their proxy statements for their annual shareholder meetings and hold their annual shareholder meetings. Proposals received for the 2018 proxy season are proposals received for any meeting occurring in 2018.

² We have made minor adjustments to the available ISS data to address observable errors in that data.

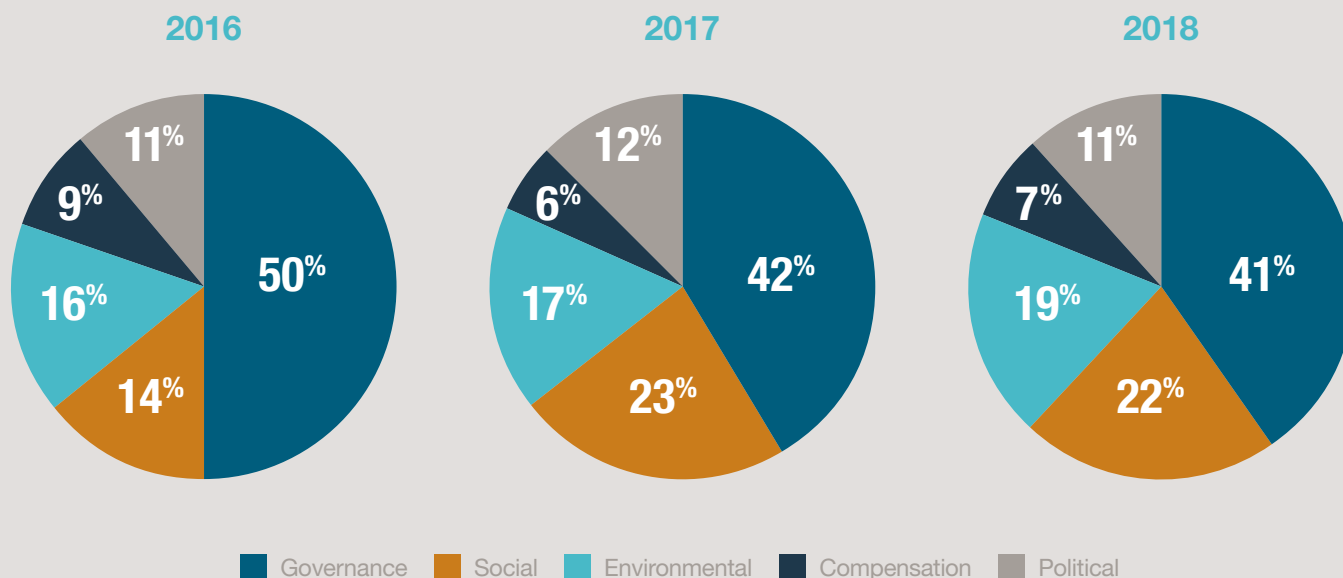
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THREE-YEAR
SHAREHOLDER
PROPOSAL TRENDS

Based on ISS data, over the last two years the percentage of shareholder proposals submitted that pertain to more traditional governance matters (e.g., shareholder rights and board composition) and the number of shareholder proposals pertaining to environmental or social matters (e.g., climate change and human rights) have been nearly equal. When evaluating the last three years of data, there was a marked decrease in governance proposals and corresponding increase in environmental and social proposals between 2016 meetings and 2017 meetings. For 2018 meetings, approximately 40% of shareholder proposals reported by ISS related to governance matters, while 41% related to social or environmental matters, and for 2017 meetings, approximately 42% of shareholder proposals related to governance matters, while approximately 40% of shareholder proposals related to environmental or social matters. In comparison, for 2016 meetings, approximately 50% of shareholder proposals related to governance matters, while approximately 30% of shareholder proposals related to environmental or social matters.

Over the last three years, certain subcategories of shareholder proposals — in particular, proposals relating to climate change, greenhouse gas (“GHG”) emissions and diversity-related matters — have been well represented. There has been a significant fluctuation among the top governance proposals

MEETING PROPOSALS



submitted over the past three years, and while proxy access proposals are no longer as well represented as they were for 2016 meetings, they remain relevant, as do “fix” proxy access proposals (i.e., proposals requesting that the board make specific changes to a previously adopted proxy access provision). The following subcategories of proposals have been the most recently submitted over the last three years:

	2016	2017	2018
Environmental	<ul style="list-style-type: none"> 31 proposals on adopting GHG goals or disclosure 26 proposals on climate change-related risks 25 on renewable energy 	<ul style="list-style-type: none"> 33 proposals on climate change-related risks 31 proposals on adopting GHG goals or disclosure 27 proposals on the environmental impact of the business 	<ul style="list-style-type: none"> 38 proposals on adopting GHG goals or disclosure 27 proposals on issuing a sustainability report 21 proposals on climate change-related risks
Social	<ul style="list-style-type: none"> 26 proposals on board diversity 15 proposals on human rights violations 13 proposals on gender pay gap 	<ul style="list-style-type: none"> 33 proposals on board diversity 22 proposals on gender pay gap 21 proposals on preparing a diversity report 	<ul style="list-style-type: none"> 29 proposals on board diversity 25 proposals on gender pay gap 23 proposals on preparing a diversity report
Governance	<ul style="list-style-type: none"> 195 proposals on adopting proxy access 55 proposals on independent board chair 30 proposals on reducing supermajority vote requirements 	<ul style="list-style-type: none"> 86 proposals on adopting proxy access 48 proposals on independent board chair 30 proposals on amending existing proxy access provisions 	<ul style="list-style-type: none"> 74 proposals on reducing the threshold for/permitting shareholders to call a special meeting 53 proposals on independent board chair 42 proposals on permitting shareholders to act by written consent
Compensation	<ul style="list-style-type: none"> 24 proposals on equity award vesting 14 proposals on using particular performance metrics 13 proposals on adopting stock retention/holding periods 	<ul style="list-style-type: none"> 14 proposals on using particular performance metrics 12 proposals on equity award vesting 6 proposals on clawbacks 	<ul style="list-style-type: none"> 22 proposals on using particular performance metrics 12 proposals on clawbacks 8 proposals on equity award vesting
Political	<ul style="list-style-type: none"> 48 proposals on reporting lobbying payments 39 proposals on reporting political contributions 7 proposals on membership in lobbying organizations 	<ul style="list-style-type: none"> 49 proposals on reporting lobbying payments 36 proposals on reporting political contributions 16 proposals on reporting political activity and risks 	<ul style="list-style-type: none"> 47 proposals on reporting lobbying payments 37 proposals on reporting political contributions 4 proposals on charitable contributions

