

**Practice
Guides**

DIVERSITY AND INCLUSION

Contributing Editor
Timothy Chow



LEXOLOGY

Getting the Deal Through

DIVERSITY AND INCLUSION

Practice Guide

Contributing Editor
Timothy Chow

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1

Shareholder Derivative Actions in the United States

Timothy Chow, Sharon Nelles and Katharine Rodgers¹

Introduction

In recent years, there has been an increased focus on corporate America's commitments to environmental, social and governance (ESG) goals, including diversity, equity and inclusion (DEI). The general public, as well as investors, lawmakers and regulators have called for companies to demonstrate a commitment to DEI. A few states have passed laws requiring increased board diversity and the US Securities and Exchange Commission (SEC) has proposed rules concerning ESG disclosures. In response to these calls, many companies have committed to improving DEI. These commitments, however, are not without risk and, if a company's actions fall short of its DEI commitments, there can be numerous consequences, including shareholder derivative suits.

Against the backdrop of pressure on corporate America to commit to and improve DEI, this chapter discusses shareholder derivative actions in the US, focused on boards' alleged failures to follow through on commitments to DEI. It also outlines certain takeaways for boards and corporations when committing to DEI efforts.

All stakeholders increase their focus on DEI in corporate America

Corporate America is facing increasing pressure from stakeholders to implement and report ESG initiatives. The general public, customers and consumers, shareholders, lawmakers and regulators each have tools to push companies to make ESG a priority. ESG represents the moral, ethical and cultural standards to which a company has committed. The 'environmental' part of ESG includes a company's approach to climate change and sustainability, such as initiatives to preserve natural resources or reduce or offset its carbon footprint. 'Governance' encapsulates a company's ethical standards for its employees and management, and includes compensation, shareholder rights and management remuneration. 'Social' incorporates a company's approach

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to its employee relations, including DEI efforts, working conditions, employee safety and wellness benefits and consumer protection. To the extent DEI efforts focus on diversity at the board and executive levels, these can also be considered governance.

Recent social movements, including #MeToo and Black Lives Matter, have only heightened the focus on DEI in corporate America. The #MeToo movement, which began as a social movement against sexual abuse and sexual harassment, has expanded to encompass gender discrimination and retaliation. Black Lives Matter was initially aimed at combating police brutality against Black people and similarly has expanded to highlight racism, discrimination and inequality experienced by Black people.

In the past, companies have responded to allegations of discrimination or misconduct by separating from (through firing or resignation) the 'bad apple' employees.² Although, after an internal investigation, such actions may still be a necessary response, they are no longer sufficient. Corporate stakeholders are exerting pressure on companies to do more to:

- stop and prevent harassment, misconduct, discrimination and retaliation; and
- commit to and improve DEI within corporate America.

Public pressure

Consumers are using their wallets to communicate their values to companies. A 2018 survey found that 'nearly two-thirds (64 per cent) of consumers around the world now buy on belief', meaning they 'will choose, switch, avoid or boycott a brand based on where it stands on the political or social issues they care about'.³

Consumers have always had the power to boycott companies that do not align with their values. In recent years, however, there has been a rise of consumer boycotts related to DEI. For example, in response to allegations of sexual harassment and lack of HR response at Uber, 'waves of customers deleted Uber's app'.⁴

In addition to consumer boycotts, companies may respond to consumer pressure to boycott another company or otherwise take action that they believe is consistent with their own stated DEI principles. For example, in response to Facebook's purported failures to appropriately monitor speech on its platforms, numerous companies suspended their advertising on Facebook.⁵

2 See, for example, Tim Stelloh, Claire Atkinson and James Rainey, Hollywood Mogul Harvey Weinstein Fired Amid Sexual Harassment Allegations, *NBC News*, 8 October 2017, www.nbcnews.com/storyline/sexual-misconduct/hollywood-mogul-harvey-weinstein-fired-amid-sexual-harassment-allegations-n808881; Transcript: Firing of Matt Lauer Announced on 'Today', *New York Times*, 29 November 2017, www.nytimes.com/2017/11/29/business/media/matt-lauer-today-show.html; Jemima McEvoy, Every CEO and Leader that Stepped Down Since Black Lives Matter Protests Began, *Forbes*, 1 July 2020, www.forbes.com/sites/jemimamcevoy/2020/07/01/every-ceo-and-leader-that-stepped-down-since-black-lives-matter-protests-began/?sh=332314905593.

