

# Corporate Governance Hot Topics

Quarterly Update (August 2021)

## Boardroom Buzz

*Potential topics for the board's agenda this quarter:*

- Are we exercising an appropriate level of oversight over key post-pandemic related risks, such as labor shortages, supply chain disruptions, inflation and cybersecurity issues?
- Do we need to dust off any of our management succession plans or board refreshment plans now that we have seemingly weathered the first early stages of the pandemic?
- Is management responsive to post-pandemic changes in our ways of working? Do the company's capital expenditure budgets and strategic plans reflect changes in our operations, capital allocation needs, consumer behavior and other trends resulting from the pandemic?
- Do we understand the impact that recent legislative and regulatory developments may have on the company?
- Does the company have any exposure to recent signals that non-U.S. governments are taking a more active approach to the regulation of commerce?
- Should the company include a director in its off-season shareholder engagement meetings? Has the company addressed any low-hanging fruit raised by investors in prior engagement meetings? Is the company providing sustainability and other ESG-related information to investors consistent with best practices and its peers?

## 1. Proxy Advisory and Institutional Investor Updates

- **Changes in Director Overboarding Policies:** Institutional investors have developed policies in response to concerns about the "overboarding," or over-commitment, of directors who serve on multiple boards. Effective January 2021, BlackRock expanded its overboarding policy such that a director who is also a public company executive or a fund manager may serve on a maximum of one outside public board, while a director who is not an executive or a fund manager may serve on a maximum of three outside public boards. State Street has amended its policy such that it no longer considers service on a mutual fund board or the board of a UK investment trust when evaluating directors for excessive commitments. Vanguard maintained its policy that considers that directors are over-committed when they serve on five or more public company boards or, if they are also executives, on more than one outside company board. The full text of the BlackRock report is available [here](#). The full text of the State Street report is available [here](#). The full text of the Vanguard report is available [here](#).

- **BlackRock Published Human Rights Engagement Policy:** In March 2021, BlackRock Investment Stewardship published a report describing BlackRock's approach to engagement with companies regarding their impact on human rights. BlackRock's policy emphasizes the importance of proactive risk management regarding potential human rights issues, tying the potential human toll of ineffective controls to impacts on shareholder value. BlackRock encourages companies to "provide access to resources and/or compensation in the event of displacement or destruction." The update also warns that BlackRock may challenge directors of companies seen as "not effectively addressing or disclosing material human rights-related risks or impacts." The full text of the report is available [here](#).
- **Glass Lewis Released Report on Independent Board Chairs:** In March 2021, Glass Lewis released an updated report finding that boards with independent chairs serve shareholders more effectively than boards led by a CEO or other executive. The report cited a recent study by the Millstein Center for Corporate Governance and Performance at the Yale School of Management that "the independent chair curbs conflicts of interest, promotes oversight of risk, manages the relationship between the board and CEO, serves as a conduit for regular communication with shareowners, and is a logical next step in the development of an independent board." The full text of the report is available [here](#).

## 2. Litigation Developments

- **Delaware Supreme Court Affirmed That D&O Policies May Cover Fraudulent Conduct:** In March 2021, in *RSUI Indemnity Company v. Murdock*, the Delaware Supreme Court affirmed a trial court's judgment that required a D&O insurer to pay for losses resulting from the fraud of Dole Food Company's CEO and director. The Court held that public policy does not prevent D&O policies from insuring against fraud. Additionally, the Court interpreted Section 145 of Delaware's General Corporation Law to suggest that companies have "statutory authority to obtain D&O insurance for liabilities arising from bad-faith conduct." The ruling serves as a good reminder for companies to renew their D&O policies and ensure that they provide adequate coverage. The full text of the opinion is available [here](#). A Sullivan & Cromwell memorandum on the decision is available [here](#).

## 3. Surveys, Policies and Reports

- **2021 Say on Pay Results:** As of June, 2021, 37 Russell 3000 companies failed Say on Pay. That equates to a failure rate of 3.1%, which is higher than last year's 2.2% failure rate. Fourteen companies that failed Say on Pay are in the S&P 500. A Sullivan & Cromwell memorandum on the topic is available [here](#).
- **Institutional Investor Survey Reveals Disparity in U.S. and UK/EU Companies Including ESG Measurements in Incentive Compensation Plans:** Surveys conducted by Pay Governance on ESG metrics in 2020 incentive compensation plans in the United States, the United Kingdom, and the European Union, indicate that UK and EU companies include ESG metrics more frequently than U.S. companies. While 22% of U.S. companies surveyed incorporated ESG metrics in their 2020 plans, 90% of UK and EU companies surveyed utilized such metrics. The full text of the report is available [here](#).

- **Shareholder Activism Digest:** 2021 has seen an increase in activism compared to 2020. According to a report by Lazard, activists have secured 42 board seats during the first quarter of 2021, all through negotiated settlements. However, companies have had some success fending off activist campaigns. At TEGNA Inc.'s contested annual meeting on May 7, 2021, for example, shareholders voted to re-elect the entire slate of incumbent directors, rebuking the nominees of dissident hedge fund Standard General for the second year in a row. The Lazard report also highlighted that M&A activity remains the primary activist campaign objective, with 47% of activist campaigns driven by M&A activity during the first quarter of 2021. The full Lazard report is available [here](#).
- **Board Governance and Cybersecurity Risk:** Recent events, such as the ransomware attack against Colonial Pipeline and the cyberattack against Microsoft Exchange, have highlighted the importance of effective cybersecurity risk management. In March 2021, the World Economic Forum released a report stating that cyber risk remains among the top risks facing business organizations today and lists cybersecurity failure as a top "clear and present danger" and critical global threat. The report found that when boards consider and manage the entire portfolio of risks, including cyber risk, their companies do better in the marketplace. The report also expects that cybersecurity will remain a priority for business leaders for years to come. The full text of the report is available [here](#).