The number of environmental proposals receiving significant shareholder support has been slowly increasing over the last three years. Based on ISS data, shareholder proposals receiving majority shareholder support³ during the last three years were:

2016 MEETINGS	2017 MEETINGS	2018 MEETINGS (SO FAR)
<p>2 environmental proposals</p> <ul style="list-style-type: none"> Kellogg Company, support for animal welfare improvements, 98.2% of votes cast WPX Energy, Inc., report on methane emissions, 50.8% of votes cast 	<p>4 environmental proposals</p> <ul style="list-style-type: none"> Exxon Mobil Corp., report on climate change policies, 62.1% of votes cast Pioneer Natural Resources Company, sustainability report, 52.1% of votes cast PPL Corp., portfolio impacts of policy to meet 2 degree scenario, 56.8% of votes cast Occidental Petroleum Corp., portfolio impacts of policy to meet 2 degree scenario, 67.3% of votes cast 	<p>7 environmental proposals</p> <ul style="list-style-type: none"> Ameren Corp., risks associated with coal ash, 53.2% of votes cast Anadarko Petroleum Corp., report on stranded carbon assets, 53.0% of votes cast Genesee & Wyoming Inc., GHG emissions reduction goals, 57.2% of votes cast Kinder Morgan, Inc., portfolio impact of policies to meet 2 degree scenario, 59.7% of votes cast Kinder Morgan, Inc., sustainability report, 60.4% of votes cast The Middleby Corp., sustainability report, 57.2% of votes cast Range Resources Corp., report on methane emissions, 50.3% of votes cast
<p>3 social proposals</p> <ul style="list-style-type: none"> eBay Inc., gender pay gap report, 51.2% of votes cast FLEETCOR Technologies, Inc., report on plans to increase board diversity, 72.4% of votes cast J.B. Hunt Transport Services, Inc., amend EEO policy to prohibit discrimination based on sexual orientation, 54.7% of votes cast 	<p>2 social proposals</p> <ul style="list-style-type: none"> Cognex Corp., board diversity policy, 62.8% of votes cast Hudson Pacific Properties, Inc., board diversity report, 84.8% of votes cast 	<p>2 social proposals</p> <ul style="list-style-type: none"> Depomed, Inc., report on governance measures related to opioids, 62.3% of votes cast Sturm, Ruger & Company, Inc., report on gun violence, 68.8% of votes cast
<p>82 governance proposals</p>	<p>59 governance proposals</p>	<p>25 governance proposals</p>
<p>1 executive compensation proposal</p> <ul style="list-style-type: none"> Bed Bath & Beyond Inc., submit severance agreement to shareholders, 59.9% of votes cast 	<p>No executive compensation proposals</p>	<p>No executive compensation proposals</p>
<p>2 political contributions proposals</p> <ul style="list-style-type: none"> Fluor Corp., report on political contributions, 61.9% of votes cast NiSource Inc., report on political contributions, 50.3% of votes cast 	<p>No political contribution proposals</p>	<p>1 charitable contributions proposal</p> <ul style="list-style-type: none"> McDonald's Corp., report on charitable contributions, 97.1% of votes cast

³ Majority shareholder support is measured by the number of votes cast "for" the proposal divided by the number of votes cast "for" the proposal plus the number of votes cast "against" the proposal, without regard to abstentions or broker non-votes, regardless of the company's specific voting standard.

Upcoming V&E CLE: September 20, 2018

THE NEW GOVERNANCE: NAVIGATING THE RISING ESG TIDE

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We saw a number of emerging shareholder proposals during the 2018 proxy and proposal season. Specifically, there were approximately:

- 10 proposals requesting a report on governance proposals implemented to monitor and manage financial and reputational risks related to the opioid crisis in the U.S. and seven proposals touching upon drug prices;
- six proposals requesting a report on “truthful” news operations;
- three proposals touching upon cybersecurity and cybersecurity risk matters; and
- two proposals requesting reports on gun violence or safety.

In addition, although not entirely new to the 2018 proxy and proposal season, there also were approximately three proposals that touched upon corporate tax practices.

As a reminder, there is currently a bill before the House Financial Services Committee, which would increase the ownership threshold under Rule 14a-8 from \$2,000 worth to 1%, and would also increase the resubmission thresholds and impose restrictions on “proposals by proxy.”