3 See Edelman, *Earned Brand 2018*, 2 October 2018, www.edelman.com/earned-brand.

4 Lydia Dishman, This 'Me Too' Timeline Shows Why 2017 Was a Reckoning for Sexism, *Fast Company*, 6 December 2017, www.fastcompany.com/40504569/this-me-too-timeline-shows-why-2017-was-a-reckoning-for-sexism.

5 Micah Maidenberg, Facebook Sees Growing Ad Boycott in Protest Against Handling of Speech, *Wall Street Journal*, 30 June 2020, www.wsj.com/articles/clorox-to-halt-facebook-ads-through-year-end-joining-advertiser-push-on-content-11593459934; see also Suzanne Vranica, Disney Slashed Ad

Employees

Companies also risk employee demonstrations, and the related news coverage, if they fail to take DEI seriously. For example, in response to allegations of mishandling of sexual misconduct claims, Google employees around the world staged a series of walkouts.⁶ Pinterest employees also staged a virtual walkout in August 2020 to express solidarity with three former co-workers who accused Pinterest of racial and gender discrimination and retaliation.⁷

Institutional investors

Prominent institutional investors also have stated that board diversity is a priority for them.⁸ The 30% Club, whose 'mission is to reach at least 30% representation of all women on all boards and C-suites globally,'⁹ counts prominent institutional investors, such as BlackRock, State Street and Vanguard among its US members.¹⁰

Proxy advisers

Similarly, proxy advisory firms, which have significant influence over how investors vote, factor DEI into their advice. For example, Institutional Shareholder Services Inc (ISS)'s 2021 US Proxy Voting Guidelines recommend that shareholders 'generally vote for proposals requesting a company disclose its diversity policies or initiatives'.¹¹

Lawmakers and regulators

Lawmakers and regulators have also contributed to the focus on ESG and DEI. For example, on 30 September 2020, California Governor Gavin Newsom signed into law a new diversity requirement for boards of directors of public companies, requiring foreign and domestic public companies with their principal executive offices in California to have at least one director from an underrepresented community on their boards by the end of 2021.¹² Depending on the size of their boards, these companies may need to have additional directors from underrepresented

Spending on Facebook Amid Growing Boycott, *Wall Street Journal*, 18 July 2020, www.wsj.com/articles/disney-slashed-ad-spending-on-facebook-amid-growing-boycott-11595101729.

6 Dave Lee, Google Staff Walk Out Over Women's Treatment, *BBC*, 1 November 2018, www.bbc.com/news/technology-46054202.

7 Erin Griffith, Pinterest Employees Demand Gender and Race Equality, *New York Times*, 14 August 2020, www.nytimes.com/2020/08/14/technology/pinterest-walkout-equality.html.

8 See, for example, BlackRock Investment Stewardship, Our Approach to Engagement on Board Diversity, March 2021, www.blackrock.com/corporate/literature/publication/blk-commentary-engaging-on-diversity.pdf ('We believe that a proactive approach to managing diversity needs to be taken by all boards. A shift in mindset may be necessary in some companies, particularly for those that have yet to view board diversity as a performance imperative in today's dynamic corporate boardroom and work environment.').

9 30% Club, Our Mission, <https://30percentclub.org/about/who-we-are>.

10 US 30% Club, About, <https://us.30percentclub.org/about/>.

11 See ISS, *United States Proxy Voting Guidelines, Benchmark Policy Recommendations*, at 62, 19 November 2020, www.issgovernance.com/file/policy/latest/americas/US-Voting-Guidelines.pdf.

12 Dylan Bruce and Peter Rasmussen, Analysis: Mandated Board Diversity Takes Center Stage in 2021, *Bloomberg Law*, 16 November 2020, <https://news.bloomberglaw.com/bloomberg-law-analysis/analysis-mandated-board-diversity-takes-center-stage-in-2021>; Cal Corp Code § 301.4.

communities by the end of 2022.¹³ As another example, in December 2019, New York enacted a 'Women on Corporate Boards Study' law requiring domestic and foreign corporations authorised to do business in New York to report the total number of directors appointed to their boards and the number who are female.¹⁴ A study analysing the change in the number of female directors over time and the total percentage of women on boards will be published by 1 February 2022.¹⁵ While California and New York are some of the first states to act, boards should expect similar laws from other states.

