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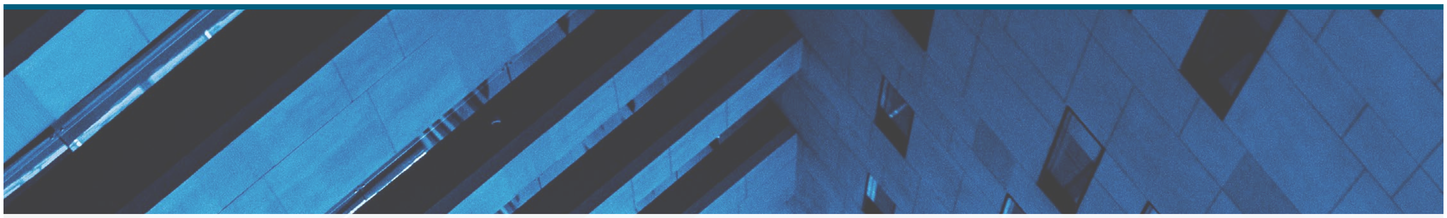
V&E GOVERNANCE UPDATE

SUMMER 2019



V&E SUMMER 2019

GOVERNANCE UPDATE

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LETTER FROM THE EDITORS

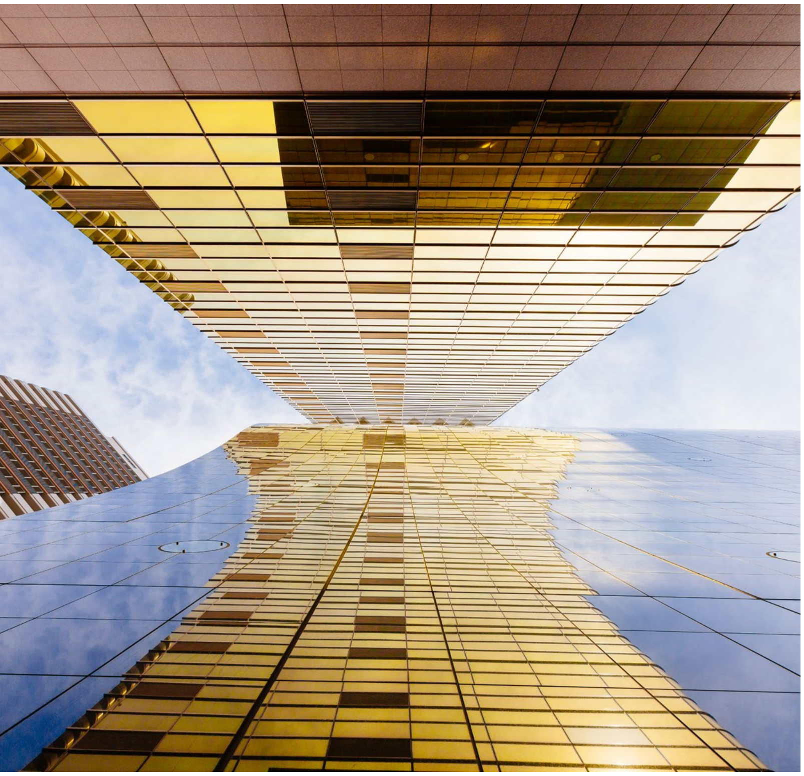
THE PROBLEM WITH ESG

The term "ESG," standing for environmental, social and governance, appears to have been first coined in 2005. Since then, the concept has been widely adopted and discussed, and has come to include an ever expanding array of topics, reporting regimes, proposals, panels and roundtables. As governance professionals, we frequently get asked "What is ESG? How does it differ from sustainability? How does it differ from corporate social responsibility? Does it include all of the governance issues traditionally of interest to investors? What is ESG *not*?"

Increasingly, ESG is the new definition of corporate governance. It includes everything that has been traditionally considered part of a company's governance considerations, plus more. It is the "plus more" that is the source of conversation, confusion and not just a little consternation, but that has always been the case in the dialogue regarding corporations, the duties they owe, and the persons to whom they owe those duties. Calls for new types of corporate governance disclosure frequently meet a degree of suspicion, particularly when those calls are for additional regulation rather than voluntary disclosure. This suspicion can be warranted as not every corporate matter that is of interest is necessarily material, and nailing down what corporate matters are broadly material is no simple task. Moreover, once new disclosure requirements are introduced, the subject matter of those requirements tends to be assumed to be material, even if it arguably is not. For example, the true materiality of certain executive compensation disclosures required of public companies can be doubted, but those disclosures have become a reality that is unlikely to change.

The term "ESG" is a useful one because it helps us understand when the conversation has ventured into that broader "plus more" space, but the term "ESG" is unhelpful in discussing and evaluating the practical realities of an individual company seeking to create effective corporate governance, risk management, and corporate compliance programs. When it comes to the uniqueness of a company's corporate strategy and systems, a more bespoke approach to ESG will always be necessary — we cannot speak about "ESG" meaningfully in that context, but we may be able to speak meaningfully about the implications of climate change on properties near the Gulf Coast over the next 10 to 20 years, or the human rights implications of deforestation in Brazil, or the public health risks of potentially hazardous materials in popular manufactured foods. There is no "ESG policy" that can effectively speak to an individual company's corporate strategy and systems any more than there is a single "governance policy" that can fully describe all the subtleties of that company's board and management practices, its strategic approaches to overseeing and motivating management, its engagement with its investors.