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2018 NO-ACTION
REQUEST LETTER
TRENDS

As we discussed in our [November 6, 2017 article](#), the SEC kicked off the 2018 proxy and proposal season by issuing new [Staff Legal Bulletin No. 14I](#) (“SLB 14I”). Therefore, the 2018 proxy and proposal season was the first time we saw SLB 14I in action. SLB 14I addressed the Staff’s notoriously complex “ordinary business” exception under Rule 14a-8(i)(7), and permits companies’ boards of directors to weigh in on whether a particular proposal raises a policy issue and the significance of that issue to the company. SLB 14I also addressed the “economic relevance” exception under Rule 14a-8(i)(5), the degree to which shareholders may submit proposals through a representative, and the use of graphs and images in shareholder proposals.

There have been approximately 252 no-action request letters submitted to the SEC for 2018 meetings to date. The Staff has refused to concur with the arguments presented in approximately 67 of those letters and has concurred with exclusion in approximately 128 instances. Approximately 50 of those letters pertained to proposals that were ultimately withdrawn, and a few letters have yet to be answered or have received Staff responses that permitted revision or provided for only a portion of the proposal to be excluded. Of the letters that were responded to favorably, approximately 45 were instances in which the Staff concurred with exclusion on the basis of (i)(7) (the “ordinary business” exclusion) and approximately 41 were instances in which the Staff concurred with exclusion on the basis of (i)(10) (the “substantial implementation” exclusion). The (i)(7) and (i)(10) bases, together with various procedural bases (which, for 2018 meetings, represented 19 exclusions) remain the most successful bases for companies to use in seeking to exclude Rule 14a-8 proposals.

NOTEWORTHY CONCURRENCES

- The Staff concurred with EOG Resources’ request to exclude a proposal asking that the company adopt company-wide, quantitative, time-bound targets for reducing greenhouse gas emissions and issue a report discussing its plans and progress towards achieving those targets on (i)(7) grounds. The company argued, among other things, that the proposal sought to micromanage the company and cited [Apple, Inc. \(avail. Dec. 5, 2016\)](#). The company also included a discussion of the company’s board’s analysis of the proposal. In response, the Staff stated that the proposal sought “to micromanage the [c]ompany by probing too deeply into matters of a complex nature upon which shareholders, as a group, would not be in a position to make an informed judgment. ([EOG Resources, Inc. \(avail. Feb. 26, 2018\)](#)). In [Paypal Holdings, Inc. \(avail. Mar. 6, 2018\)](#), the Staff concurred with exclusion with a similar proposal, notwithstanding the fact that the company chose not to include a discussion of its board’s analysis of the proposal.

- The Staff concurred with Dunkin' Brands Group's request to exclude a proposal asking that the board issue a report assessing the environmental impacts of continuing to use K-Cup Pods brand packaging on (i)(5) grounds. The company argued that the proposal related to operations that account for less than 5% of the company's total assets at the end of its most recent fiscal year. The company also included a discussion of their board's analysis of the proposal and process for assessing its significance, in accordance with SLB 14I. In concurring with exclusion, the Staff noted that the proposal's "significance to the [c]ompany's business is not apparent on its face, and ... the [p]roponent has not demonstrated that it is otherwise significantly related to the [c]ompany's business." (**Dunkin' Brands Group, Inc. (avail. Feb. 22, 2018)**).
- On the basis of Rule 14a-8(i)(9), the Staff concurred with the exclusion of a number of special meeting proposals on the grounds that shareholders could not logically vote in favor of both a company proposal ratifying the company's current position and the special meeting proposal calling for a lower ownership threshold. See, for example, **ITT Inc. (avail. Feb. 22, 2018)**.

NOTEWORTHY DENIALS

- The Staff was unable to concur with Apple's request to exclude a proposal asking that Apple "establish a Human Rights Committee to review, assess, disclose, and make recommendations to enhance Apple's policy and practice on human rights" on (i)(7) grounds. The Staff stated that it was "unable to conclude, based on the information presented in your correspondence, including the discussion of the board's analysis on this matter, that this particular proposal is not sufficiently significant to the Company's business operations such that exclusion would be appropriate." (**Apple Inc. (avail. Dec. 21, 2017 (Zhao))**).
- The Staff was unable to concur with AmerisourceBergen's request to exclude a proposal asking that the company report on "the governance measures ... implemented since 2012 to more effectively monitor and manage financial and reputational risks related to the opioid crisis in the U.S." on (i)(7) grounds. The Staff stated that it was "unable to conclude, based on the information presented in your correspondence, including the discussion of the board's analysis on this matter, that this particular proposal is not sufficiently significant to the Company's business operations such that exclusion would be appropriate." (**AmerisourceBergen Corp. (avail. Jan. 11, 2018)**).
- The Staff was unable to concur with Entergy's request to exclude a proposal asking that the company prepare a report "describing how the Company could adapt its enterprise-wide business model to significantly increase deployment of distributed-scale non-carbon-emitting electricity resources as a means of reducing greenhouse gas emissions consistent with limiting global warming to no more than 2 degrees Celsius" on (i)(7) grounds. The Staff stated that although the company's "discussion of the board's analysis sets forth several factors the board considered in evaluating the [p]roposal" the company had "not provide[ed] a sufficient level of detail to reach a determination that exclusion of the [p]roposal is appropriate." (**Entergy Corp. (avail. Mar. 14, 2018)**).
- The Staff was unable to concur with Eli Lilly's request to exclude a proposal asking the company to prepare a report on lobbying contributions and expenditures on (i)(5) and (i)(7) grounds. The Staff noted that the company's "shareholders have voted on a similar proposal that received approximately 25% of the vote" and because the company's discussion of its "board's analysis [did] not adequately address these voting results," the Staff was unable to concur with exclusion. (**Eli Lilly and Company (avail. Mar. 2, 2018)**). See also, **Alliant Energy Corp. (avail. Mar. 30, 2018)**.