At the federal level, on 16 June 2021, the US House of Representatives passed legislation 'that would require public companies to report [ESG] metrics, betting that shareholders will use the information to pressure corporations on climate risk and other issues'.¹⁶ The bill is currently with the US Senate.¹⁷ It 'would require publicly traded companies to disclose and define ESG metrics' as well as 'their view on the link between ESG and long-term business performance'.¹⁸ In terms of DEI, the bill would require disclosing:

- 'the race, ethnicity, gender, sexual orientation and veteran status of board members and executives;
- 'workforce-related information, including diversity, safety and pay;
- 'settlements or judgments connected to workplace harassment'.¹⁹

US regulators have also indicated an increased commitment to ESG, including DEI. The SEC recently announced the creation of a Climate and ESG Task Force in its Enforcement Division, which, 'consistent with increasing investor focus and reliance on climate and ESG-related disclosure and investment, . . . will develop initiatives to proactively identify ESG-related misconduct'.²⁰ The SEC is also intending to propose new rules in October 2021 aimed at enhancing disclosures concerning human capital management,²¹ which could include metrics on workforce turnover, compensation, benefits and workforce demographics,²² and the diversity of board members and

13 Dylan Bruce and Peter Rasmussen, Analysis: Mandated Board Diversity Takes Center Stage in 2021, *Bloomberg Law*, 16 November 2020, <https://news.bloomberglaw.com/bloomberg-law-analysis/analysis-mandated-board-diversity-takes-center-stage-in-2021>.

14 *ibid.*

15 Teri Wilford Wood and Anna Broccolo, New York Enacts Legislation Related to Board Diversity, *National Law Review*, Vol X, No. 17, 17 January 2020, www.natlawreview.com/article/new-york-enacts-legislation-related-to-board-diversity.

16 Laura Weiss, House Passes ESG, Climate Disclosure Rules for Public Companies, *Roll Call*, 16 June 2021, www.rollcall.com/2021/06/16/house-passes-esg-climate-disclosure-rules-for-public-companies/.

17 117th Cong (2021–2022), HR 1187 – Corporate Governance Improvement and Investor Protection Act, www.congress.gov/bill/117th-congress/house-bill/1187/all-actions?overview=closed#tabs.

18 HR 1187, 117th Cong (2021–2022); Laura Weiss, *op cit* at footnote 16.

19 Laura Weiss, *op cit* at footnote 16.

20 Press Release, SEC, SEC Announces Enforcement Task Force Focused on Climate and ESG Issues (4 March 2021), www.sec.gov/news/press-release/2021-42.

21 Office of Information and Regulatory Affairs, Human Capital Management Disclosure, Spring 2021, www.reginfo.gov/public/do/eAgendaViewRule?pubId=202104&RIN=3235-AM88.

22 Speech, SEC Chair Gary Genster, Prepared Remarks at London City Week, 23 June 2021, www.sec.gov/news/speech/genster-speech-london-city-week-062321.

nominees.²³ Furthermore, the SEC recently approved Nasdaq's Board Diversity Rule requiring listed companies to have at least two diverse board members or explain their failure to meet the requirement, with certain exceptions.²⁴

Boards should continue to watch for developments from lawmakers and regulators in this space. While the E of ESG, particularly as it relates to climate change, is front and centre of these new regulations, DEI is a close second. This is, in part, because a company's efforts to affect climate change and diversity are more measurable than other ESG goals, such as employee well-being or management's ethical standards. We anticipate that the US legislation (if it passes the Senate) and the SEC's Climate and ESG taskforce and the resulting required corporate disclosures will be followed by investigations and litigation initiated by federal agencies, such as the SEC and the US Equal Employment Opportunity Commission. There is likely to also be a rise in shareholder derivative litigation focused on ESG, so it is important for corporations to understand the current state of play in diversity-driven derivative actions.