Moreover, the relative newness of the term "ESG" can create the impression that something new is also required to address it, but this is not always the case. When ESG is broken down to its components at the individual-company level, it is largely about the company's corporate culture, risk identification and mitigation, corporate communication (both internally and externally) and internal controls. As governance professionals, we see a correlation between companies that are willing to have conversations regarding the "plus more" in ESG and those that have a sophisticated enterprise risk management ("ERM") system, culture of compliance and effective disclosure, and history of strong internal controls. This correlation probably exists



for two reasons: first, when these corporate structures — a sophisticated ERM system, culture of compliance and effective disclosure and strong internal controls — are in place, they create a more stable platform for a company to have an effective internal ESG discussion, and second, a company is more likely to be able to identify potential ESG risks and opportunities if these structures exist.

So what do we do with the problems posed by ESG? We have four simple recommendations for companies, both private and public, to consider:

- ***Get as specific as possible.*** What specific ESG elements are most relevant to the company's strategy and risk profile? Just as importantly, are there ESG elements that can be eliminated (or set aside for a time) as potential areas of interest or concern? Avoid attempting to focus on all of "ESG."
- ***Identify what already exists.*** Often we find that companies are already addressing various ESG matters before any investor or interest group approaches asking for their "ESG policy." Before reacting to any requests, we recommend understanding what the company is already doing (i.e., health, safety and environment ("HSE") program, corporate social responsibility program, alliances with charitable organizations).
- ***Know your team.*** ESG matters frequently require the expertise of people in different business units as well as external experts. Groups that should be considered include legal, investor relations, public relations/ marketing, HSE, HR, operations, and internal controls. We recommend identifying these folks before moving forward on any new ESG requests. Note that getting the various member groups on the same page can be half the battle, particularly when disclosures involving detailed scientific analyses are involved.
- ***Create a plan.*** Often we find that companies react to requests for disclosure without considering next steps or even the purpose of the disclosure. Before calling the public relations or marketing firm to draft a sustainability policy, we recommend giving some thought to what happens next. Will the company continue to provide disclosures of this nature going forward? Does the company have the resources to address this or future requests? What expectations is the company creating in its investor base and among other stakeholders? What does the company hope to achieve? And don't forget to involve the necessary members of your ESG team.

Ultimately, companies should view ESG as a new framework for considering their existing corporate governance, risk profile and strategy, and use it to enhance, rather than detract, from creating a more wholistic and transparent corporate governance program.

Are you interested in a step-by-step guide for adopting a strategic approach to ESG matters relevant to your company? **Contact us** for our ESG Strategy Menu.

SEEING OTHER PEOPLE: THE BUSINESS ROUNDTABLE RECONSIDERS 'SHAREHOLDERS FIRST' DOCTRINE

In mid-August, the Business Roundtable released a new **Statement on the Purpose of a Corporation**, signed 181 CEOs of the top U.S. companies, including the likes of Jeff Bezos, Larry Fink, Lachlan Murdoch and Jamie Dimon. The Statement provides that

> Since 1978, Business Roundtable has periodically issued Principles of Corporate Governance that include language on the purpose of a corporation. Each version of that document issued since 1997 has stated that corporations exist principally to serve their shareholders. It has become clear that this language on corporate purpose does not accurately describe the ways in which we and our fellow CEOs endeavor every day to create value for all our stakeholders, whose long-term interests are inseparable.

The Statement goes on to discuss these CEOs' and their companies' commitment to delivering value to customers, investing in employees, dealing fairly and ethically with suppliers and supporting the communities in which they work, as well as generating long-term value for shareholders. The Statement echoes **Larry Fink's letter to CEOs earlier this year**, in which BlackRock's Chairman and CEO stated that "[p]rofits are essential if a company is to effectively serve all of its stakeholders over time – not only shareholders, but also employees, customers, and communities."

The boldness of the Statement cannot be underestimated, however it also stops short of suggesting that the corporation may consider interests other than those of shareholders if the interests of various stakeholders diverge. In other words, it is fine for a company to consider the interests of customers, employees, suppliers and communities provided those interests also serve the long-term interests of its shareholders. However, the shift from an inward "board-focused governance" — as a reminder, the 2012 Business Roundtable principles of corporate governance focused on governance matters like independent chairs, majority voting, risk oversight and succession planning — to an outward corporate responsibility focus is noteworthy.

Will the Statement's positions adopted by the CEOs of top U.S. companies result in meaningful change in how corporations engage with key stakeholders? Well, shortly before Jeff Bezos signed the Statement, Amazon received twelve shareholder proposals for its 2019 annual shareholders' meeting that were included in its **proxy statement**, including proposals regarding products allegedly promoting bigotry or hate crimes, sexual harassment, climate change, food waste, board diversity, gender pay equity and the integration of ESG metrics into executive compensation. The Amazon board recommended "against" all shareholder proposals.

SHALL WE DANCE? THE SEC CONTINUES TO FLIRT WITH REVISITING QUARTERLY REPORTING

In mid-July, the SEC Division of Corporation Finance hosted a **roundtable** to discuss the impact of "short-termism" on the U.S. capital markets. The roundtable follows the Commission's December 2018 **request for comment**, which remains open, on the quarterly reporting regime. The two panels focused on whether changes to the SEC's periodic reporting regime could reduce short-termism and discussed whether the SEC should discourage the widely adopted practice of providing quarterly earnings guidance.