- The Staff was unable to concur with General Motor's request to exclude a proposal asking for a report describing whether the company's fleet greenhouse gas emissions through 2025 will increase on (i)(7) grounds. The Staff specifically noted that the company's no-action request did "not include a discussion of the board's analysis" and thus, as a result, the Staff did not have the benefit of the board's views on these matters. ([General Motors Company \(avail. Apr. 18, 2018\)](#)). See also, [Verizon Communications Inc. \(avail. Mar. 8, 2018\)](#).
- The Staff stopped permitting exclusion on the basis of (i)(3) (i.e., vague and misleading) proposals that include a reference to exchange rules. See, [Sears Holdings Corp. \(avail. Feb. 9, 2018\)](#); [Bloomin' Brands, Inc. \(avail. Feb. 9, 2018\)](#).

SHAREHOLDER PROPOSAL AND NO-ACTION TRENDS: WHAT DO THEY MEAN?

- The prevalence of environmental and social proposals, and investor interest in such topics, continues to rise, both with respect to the number of proposals submitted, and the level of shareholder support. Therefore, companies, particularly those in energy and energy-related industries, should consider setting time aside in the board and upper-level management calendars for discussions regarding these matters.
- While S&P 500 companies remain the most likely to receive Rule 14a-8 proposals, increasingly small and mid-cap companies are beginning to receive proposals as well, and small and mid-cap companies can always be the targets of activists. Therefore, it is never too early to begin considering how to address investor concerns, including those relating to "softer" governance matters, including environmental and social matters.
- While the number and subject matters of Rule 14a-8 proposals fluctuates from year to year, the complexity of no-action request letters only increases; therefore, if a company receives a Rule 14a-8 proposal, it is imperative that it involve sophisticated counsel.
- While there are currently legislative revisions to Rule 14a-8 on the table, companies should not assume that these changes will be enacted.

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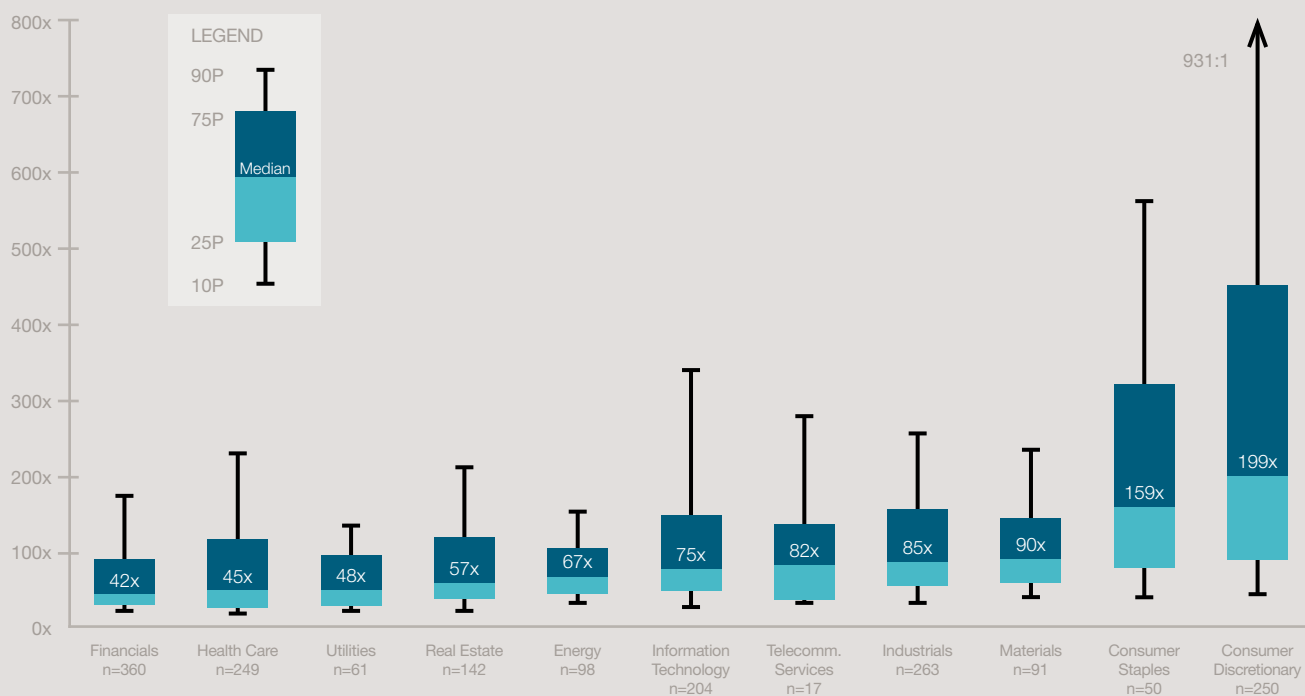
PAY RATIO
DISCLOSURE
DEVELOPMENTS

As we discussed in our [January 30, 2018 blog post](#), the 2018 proxy season was the first time many companies were required to comply with the SEC's pay ratio disclosure rule, which was adopted by the Commission in 2015 pursuant to the Dodd-Frank Act. In an [April 18, 2018 survey](#), Deloitte Consulting analyzed the CEO pay ratio disclosures of 294 S&P 500 companies from their proxy statement filings as of April 10, 2018. According to Deloitte's article:

- Median pay ratio is 153:1.
- Median employee's total annual compensation is \$70,867.
- 21% of companies disclose information about the median employee's employment status, geographic location, and/or role.
- Larger companies (in terms of revenue) had higher median ratios than smaller companies; however, the median employee's pay did not correlate with revenue size.
- 51% of companies chose a date other than the fiscal year end as the measurement date.
- The "consistently applied compensation measure" used to identify the median employee varied significantly, with total cash compensation used by 32%, base pay and wages at 23%, W-2 wages at 20%, and total direct compensation at 18%.
- Only 8% of companies used statistical sampling.
- Only one company adjusted pay for the cost of living.
- 16% of companies added health benefits to total annual compensation.
- 81% of companies placed the CEO pay ratio disclosure immediately following the termination tables, while only 4% included it in the CD&A.

According to a [May 23, 2018 study](#) by Semler Brossy, the median ratio of the 224 S&P 500 reporting as of May 21, 2018 is more than twice that of the 845 Russell 3000 reporting as of the same date. The CEO pay ratio is inversely correlated with median employee compensation — companies with bottom quartile median employee compensation have significantly higher ratios. The composition of a company's workforce, including whether it uses seasonal or part-time workers, is a primary driver of high CEO pay ratios at the 75th and 90th percentiles in the Consumer Staples and Consumer Discretionary sectors, whereas highly-paid CEOs in the Information Technology sector are driving high CEO pay ratios at the 90th percentile. Of the S&P 500 and Russell 3000 companies that had disclosed say-on-pay voting results as of May 21, there is an inverse relationship between say-on-pay support and CEO pay ratio among S&P 500 constituents and say-on-pay support declines among Russell 3000 companies that disclose ratios above the 75th percentile.

RUSSELL 3000 CEO PAY RATIO VARIANCE BY GICS SECTOR



Source: 2018 Say on Pay and Proxy Results, Russell 3000, Semler Brossy (May 23, 2018).

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The [V&E] team is outstanding. Key strengths are knowledge, tenacity, enthusiasm and being a pleasure to deal with.

– Chambers Global 2018

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#METOO DURING MEETING SEASON



As we discussed in our [March 2018 webcast](#) on boardroom diversity, the #MeToo movement has raised questions about corporate boards' oversight of employment and labor-related risks, and has also increased the stakes for companies that do not effectively implement appropriate processes and procedures around anti-harassment training and internal reporting and investigations. During the 2018 proxy and proposal season, a number of public companies found themselves under a particularly unforgiving spotlight during their proxy preparation and solicitation periods.

In February 2018, about two months before filing its preliminary proxy statement, Lululemon Athletica Inc. [announced](#) the departure of their Chief Executive Officer, Laurent Potdevin, stating that the company "expects all employees to exemplify the highest levels of integrity and respect for one another" and that "Mr. Potdevin fell short of these standards of conduct." The resignation followed a lawsuit alleging that Lululemon knowingly allowed a manager who had been the subject of sexual harassment complaints to continue working for the company. Also in February 2018, Stephen A. Wynn resigned as Chairman of the Board and Chief executive Officer of Wynn Resorts, Limited. In his statement accompanying the company's [press release](#), Mr. Wynn stated that he had found himself "the focus of an avalanche of negative publicity," and that he therefore could not "continue to be effective in [his] current roles." The resignation followed allegations that Mr. Wynn had harassed female employees for decades, according to an in-depth Wall Street Journal investigation, resulting in a more than 8% decline in the company's stock price in the days immediately following the news of the allegations, and the initiation of a suit by New York State Comptroller Thomas DiNapoli against the company's board of directors. The resignation was not enough to halt the activist campaign waged by Mr. Wynn's ex-wife, Elaine Wynn. A New York-based real estate investment trust, Cedar Realty Trust, similarly faced an activist campaign brought by Snow Park Capital Partners while confronting a sexual harassment suit filed against their Chief Executive Officer.

#METOO DURING MEETING SEASON:
WHAT DOES IT MEAN?

As discussed in our [October 2017 blog post](#), there are practical steps companies can take in addressing #MeToo pressure and issues regarding gender parity. For creative ideas and recommendations regarding addressing gender dynamics, see the [NACD article on boardroom diversity](#), this recent [webcast by Deloitte and V&E on boardroom diversity](#), or contact your V&E lawyers for upcoming trainings.

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RECENT INVESTOR
POSITIONS

As we touched upon in our [December 2017 article](#), in recent years, institutional investors have taken interest in a number of “softer” governance issues — including board diversity and climate change. During the 2018 proxy and proposal season, this trend continued. In March 2018, BlackRock issued a [short white paper](#) on the firm’s approach to engagement on human capital management (“HCM”). The white paper built on BlackRock CEO Larry Fink’s [2018 annual letter to CEOs](#), in which, as we discussed in our [January 2018 article](#), Fink stated that “[t]o prosper over time, every company must not only deliver financial performance, but also show how it makes a positive contribution to society. Companies must benefit all of their stakeholders, including shareholders, employees, customers, and the communities in which they operate.” The white paper builds on this by stating that “[a] company’s approach to HCM — employee development, diversity and a commitment to equal employment opportunity, health and safety, labor relations, and supply chain labor standards, amongst other things — will vary across sectors but is a factor in business continuity and success.” In the white paper, BlackRock states that it is a member of the Investor Advisory Group of the Sustainability Accounting Standards Board, which provides industry-specific HCM metrics, and sets forth the specific HCM matters that BlackRock is interested in engaging with companies on.