Novel diversity-driven shareholder derivative actions

In response to the increasing pressure on corporate America to commit to ESG, including DEI, many companies have made public commitments to DEI. CEO Action for Diversity and Inclusion, which 'was founded on a shared belief that diversity, equality and inclusion is a societal issue, not a competitive one, and that collaboration and bold action from the business community . . . is vital to driving change at scale', has nearly 2,000 CEO signatories committing to advance DEI in the workplace.²⁵ Likewise, companies have made statements committing to certain DEI goals. For example, Salesforce announced initiatives aimed at (among other things) encouraging open dialogues on DEI issues, recruiting and promoting individuals from underrepresented minorities, and supporting efforts to diversify its supplier base.²⁶ Nike made a 'US\$40 million commitment over . . . four years to support the Black community in the US', which 'will be focused on investing in and supporting organizations that put social justice, education and addressing racial inequality in America at the center of their work'.²⁷ Nike also said it had 'stepped up [its] own efforts and measures of accountability in the areas of Diversity, Inclusion and Belonging to foster an inclusive environment and attract a more diverse workforce' and committed itself to sharing its 'progress in these areas annually through the Nike Impact Report'.²⁸

23 Office of Information and Regulatory Affairs, Corporate Board Diversity, Spring 2021, www.reginfo.gov/public/do/eAgendaViewRule?publd=202104&RIN=3235-AL91.

24 Public Statement, SEC Chair Gary Gensler, Statement on the Commission's Approval of Nasdaq's Proposal for Disclosure About Board Diversity and Proposal for Board Recruiting Service, 6 August 2021, www.sec.gov/news/public-statement/gensler-statement-nasdaq-proposal-disclosure-board-diversity-080621; see also SEC Release No. 34-92590 (6 August 2021), www.sec.gov/rules/sro/nasdaq/2021/34-92590.pdf.

25 CEO Action for Diversity & Inclusion, Purpose, www.ceoaction.com/purpose/.

26 Press Release, Salesforce, Taking Action for Racial Equality and Justice (10 June 2020), www.salesforce.com/news/stories/taking-action-for-racial-equality-and-justice/.

27 Press Release, Nike Inc, Nike, Inc Statement on Commitment to the Black Community (5 June 2020), <https://news.nike.com/news/nike-commitment-to-black-community>.

28 *ibid.*

While efforts to improve DEI in corporate America are laudable, companies and the boards that oversee them should be aware of the risks of making commitments without any real plan to follow through on them. Failure to prioritise and adhere to DEI commitments leaves a company vulnerable to actions from numerous stakeholders.

Within this environment, in addition to efforts to fill company boards with ESG-minded directors, investors have started to bring derivative actions against boards for failures to take seriously their commitments to DEI. These derivative suits typically follow a basic formula: shareholders allege that boards breached their fiduciary duties to a company and/or securities laws by failing to carry out commitments to DEI and/or creating, tolerating or ignoring gender and race discrimination. Because ESG issues often relate to high-profile incidents, a company's reputation, and often its long-term financial wellbeing, may be at stake in ESG derivative suits. ESG topics have included, but are not limited to, DEI, gender and race discrimination and retaliation. These topics have inspired recent shareholder derivative actions against companies including Facebook, as described below.

In July 2020, a wave of novel diversity-driven derivative actions emerged, in which shareholder plaintiffs alleged that the defendant directors touted the companies' commitment to DEI yet failed to act on these commitments. One of the first of these cases was filed against Facebook,²⁹ and nearly a dozen largely similar actions were filed in the following months (many by the same firm).³⁰ We shall examine the *Facebook* litigation as a lens through which boards can better understand this novel type of diversity-driven derivative action, including the types of statements that could form a basis for a similar derivative suit, the court's rationale in dismissing the action and what boards can do to minimise the risk of a diversity-driven derivative action.