This isn't the first time the SEC has weighed whether it should reconsider its approach to interim reporting. In 2016, the SEC issued a lengthy **concept release and request for comment** on, among other things, how the periodic reporting system, earnings releases and earnings guidance may affect corporate decision making and result in short-termism, and in 2013, the SEC staff's **report to Congress**, submitted as part of the SEC's disclosure effectiveness review, touched upon the history of quarterly reporting and the degree to which it remains useful. While we likely remain a distance from the SEC materially changing the periodic reporting regime, it is possible we will see guidance from the SEC on the widely adopted practice of issuing quarterly earnings releases in the nearer term.

> "[V&E] can look at the business angle and weigh the legal risk when needed. It's a very solid team."
>
> – *Chambers USA* 2019

ISS LAUNCHES 2019 POLICY SURVEY, CONTENTS SURPRISE NO ONE

Each year in late July or early August, ISS launches its annual policy survey, which provides a sneak peek of potential policy changes for the next year. This year, ISS launched its policy survey on July 23, and the U.S. survey topics included a number of topics we've seen before:

BOARD GENDER DIVERSITY	Topic addressed in the 2018 survey for 2019 policies and in the 2017 survey for 2018 policies
DIRECTOR OVER-BOARDING	Topic addressed in the 2016 survey for 2017 policies
MULTI-CLASS CAPITAL STRUCTURES	Similar topics addressed in the 2018 survey for 2019 policies, in the 2017 survey for 2018 policies and in the 2016 survey for 2017 policies

The U.S. survey topics also included questions regarding combined chairman and CEO roles, a topic that has not been directly addressed in the survey in a number of years. A new, but perhaps not surprising, topic is director accountability relating to climate change risk. Lastly, the survey included a series of executive compensation questions regarding the performance screens for ISS's pay-for-performance models. The survey is now closed, but a copy of the questions can be accessed **here**. If ISS is consistent with prior years, it will issue proposed policy updates in October and final policy updates in November.

THE SEC TAKES A BABY STEP TOWARDS REGULATING PROXY ADVISORY FIRMS

On August 21, the SEC issued **Commission Guidance Regarding Proxy Voting Responsibilities of Investment Advisers** (the "Advisers Guidance") to assist investment advisers in using the services of proxy advisory firms in fulfilling the advisers' proxy voting responsibilities. On the same date, the SEC released the **Commission Interpretation and Guidance Regarding the Applicability of the Proxy Rules to Proxy Voting Advice** (the "Voting Advice Guidance"), which provides details on when proxy voting advice provided by a proxy advisory firm will constitute "solicitation" under federal proxy rules.

While the new guidance does not create new legal or regulatory requirements, it does go beyond the prior guidance issued by the staff of the Division of Corporation Finance — **Staff Legal Bulletin No. 20** on the proxy voting responsibilities of investment advisors and availability of exemptions from the proxy rules for proxy advisory firms — in three meaningful ways. First, the Advisers Guidance provides guidance on how advisers should consider and evaluate the voting policy methodologies of proxy advisory firms, including weaknesses in those methodologies. This change is noteworthy because proxy advisory firms' methodologies are somewhat infamously, and perhaps intentionally, cryptic. Second, the Advisers Guidance clarifies the situations in which an investment adviser who has assumed voting authority is not required to exercise that authority to vote a proxy for that client. Third, the Voting Advice Guidance clarifies that Exchange Rule 14a-9 (which prohibits any solicitation from containing any statement which, at the time and in light of the circumstances under which it is made, is false or misleading with respect to any material fact) applies to the proxy voting advice given by proxy advisory firms. The new guidance also provides more detailed answers on several topics covered by the prior guidance.

This new guidance has been a long time coming. As a reminder, the SEC first issued a **concept release** seeking public comment on the rule and legal status of proxy advisory firms in 2010 and Staff Legal Bulletin No. 20 was issued back in 2014. And while this guidance does not impose regulations on proxy advisory firms to the extent some companies no doubt hoped it would, it is a meaningful step in the Commission's consideration of the role of proxy advisory firms in the U.S. proxy process.

U.S. CONGRESSIONAL HEARING EVALUATES REQUIRING ESG DISCLOSURES

In early July, the House Financial Services Committee ("FSC") and Subcommittee on Investor Protection, Entrepreneurship and Capital Markets held a hearing to discuss five disclosure bills, including four that clearly address ESG disclosures requirements:

- The **ESG Disclosure Simplification Act of 2019** would require each issuer to disclose (i) the issuer's views on the link between ESG metrics and its long-term business strategy; and (ii) the process the issuer uses to determine the impact of ESG metrics on its long-term business strategy. The bill would also establish a permanent SEC advisory committee called the Sustainable Finance Advisory Committee comprised of individuals and entities with an interest in sustainable finance.
- The **Shareholder Protection Act of 2019** would require the Commission to amend the reporting rules to require each issuer to publish a quarterly report containing (i) a description of any expenditure for political activities made during the quarter; (ii) the date and amount of each expenditure; (iii) if the expenditure was made in support of or opposed to any candidate (including the name and party of and office sought by the candidate); and (iv) the name or identity of any trade associations or organizations that received dues or payments from the issuer.
- The **Corporate Human Rights Risk Assessment, Prevention, and Mitigation Act of 2019** would require each issuer to identity any human rights risks and impacts in its operations and value chain, ranked by severity, in its annual report under the heading "Human Rights Risk and Impact Report."
- The **Climate Risk Disclosure Act of 2019** would require each issuer to include in its annual report (i) the identification of, evaluation of potential financial impacts of, and risk management strategies relating to, physical and transition risks posed to the issuer by climate change; (ii) a description of any established corporate governance processes and structures to identify, assess, and manage climate-related risks; and (iii) a description of specific actions the issuer is taking to mitigate identified risks.