In February 2018, State Street Global Advisors (“SSGA”) released [a letter to the board members at S&P 500 companies](#) encouraging companies to comply with the investor’s governance principles. The [governance principles](#) referenced in the letter are those released by the Investor Stewardship Group, a collective of some of the largest U.S.-based institutional investors and global asset managers and their international counterparts. In the letter, Richard Lacaille, SSGA’s Chief Investment Officer, points to the firm’s 2016 focus on governance issues regarding board independence and effectiveness and the firm’s 2017 call for companies to incorporate environmental and social sustainability into their long-term strategies and increase board diversity, and states that, while SSGA has seen significant impact from those two initiatives, the firm will now take voting action where companies are unable to explain adequately why they are not compliant with the investor’s governance principles.

There were also a few companies that received targeted communications from institutional shareholders during the 2018 proxy and proposal season. For example, in January 2018, JANA Partners LLC and the California State Teachers’ Retirement System (“CalSTERS”) issued [a letter](#) to Apple Inc. encouraging the company to “offer parents more choices and tools to help them ensure that young consumers are using [the company’s] products in an optimal manner.” The letter discusses research regarding the potential unintentional negative consequences of the use of digital technologies by young users. In a June 2018 [letter](#), JANA and CalSTERS acknowledged that Apple has taken steps to address the challenges identified in the investors’ January letter.

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RECENT ESG-SPECIFIC DEVELOPMENTS



In April 2018, the U.S. Department of Labor issued **Field Assistance Bulletin No. 2018-01**, which reiterates the Department's "longstanding position that ERISA fiduciaries may not sacrifice investment returns or assume greater investment risks as a means of promoting collateral social policy goals. The Bulletin also states that while environmental, social and governance ("ESG") factors that "involve business risks or opportunities that are properly treated as economic considerations themselves in evaluating alternative investments" should be given the appropriate weight, "[f]iduciaries must not too readily treat ESG factors as economically relevant to the particular investment choices when making a decision."

In May 2018, T. Rowe Price updated its **Policy Statement on Environmental, Social, and Governance Issues**. According to the Policy, T. Rowe Price relies on its own analysts and portfolio managers, with support from the firm's Responsible Investment and Corporate Governance teams, to assess the impact of ESG factors on investments.

In May 2018, a new effort called the "**Main Street Investors Coalition**" backed by the National Association of Manufacturers, the American Council for Capital Formation, the Equity Dealers of America, the Savings & Retirement Foundation and the Small Business & Entrepreneurship Council, was created to raise awareness of the potential issues that can arise as a result of the influence of a small number of investors and proxy advisory firms on ESG issues. The Coalition publishes a **blog** that provides short articles on topics of interest to retail investors.

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Vinson & Elkins has an experienced and capable environmental team that knows and understands... how environmental issues fit into equity offerings and securities disclosures.

– Chambers USA 2018

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CLIMATE CHANGE
DISCLOSURE
DEVELOPMENTS

In March 2018, Swiss multinational investment bank UBS became the first foreign private investor to file an EU corporate sustainability report with the SEC through Form 6-K. UBS's report, which was required to be created and filed in the EU countries in which UBS operates under the **EU Non-Financial Reporting Directive**, contains information that generally falls outside what has been considered material for reporting under the SEC's 2010 **Climate Change Guidance**. UBS's Form 6-K filing also came after the U.S. Government Accountability Office released a **report** in February 2018 stating that the SEC has no current plans to modify its climate-related disclosure requirements.

In the first half of 2018, several energy companies published reports on their approach to managing climate change risks and the companies' resilience under a potential low carbon future:

- ExxonMobil's February 2018 **Energy & Carbon Summary: Positioning for a Lower-Carbon Energy Future** includes analysis based on climate scenarios developed by the International Energy Agency (IEA) and other scenarios and states that "it is possible that some higher-cost assets, which could be impacted by many factors, including future climate policy, may not be developed" under certain scenarios but then notes that "the size, diversity, and continued upgrading of [ExxonMobil's] undeveloped resources, along with technology developments, will enable the ongoing replenishment of our proved reserves under a range of potential future demand scenarios for decades to come."
- Chevron's March 2018 **Climate Change Resilience – A Framework for Decision Making** includes analysis of Chevron's resiliency under the IEA Sustainable Development Scenario, a climate scenario designed to assess the potential impact of the Paris Agreement on future global energy supply and demand. Analyzing this scenario, Chevron concluded that "[s]ome assets could be exposed if [it] took no action, although most of [Chevron's] assets are competitive" and also noted that Chevron's "ability to adjust is [its] best preparation to limit [its] assets being exposed."
- Shell's April 2018 **Energy Transition Report** includes analysis of Shell's own climate scenario, Sky Scenario, which Shell developed to assess one way in which the goals of the Paris Agreement could be achieved. Shell explains in its report that it has, and will continue to, manage its portfolio to "reduce the risk of having assets that are uneconomic to operate, or oil and gas reserves that are uneconomic to produce because of changes in demand or CO 2 regulation," including by investing in natural gas, electricity generation, wind power, and biofuels.