#### 4. Disclosure and Regulatory Developments

- **SEC Chair's Remarks About Rule 10b5-1 Trading Plans:** On June 7, 2021, SEC Chair Gary Gensler released remarks for the CFO Network Summit discussing areas for potential rulemaking relating to Rule 10b5-1 trading plans. He suggested five areas where the SEC may engage in rulemaking or enforcement actions in the near future: cooling-off periods, cancellation of trading plans, public disclosure of trading plans, limitations on the number of plans that may be adopted, and the intersection of insider trading plans with public company share buyback programs. The full text of Chair Gensler's remarks is available [here](#). A Sullivan & Cromwell memorandum on the decision is available [here](#).
- **SEC Reopens Comment Period for Mandatory Universal Proxy Proposal:** On April 16, 2021, the SEC voted to reopen the comment period on the proposed rule for the use of universal proxy cards in all non-exempt solicitations. "Reopening the comment period will allow the public to share additional views on the use of universal proxy cards in director elections, particularly in light of the corporate governance developments that have occurred since the Commission issued its proposal," added Acting Director of the SEC's Division of Corporation Finance John Coates. In October 2016, the SEC originally proposed amendments and rules to require the use of universal proxy cards in all non-exempt director elections. The public comment period remained open for 30 days and closed June 7, 2021. The SEC press release is available [here](#). A Sullivan & Cromwell memorandum on the topic is available [here](#).
- **Endeavor Executives Resign from Live Nation Board of Directors Following Antitrust Concerns:** On June 21, 2021, the U.S. Department of Justice ("DOJ") announced that two Endeavor Group Holdings executives resigned from the board of directors of Live Nation Entertainment following the DOJ's suggestion that their positions on the board might create an illegal interlocking directorate. An illegal interlocking directorate is when an agent of one company or individual serves as an officer or director of multiple companies and the positions do not fall within a safe harbor specified by Section 8 of the Clayton Act (the "Act"). Safe harbors exist where competitive sales fall under certain thresholds specified by the Act.

Though the DOJ has pursued such enforcement actions relatively infrequently, it also has adopted a broad construction of competition under Section 8. As a result, companies and board members should closely monitor their compliance with the Act. The DOJ press release is available [here](#).

- **President Biden Issues Executive Order on Competition:** On July 9, 2021, President Biden issued an Executive Order titled “Promoting Competition in the American Economy,” directing federal agencies to take a stronger role in regulating competition and enforcing antitrust laws. The Executive Order is meant to address the Biden Administration’s view that a “trend of corporate consolidation” has diminished competition and negatively impacted consumers and economic growth. The full text of the Executive Order is available [here](#). A Sullivan & Cromwell memorandum on the topic is available [here](#).

## 5. ESG-Related Developments

- **President Biden and SEC Chair Gensler Signal Increased Agency Action on Climate-Related Risk:** On June 23, 2021, SEC Chair Gary Gensler gave formal remarks at London City Week that provided insight into the agency’s work to update requirements around ESG disclosures. After receiving over 400 comment letters in response to Commissioner Allison Herren Lee’s May 2021 call for public input, Chair Gensler said the agency is in the process of developing recommendations and is considering developing disclosure requirements for companies that have made forward-looking climate-related commitments or that operate substantially in jurisdictions with federal mandates on climate goals. Chair Gensler’s remarks came just one month after President Biden’s Executive Order called for federal agencies to take wide-ranging actions regarding climate-related financial risks. The full text of Chair Gensler’s remarks is available [here](#). The full text of the Executive Order is available [here](#).
- **Engine No. 1 Activists Target ExxonMobil’s Board:** On May 26, 2021, activist hedge fund Engine No. 1 succeeded in electing two new directors to ExxonMobil’s board, and confirmed the win of a third seat on June 2. Though Engine No. 1 owns just 0.02% of Exxon’s stock, its campaign thesis of bolstering performance through prioritizing a response to climate change drew shareholder support, in part, due to the ESG priorities of large institutional investors. Engine No. 1’s letter to ExxonMobil’s board is available [here](#).
- **EEO-1 Disclosure Shareholder Votes:** Shareholder proposals to publicly disclose EEO-1 data have gained strong support during this year’s proxy season. Companies with at least 100 employees are required to file confidential annual EEO-1 reports to the Equal Employment Opportunity Commission, which includes data on workplace demographics and the racial, ethnic and gender composition of employees. Companies, including Union Pacific Corp., Nike Inc., Moody’s Investors Service Inc., and Walmart Inc., have been pressed by their shareholders to release their EEO-1 data. As of June 1, 2021, ten shareholder proposals that requested that companies disclose their EEO-1 data have gone to a vote. On April 27, 2021, IBM Corp.’s shareholders successfully voted 94% in favor of annual diversity, equity and inclusion reporting. The full text of IBM’s 2021 proxy statement, which urged shareholders to vote in favor of the proposal, is available [here](#).

The entire collection of Sullivan & Cromwell memoranda on corporate governance topics and issues is available [here](#).