The hearing also discussed an as-of-yet **unnamed bill** that would require issuers to disclose in an annual or quarterly report and on a country-by-country basis (i) the total pre-tax profit of the issuer during the period; and (ii) the total amount paid by the issuer in state, Federal and foreign taxes during the period.

A majority of the FSC staff also issued a **memorandum** discussing the broader context for the hearing, stating that SEC disclosure rules "generally require[] companies to disclose information that is reasonably likely to have a material effect on a company's financial condition or its operating performance," but that the SEC's rules "do[] not require companies to only disclose information that meets the standard of "materiality," and the SEC has broad authority to require the disclosure of information if it would be in the public interest or would protect investors." The memorandum goes on to state that "[t]here is growing evidence that ESG disclosures are material to investors," pointing out that credit rating agencies are now incorporating ESG factors into their rating methodologies, and highlighting the increase in ESG investment and recent investor petitions requesting rulemaking on ESG disclosures. As a reminder, in May, a majority of the FSC staff issued a **memorandum** which addressed several bills regarding human capital management matters.

At issue during the hearing and likely going forward is the question of materiality — specifically, to what extent these ESG matters are or should be considered material under the securities laws. While it will probably be some time before we seen any legislation of this nature adopted in the U.S., the fact these discussions are being had is in and of itself indicative that we can expect calls from investors and other interest groups for specific ESG disclosure requirements to increase in intensity.

YOU AND WHAT ARMY? $1.7 TRILLION IN ESG INVESTMENT TAKES ON WORKPLACE EQUITY DISCLOSURE

Investor signatories representing **$1.73 trillion in assets** under management

Over 3,000 companies across 23 developed market economies

In mid-June, As You Sow released an **investor statement regarding workplace equity disclosure**, calling for companies to provide greater disclosure on corporate policies and practices relating to gender, race, ethnicity, sexual orientation and other federally protected classes. As a reminder, As You Sow is a non-profit investor advocacy group that tends to focus on submitting shareholder resolutions regarding climate change and human rights, but for those who are tempted to write off this group as a small activist investor focused on submitting easily defeated proposals, this most recent investor statement is backed by investor signatories representing $1.73 trillion in assets under management, and is being sent to over 3,000 companies across 23 developed market economies. We also have reason to believe that As You Sow is not the only activist investor in the letter campaign business currently, with both CalPERS and the New York City Comptroller having submitted letters regarding board and workplace diversity to public companies in recent months.

As a reminder, the New York City Comptroller's Boardroom Accountability Project 2.0 encouraged the use of a "board matrix" (See Figure A on page 11) in proxy statement disclosure, which would provide detailed information on directors' skills and characteristics including gender, race and sexual orientation. However, increasingly we are seeing these groups expand this interest to matters regarding workplace diversity and equity.

[INSERT YOUR ORGANIZATION NAME] (FIGURE A)

Board Matrix

This sample matrix can help boards and investors assess the level of experience each company director/nominee has in various areas, as well as the in the areas of gender, sexual orientation and racial/ethnic diversity, age and tenure.

	Board of Directors							
	Name 1	Name 2	Name 3	Name 4	Name 5	Name 6	Name 7	Name 8
Skills & Experience								
Board of Directors Experience	X			X				
[Specific] Industry Experience		X					X	
CEO/Business Head	X			X				
International	X					X	X	
Human Capital Management/ Compensation			X				X	
Finance/Captial Allocation		X			X		X	
Financial literacy/Accounting (Audit Committee Financial Expert or “ACFE”)			X			X		
Government/Public Policy	X			X				
Marketing/Sales			X		X			
Environmental Science/Policy/Regulation						X		
Academia/Education								
Risk Management				X				
Corporate Goverance		X						X
Technology/Systems								X
Business Ethics			X			X		X
Real Estate		X			X			X
[Custom 1]								
Demographic Background								
Board Tenure								
Years	15	15	10	8	7	7	4	1
Sexual Orientation (voluntary)								
LGBTQ	X							
Gender								
Male		X	X	X	X	X		X
Female	X						X	
Non-Binary								
Age								
Years old	60	63	65	62	60	67	55	47
Race/Ethnicity								
African American/Black	X							
Asian, Hawaiian, or Pacific Islander								
White/Caucasian		X	X	X		X	X	X
Hispanic/Latino					X			
Native American								
Other								

Source: *“Boardroom Accountability Project 2.0.”* New York City Comptroller, 2019

SEC PROPOSES PRINCIPLES-BASED AMENDMENTS TO BUSINESS AND RISK FACTOR DISCLOSURES

On August 8, **the SEC proposed rule amendments** to modernize the description of business, legal proceedings and risk factor disclosures required under Regulation S-K. In summary, the proposed amendments would make the changes outlined below.