Several developments have occurred since the Financial Stability Board Task Force on Climate-Related Financial Disclosures (the “TCFD”) released its **final recommendations** in June 2017. In April 2018, the TCFD launched the **TCFD Knowledge Hub**, which is a repository of guidance documents and other information on climate reporting that have been created to help companies comply with the TCFD’s recommendations. On May 31, 2018, the European Bank for Reconstruction and Development (“EBRD”) and the Global Centre of Excellence on Climate Adaptation (“GCECA”) hosted a conference to discuss implementation of the TCFD recommendations on physical climate risk and opportunities. During the event, EBRD and GCECA unveiled a **report** with recommendations on disclosure of physical climate change risks, including disclosure of locations that are critical to companies’ value chains, potential impacts from extreme weather events, and other potential risks associated with climate change.

In February 2018, ISS announced that it would be implementing an Environmental and Social QualityScore and published an **FAQ**. The QualityScore is a numerical score intended to be consistent with the ISS Governance QualityScore and is based on companies’ implementation of standards published by the TCFD; the Global Reporting Initiative, an international organization that seeks enhanced disclosure of corporate social responsibility and environmental information; and the Sustainability Accounting Standards Board, a U.S.-based organization seeking enhanced disclosure of sustainability information in public financial statements.



ESG AND CLIMATE CHANGE DEVELOPMENTS: WHAT DO THEY MEAN?

- ESG matters have become the “new governance,” and many companies can expect to receive investor interest on these matters as often as they receive investor interest on classic governance matters (e.g., shareholder rights and board composition).
- Environmental and human rights topics have become among the most frequently addressed matters in Rule 14a-8 proposals. Companies should consider these topics in advance of receiving any investor correspondence. Larger institutional investors also have taken ESG positions in recent years, and while this suggests that ESG matters have gone mainstream, there are still ways for companies to negotiate with investors and other interested parties on these matters.
- Integrated reporting and changing concepts of materiality are coming, it makes sense for companies to have conversations regarding their risk analysis and disclosure as soon as possible.

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YAHOO!: THE SEC'S FIRST CYBERSECURITY DISCLOSURE ENFORCEMENT ACTION



On April 24, 2018, the SEC **announced** that Altaba Inc., the entity formerly known as Yahoo! Inc., agreed to pay a \$35 million penalty to settle charges that it misled investors by failing to disclose the December 2014 data breach in which hackers stole personal data relating to hundreds of millions of user accounts. The order represents the SEC's first cybersecurity disclosure enforcement action. According to the SEC's release, Yahoo failed to properly investigate the circumstances of the breach and to adequately consider whether the breach needed to be disclosed to investors. The breach was not publicly disclosed until more than two years later when Yahoo was in the process of closing the acquisition of its operating business by Verizon Communications, Inc. Steven Peikin, Co-Director of the SEC Enforcement Division, stated that while [the Commission] does "not second-guess good faith exercises of judgment about cyber-incident disclosure," the Commission cautions companies "that a company's response to such an event could be so lacking that enforcement action would be warranted."

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GDPR
SUMMARY

The General Data Protection Regulation (“GDPR”), the comprehensive EU legal regime intended to safeguard individuals’ data privacy rights, was adopted in April 2016 and became effective in May 2018. As discussed in greater detail in our [May 2018 article](#), there are five aspects of GDPR that governance practitioners should keep in mind:

- 1 **Consent is not the only “lawful basis” for processing data.** When data is necessary for the performance of a contract, a consumer cannot force a business to stop using that data as long as the contract is in force. That contract can be formed as simply as a consumer clicking “I agree” on an online vendor’s terms of use when purchasing a product or subscribing to a service. In such a case, a consumer who agrees to purchase a product or service from that vendor and provides her credit card information cannot then demand that the vendor erase that data before the sale has been processed.
- 2 **The right to be forgotten is not absolute.** Some may worry that GDPR will force them to delete all of an individual’s data immediately once such a request is made. In reality, Article 17 of GDPR states that immediate erasure is required only on certain grounds, such as when the data is no longer necessary for the purposes for which it was collected or if it was collected unlawfully in the first place. GDPR also allows important exceptions to the right of erasure.
- 3 **There is a difference between legal representatives and data protection officers (DPOs).** A DPO is an individual that can be a company employee or an external professional and is charged with essentially functioning as a watchdog: he or she reports to the highest levels of the company and conducts internal investigations when concerns or complaints arise about how the company manages data. DPOs are required under Article 37 for certain companies that monitor individuals on a large scale or perform large-scale processing of certain categories of data. Legal representatives are required under Article 27 for certain companies based outside the EU that process data subject to GDPR. These representatives, which may be individuals or separate entities, act as liaisons to data protection authorities.
- 4 **Rules governing data portability may create uneasy cooperation between competitors.** Under Article 20, companies must provide a person his or her personal data in a structured, commonly used, machine-readable format so long as the data processing was automated in the first place. Where the hassle of transferring data may have previously made a customer hesitate to switch products or vendors, now switching may be more seamless than ever. While that may be welcome news for consumers, businesses should be aware of the potential impact to their bottom line.
- 5 **Specific employee data privacy rules may apply.** Article 88 permits individual member states to set their own, more far-reaching rules governing employee data privacy (such as the employment-specific rules in Germany’s Federal Data Protection Act).