ITEM 101(A) OF REGULATION S-K	PROPOSED AMENDMENTS
• Currently requires a description of the general development of the business of the company during the past five years, or such shorter period as the company may have been engaged in business.	• ***Eliminate prescribed timeframe.*** Eliminate the prescribed five-year disclosure timeframe, and replace it with a requirement to focus on the information material to an understanding of the development of the company's business, irrespective of a specific timeframe. Similar revisions are proposed to eliminate the three-year disclosure timeframe applicable to smaller reporting companies. • ***Reduce duplicative disclosure regarding development of the business.*** Limit disclosure regarding the general development of business to initial registration statements, with updates on material developments, if any, to be provided in subsequent filings. Require an active hyperlink to the most recently filed disclosure that, together with any update, would present a full discussion of the general development of their business. • ***Add business strategy as a potential disclosure topic.*** Add a requirement to disclose, to the extent material to an understanding of a company's business, transactions and events that affect or may affect the company's operations, including changes to the company's previously disclosed business strategy.

ITEM 101(C) OF REGULATION S-K	PROPOSED AMENDMENTS
• Currently requires a narrative description of the business done and intended to be done by the company, by segment to the extent material to an understanding of the company's business taken as a whole. • Includes an enumerated list of disclosure items.	• ***Update disclosure topics and clarify principles-based approach.*** Update the list of enumerated disclosure topics companies must address to the extent material to an understanding of the business taken as a whole or material to a particular segment, and clarify that topics that are not material to an understanding of the company's business do not need to be addressed. • ***Address human capital management.*** Replace the current requirement to disclose the number of employees with a requirement to disclose a description of the company's human capital resources, including a description of any human capital measures or objectives that management focuses on in managing the business. • ***Expand legal compliance focus.*** Expand the regulatory compliance requirement to include material government regulations, not just environmental laws.

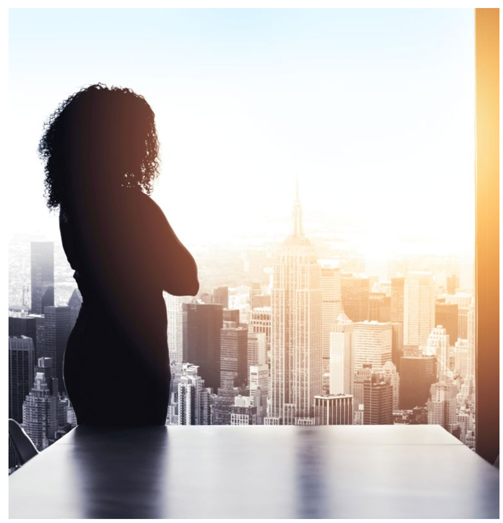
ITEM 103 OF REGULATION S-K	PROPOSED AMENDMENTS
• Currently requires disclosure of any material pending legal proceedings, other than ordinary routine litigation incidental to the business, to which the company is a party or to which any of the company's property is subject.	• ***Use hyperlinks to reduce duplicative disclosure.*** Explicitly permit the use of hyperlinks or cross-references to avoid repetitive disclosure due to the overlapping disclosure requirements contained in Item 103 of Regulation S-K and U.S. GAAP. • ***Adjust environmental proceedings disclosure threshold.*** Revise the $100,000 threshold for disclosure of environmental proceedings to which the government is a party to $300,000 to adjust for inflation.

ITEM 105 OF REGULATION S-K	PROPOSED AMENDMENTS
• Currently requires disclosure of the most significant factors that make an investment in the company or its offering speculative or risky.	• ***Address the increasing length of risk factor disclosure.*** Require a summary risk factor disclosure if the risk factor section for a company exceeds 15 pages. • ***Refocus on material risks.*** Replace the requirement to disclose the "most significant" risk factors with the "material" risk factors. • ***Enhance organization of risk disclosure. Require companies to:*** – Organize risk factors under relevant headings. – Identify risk factors that could apply to other companies or securities offerings and that do not provide an explanation of why the risk is specifically relevant to the company's investors under the caption "General Risk Factors."

The comment period for the proposed rules will close October 22, 2019.

UPDATE ON BOARD DIVERSITY

In early August, the conservative activist group, Judicial Watch, filed a lawsuit challenging the constitutionality of California's mandatory board diversity law. As a reminder, California Senate Bill 826 was signed into law in September 2018, and requires each publicly held corporation having principal offices in California to have at least one female director on its board of directors by the end of 2019, and at least (i) three female directors (if the board has six or more directors), (ii) two female directors (if the board has five directors), or (iii) one female director (if the board has fewer than five directors) by the end of 2021. Companies that do not comply will be subject to fines. The California board diversity law faced controversy before it was passed, and it is possible that additional challenges will follow, however, a number of other states are already considering similar measures. In addition, we expect investors to continue to press the issue, notwithstanding challenges to any legislative measures, so companies with all-male boards are still likely to receive attention.



In July, the last S&P 500 company with an all-male board, Copart Inc., added its first female director. While progress outside of the S&P 500 has been slower, consistent with other governance trends, we expect calls for greater board diversity to continue to spread and drive deeper into the market, as investors, including the likes of BlackRock, Vanguard and State Street, continue to support these efforts.