Upcoming V&E CLE: November 1, 2018

CYBER-GOVERNANCE: LEGAL CONSIDERATIONS FOR CYBER DISCLOSURE AND PREPAREDNESS

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CYBER DISCLOSURES RECAP

As we discussed in our [earlier article](#), on February 21, 2018, the SEC issued the “[Commission Statement and Guidance on Public Company Cybersecurity Disclosures](#).” This is the first time since the SEC issued [CF Disclosure Guidance: Topic No. 2](#) in October 2011 that the Commission has provided substantive guidance on companies’ disclosure obligations with respect to cybersecurity risks and cyber incidents. A few takeaways from this guidance:

- 1 Review your risk assessment and mitigation processes and disclosure controls;
 - 2 Use existing disclosure requirements to provide timely information on material risks and events;
 - 3 Consider broader disclosure obligations under Regulation FD; and
 - 4 Review insider trading policies and codes of ethics/conduct.
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UPDATED
PROXY C&DIS

On May 11, 2018, the SEC updated the Compliance and Disclosure Interpretations (“C&DIs”), replacing the prior Telephone Interpretation Manual and the March 1999 Supplement that related to the proxy rules and Schedules 14A/14C. Updates to more C&DIs can be expected. While most of the new C&DIs merely reiterate the prior guidance, four make technical revisions (C&DIs 126.04, 126.05, 158.01 and 158.03) and the following six C&DIs make substantive changes to the prior guidance:

124.01: Question: Rule 14a-4(b)(1) states that a proxy may confer discretionary authority with respect to matters as to which a choice has not been specified by the security holder, so long as the form of proxy states in bold-faced type how the proxy holder will vote where no choice is specified. If action is to be taken with respect to the election of directors and the persons solicited have cumulative voting rights, can a soliciting party cumulate votes among director nominees by simply indicating this in bold-faced type on the proxy card?

Answer: Yes, as long as state law grants the proxy holder the authority to exercise discretion to cumulate votes and does not require separate security holder approval with respect to cumulative voting.

124.07: Question: The Division has permitted registrants to avoid filing proxy materials in preliminary form despite receipt of adequate advance notification of a non-Rule 14a-8 matter as long as the registrant disclosed in its proxy statement the nature of the matter and how the registrant intends to exercise discretionary authority if the matter is actually presented for a vote at the meeting. See Section IV.D of Release No. 34-40018 (May 21, 1998). Can a registrant rely on this position if it cannot properly exercise discretionary authority on the matter in accordance with Rule 14a-4(c)(2)?

Answer: No.

126.02: Question: Is a registrant required to file a preliminary proxy statement in connection with a proposed corporate name change to be submitted for security holder approval at the annual meeting?

Answer: No. As set forth in Release No. 34-25217 (Dec. 21, 1987), the underlying purpose of the exclusions from the preliminary proxy filing requirement is “to relieve registrants and the Commission of unnecessary administrative burdens and preparation and processing costs associated with the filing and processing of proxy material that is currently subject to selective review procedures, but ordinarily is not selected for review in preliminary form.” Consistent with this purpose, a change in the registrant’s name, by itself, does not require the filing of a preliminary proxy statement.

151.01: Question: A registrant solicits its security holders to approve the authorization of additional common stock for issuance in a public offering. While the registrant could use the cash proceeds from the public offering as consideration for a recently announced acquisition of another company, it has alternative means for fully financing the acquisition (such as available credit under an executed credit agreement in the full amount of the acquisition consideration) and may choose to use those alternative financing means instead. Would the proposal to authorize additional common stock “involve” the acquisition for purposes of Note A of Schedule 14A?

Answer: No. Raising proceeds through a sale of common stock is not an integral part of the acquisition transaction because at the time the acquisition consideration is payable, the registrant has other means of fully financing the acquisition. The proposal would therefore not involve the acquisition and Note A would not apply. By contrast, if the cash proceeds from the public offering are expected to be used to pay any material portion of the consideration for the acquisition, then Note A would apply.

161.03: Question: If a registrant is required to disclose the New Plan Benefits Table called for under Item 10(a)(2) of Schedule 14A, should it list in the table all of the individuals and groups for which award and benefit information is required, even if the amount to be reported is “0”?

Answer: Yes. Alternatively, the registrant can choose to identify any individual or group for which the award and benefit information to be reported is “0” through narrative disclosure that accompanies the New Plan Benefits Table.

163.01: Question: Does a proxy statement seeking security holder approval for the elimination of preemptive rights from a security involve a modification of that security for purposes of Item 12 of Schedule 14A?

Answer: Yes. Accordingly, financial and other information would be required in the proxy statement to the extent required by Item 13 of Schedule 14A.





ONE REMINDER: MAKING THE MOST OF YOUR ANNUAL BOARD CALENDAR

As governance professionals, we assist many companies with their annual board meeting calendars each year. Here are a few reminders for establishing your board and committee meeting schedule and agendas:

- Failure to attend at least 75 percent of the aggregate applicable board and committee meetings is likely to earn a director a negative vote recommendation from ISS, unless there is an “acceptable” reason for his or her absences. For that reason, among others, it is important to check directors’ calendars early in the process of setting the board calendar, and keep an eye out for directors coming close to the 75 percent threshold.
- Companies frequently include a minimum number of meetings in one or more of their board committee charters — don’t forget to check for meeting minimums when establishing the meeting schedule. Also, companies frequently state that certain board and committee tasks will be completed “annually” or “each year” (some of which address actual SEC and exchange requirements and some of which do not) — check for these types of statements in the committee charters and other governance documents when establishing board and committee agendas.
- Consider whether there is pending legislation, regulations or guidance that your board or a board committee will need to evaluate prior to the end of the board calendar year.
- Consider whether any new disclosures have committed the board or a board committee to reviewing certain information or establishing certain procedures and protocols.

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For more information, visit our Corporate Governance page at:
<http://www.velaw.com/What-We-Do/Corporate-Governance/>.



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