> Vinson & Elkins is recognized as a **national tier 1 law firm in 19 practice areas**, with a total of **37 national rankings** in the "Best Law Firms" survey.
>
> – *The U.S. News – Best Lawyers®* 2018

UPDATE ON CLIMATE CHANGE REPORTING

In June, the Task Force on Climate-Related Financial Disclosure ("TCFD") issued a **status report** to provide an overview of current disclosure practices as they relate to the TCFD 2017 recommendations. As a reminder, TCFD is a market-driven initiative established by the Financial Stability Board and comprised of 31 members from across the G20. The TCFD released its **final recommendations** providing a framework for companies and other organizations to develop more effective climate-related financial disclosures in June 2017 (See Figure B on page 16). The status report, which is in part the result of a survey conducted by TCFD on companies' efforts to implement the TCFD recommendations as well as investors' views on the usefulness of climate-related financial disclosures, finds that:

- Disclosure of climate-related financial information has increased since 2016, but is still insufficient given the speed at which changes are needed to limit the rise in global average temperature.
- The top area identified by users of climate-related financial disclosures as needing improvement is for companies to provide more clarity on the potential financial impact of climate-related issues on their businesses.
- Of the companies using scenario analysis to assess the resilience of their strategies, most do not disclose information on the resilience of their strategies.
- While sustainability and corporate responsibility functions are the primary drivers of TCFD implementation efforts, risk management, finance and executive management are increasingly involved as well.

TCFD notes that it is considering clarifying elements of the supplemental guidance it issued as an annex to its 2017 recommendations, developing process guidance for companies on how to introduce and conduct climate-related scenario analysis and identifying business-relevant and accessible climate-related scenarios. TCFD expects to issue another report in September 2020. As a reminder, TCFD-based reporting will become **mandatory for signatories** to the United Nation's Principles for Responsible Investment ("UN PRI") in 2020. See Figure C (on page 16) for a list of just a few of the nearly 500 U.S.-based asset owners, investment managers and service providers that currently are PRI signatories.

Also in June, the Commodity Futures Trading Commission's ("CFTC") Market Risk Advisory Committee held a public meeting to discuss (1) the impact of climate change on the future stability of the global financial system; (2) the current U.S. and international initiatives seeking to address climate-related financial risks; (3) the financial industry's approaches to managing and mitigating climate-related financial risks; and (4) future challenges for regulators and market participants in the derivatives industry. In his **opening statement**, Commissioner Rostin Behnam stated that "[a]ssessing climate-related market risk must be a priority — and it must start now," pointing to the rising worldwide economic cost of natural disasters and the efforts taken to date by the CFTC's international counterparts, including the efforts of the Network for Greening the Financial System and TCFD.

RECOMMENDATIONS AND SUPPORTING RECOMMENDED DISCLOSURES (FIGURE B)

Governance	Strategy	Risk Management	Metrics and Targets
Disclose the organization's governance around climate-related risks and opportunities.	Disclose the actual and potential impacts of climate-related risks and opportunities on the organization's businesses, strategy, and financial planning where such information is material.	Disclose how the organization identifies, assesses, and manages climate-related risks.	Disclose the metrics and targets used to assess and manage relevant climate-related risks and opportunities where such information is material.
a) Describe the board's oversight of climate-related risks and opportunities.	a) Describe the climate-related risks and opportunities the organization has identified over the short, medium, and long term.	a) Describe the organization's processes for identifying and assessing climate-related risks.	a) Disclose the metrics used by the organization to assess climate-related risks and opportunities in line with its strategy and risk management process.
b) Describe management's role in assessing and managing climate-related risks and opportunities.	b) Describe the impact of climate-related risks and opportunities on the organization's businesses, strategy, and financial planning.	b) Describe the organization's processes for managing climate-related risks.	b) Disclose Scope 1, Scope 2, and, if appropriate, Scope 3 greenhouse gas ("GHG") emissions, and the related risks.
	c) Describe the resilience of the organization's strategy, taking into consideration different climate-related scenarios, including a 2°C or lower scenario.	c) Describe how processes for identifying, assessing, and managing climate-related risks are integrated into the organization's overall risk management.	c) Describe the targets used by the organization to manage climate-related risks and opportunities and performance against targets.

Source: *"Taskforce on Climate-related Financial Disclosures: Status Report."* June 2019

SAMPLE OF U.S. UN PRI SIGNATORIES (FIGURE C)

- AFL-CIO Reserve Fund
- Bank of America Global Wealth and Investment Management
- BlackRock
- CalPERS
- CalSTRS
- Fidelity Investments
- Goldman Sachs Asset Management
- J.P. Morgan Asset Management
- MetLife Investment Management
- State Street Global Advisors
- The Vanguard Group, Inc.
- TIAA-CREF
- TPG Capital Advisors, LLC
- T. Rowe Price

Are your investors UN PRI signatories? The full list of UN PRI signatories is available here.

LITIGATION UPDATE

In late 2014 or early 2015, Blue Bell Creameries got some bad news — the South Carolina Department of Health and Environmental Control had identified listeria in the company's distribution center for Chocolate Chip Country Cookie Sandwiches and Great Divide Bars. The events of the next few months would result in Blue Bell recalling all of its products, shutting down production at all of its plants and laying off over a third of its workforce. Serious financial issues followed, and a shareholder brought a derivative suit against two executive officers and the board of directors claiming breach of fiduciary duties. In June, the Delaware Supreme Court reversed the 2018 decision of the Court of Chancery in *Marchand vs. Barnhill* to dismiss that shareholder derivative suit, and the case is serving as a good reminder of three fundamental corporate governance truths:

1. ***The importance of risk oversight cannot be over emphasized.*** A board's attentive oversight to the material risks faced by the company, or failure to act in an informed manner and make a good faith effort to oversee a material risk area, can be the difference between success and failure in litigation. And remember: What constitutes acting in an informed manner and in good faith will be judged with the benefit of hindsight.

2. ***The quality and sophistication of your board minutes and materials can save your bacon.*** As governance professionals, we can hear the room groan when we bring up the topic of board minutes and materials, but among "boring" governance topics, it is among the most important. Board minutes and materials are the voice of the corporation, and establishing that the board acted in an informed manner and in good faith will often ultimately come down to the record.

3. ***The bright line independence rules are not the only independence rules.*** While it can be tempting to treat the bright line independence rules of the New York Stock Exchange and Nasdaq as the only independence rules, in litigation, often it is the informal but close relationships with members of management that the court looks to. If a company is already close to the edge with respect to the majority independence requirements, this additional layer of scrutiny can spell disaster.

REMINDERS

REVIEW YOUR RISK FACTORS, YES, AGAIN

In light of the **SEC's recent $100M fine against Facebook for misleading public disclosures, including risk factor disclosure**, it is worth paying close attention to disclosure that describes hypothetical or theoretical possibilities. This is particularly, but not exclusively, true for risk factors or filings in which risk factors may be included.

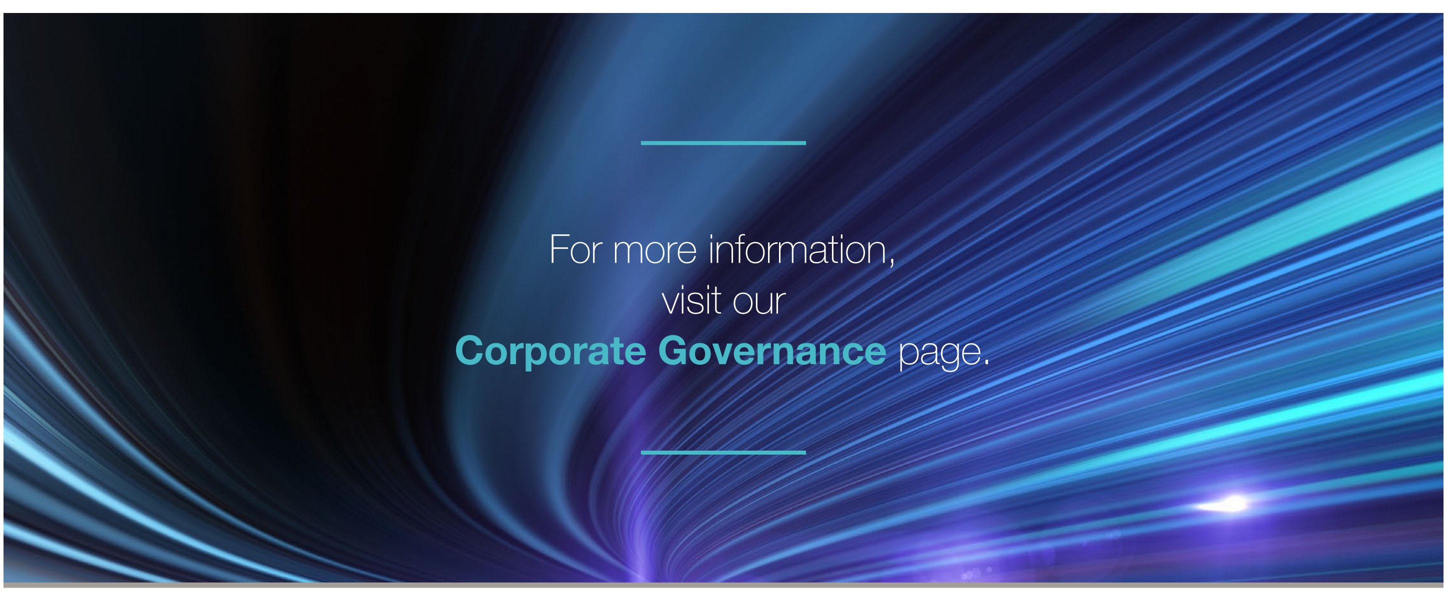
A few specific reminders and recommendations:

- ***General rule*** — Risk factors should always be specific and, whenever possible, describe what has already occurred and then describe the risk going forward.
- When reviewing this language, always ask whether the possible events being described have begun to materialize or have fully materialized. ***Note that if an event is described in disclosure as hypothetical or theoretical, but has actually begun to materialize or has fully materialized, the SEC may view the disclosure as materially misleading.***
- Risk language regarding environmental and climate change-related matters, cyber security and data privacy matters and material transactions should receive extra attention.

CAMs: ANOTHER OPPORTUNITY TO UPDATE YOUR AUDIT COMMITTEE

In July, the PCAOB issued guidance on critical audit matters ("CAM") for audit committees and investors. As a reminder, for audits of large accelerated filers, CAM requirements are effective for fiscal years ending on or after June 30, 2019. For audits of all other companies to which they apply, CAM requirements are effective for fiscal years ending on or after December 15, 2020.

The PCAOB's **Insights for Audit Committees** provides clarity with respect to the role of the audit committee in understanding and communicating regarding CAMs. The PCAOB guidance for audit committees also provides a usable framework for updating audit committees on the practicalities of what the new requirements mean for their obligations as audit committee members. See Figure D (on page 19). In addition, the PCAOB's **Insights for Investors** can help guide companies in engaging with their investors on the new requirements.



Prior results do not guarantee a similar outcome.

WHEN IS A MATTER ARISING FROM THE AUDIT OF FINANCIAL STATEMENTS A CRITICAL AUDIT MATTER (CAM)? (FIGURE D)

Is the matter communicated or required to be communicated to the audit committee?

NO → The matter is not a CAM.

YES ↓

Does the matter relate to accounts or disclosures that are material to the financial statements?

NO → The matter is not a CAM.

YES ↓

Does the matter involve especially challenging, subjective, or complex auditor judgment?

NO → The matter is not a CAM.

YES ↓

The matter is a CAM. Communicate the CAM in the auditor's report.

↓

What should the communication of each CAM include?

1. Identify the CAM
2. Describe the principal considerations that led the auditor to determine that the matter is a CAM
3. Describe how the CAM was addressed in the audit
4. Refer to relevant financial statement accounts or disclosures that relate to the CAM

Source: *"Insights for Audit Committees."* Public Company Accounting Oversight Board, 2019

CORPORATE GOVERNANCE & ESG AT V&E

Vinson & Elkins lawyers are available to assist in addressing any questions you have regarding the matters included in this Governance Update. To learn more about these matters, please contact any of the following lawyers:

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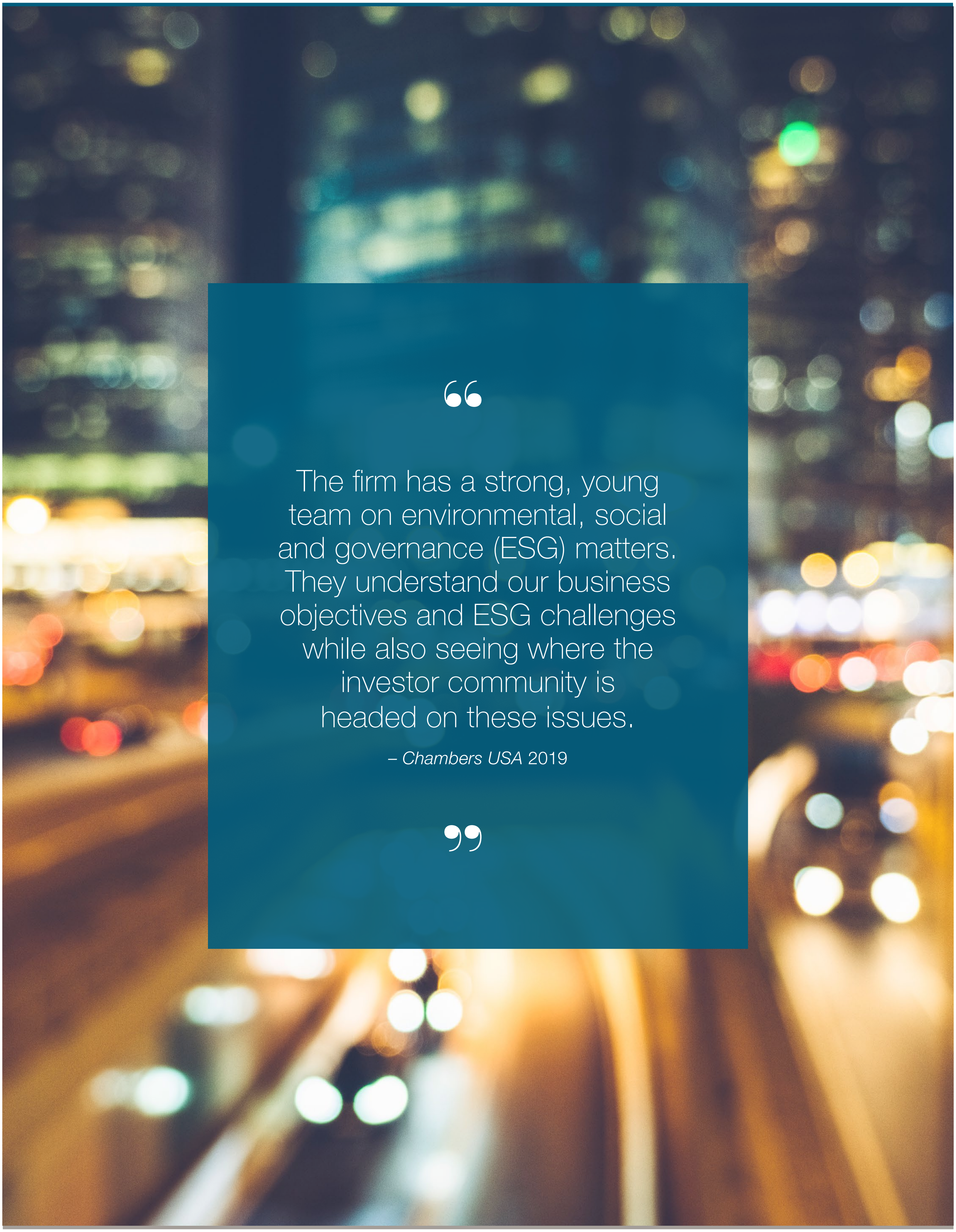

> The firm has a strong, young team on environmental, social and governance (ESG) matters. They understand our business objectives and ESG challenges while also seeing where the investor community is headed on these issues.
>
> – *Chambers USA* 2019

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