The Facebook case

In the *Facebook* action, the plaintiff alleged (among other things) that members of the board and executive management team, who remain mostly white save one Black board member, breached their fiduciary duties and violated federal securities law by failing to diversify Facebook's board of directors, executives and workforce, despite company statements committing to diversity.³¹ The plaintiff sought various forms of relief, including:

- immediate resignation of a number of directors and inclusion of minorities in the replacement applicants;
- disgorgement by directors of their compensation (to be donated to a charity focused on the advancement of minorities);
- the creation of a fund committed to the advancement of minorities at the company;
- annual diversity training; and

29 See *Ocegueda v Zuckerberg*, No. 20-cv-04444, 2020 WL 3642982 (ND Cal, 2 July 2020) (Facebook Compl).

30 See, for example, *Klein v Ellison*, No. 20-cv-04439, 2020 WL 3816836 (ND Cal, 2 July 2020) (defendant Oracle); *Kiger v Mollenkopf*, No. 20-cv-01355 (SD Cal, 17 July 2020) (defendant Qualcomm, Inc); *Lee v Fisher*, No. 20-cv-06163 (ND Cal, 1 September 2020) (defendant The Gap, Inc); *Falat v Sacks*, No. 20-cv-01782 (CD Cal, 18 September 2020) (defendant Monster Beverage Corp); *In re Danaher Corp Shareholder Deriv Litig*, No. 20-cv-02846, (DDC, 6 October 2020) (defendant Danaher Corp).

31 Facebook Compl at ¶¶7–12.

- revision of the executive compensation structure to make a percentage of executive compensation tied to the achievement of diversity goals.³²

The plaintiff argued that: 'Platitudes in proxy statements are not progress'.³³ The plaintiff alleged that Facebook's board 'deceived stockholders and the market by repeatedly making false assertions about the Company's commitment to diversity',³⁴ and cited the company's 2019 and 2020 proxy statements, including:

- Facebook's statement on diversity and inclusion in its 2019 proxy statement, which said, in part:

We are committed to building a workforce that is as diverse as the communities we serve. We support an open culture and encourage our workforce to bring their authentic selves to work.

We publish our global gender diversity and US ethnic diversity workforce data annually. . . . To support our goals of diversifying our workforce, we globally rolled out our Diverse Slate Approach, which sets the expectation that hiring managers will consider candidates from under-represented backgrounds when interviewing for an open position. . . . We also continue to expand our recruiting team and develop internship programs for women and minorities. . . .

We believe retention, people development, and inclusion are just as crucial as recruiting. This is why we invest in our thriving Facebook Resource Groups and our annual Community events such as Women's Community Summit, Black Community Summit, Latin Community Summit, and Pride Community Summit. . . . We encourage all employees to take our 'Managing Unconscious Bias' training to help reduce the effects of bias in the workplace and to help employees better understand diverse perspectives. . . .

We are committed to a policy of inclusiveness and to pursuing diversity in terms of background and perspective when evaluating candidates for membership on our board of directors. . . .

*We are also committed to promoting diversity among the companies that do business with Facebook. . . .*³⁵

- The statement in Facebook's 2020 proxy statement: 'We have an obligation to build a culture of inclusion where everyone can thrive'.³⁶

The plaintiff contended that, despite these statements, Facebook and its board 'failed to act in the face of numerous "red flag" warnings indicating the Company's internal controls and policies were not only insufficient, but actually fostered . . . discriminatory practices, a lack of diversity on the Board and among the Company's executive ranks, and the Company's repeated failure to stop hate speech that resulted in a massive boycott by advertisers'.³⁷ The purported red flags, as the court described them, generally related to Facebook's 'lack of diversity (on the board, in

32 *ibid* at ¶30.

33 *ibid* at ¶25.

34 *ibid* at ¶12.

35 *ibid* at ¶52.

36 *ibid* at ¶53.

37 *ibid* at ¶55.

senior management, and in its workplace), its discriminatory advertising, and its failure to curb hate speech,' and the complaint cited a range of specific examples, including:

- news articles describing diversity and discrimination problems at the company;
- CEO Mark Zuckerberg's testimony before the US Senate Judiciary and Commerce Committees concerning Facebook's purported allowance of discriminatory housing ads; and
- criticism of Facebook 'by its own employees for refusing to censor or moderate' certain posts.³⁸

On 19 March 2021, the court granted Facebook's motion to dismiss the derivative action, though it did permit the plaintiff an opportunity to amend her complaint as to the federal securities law claim.³⁹ The court dismissed the plaintiff's claims on three separate grounds:

- First, the court held that the plaintiff failed to plead demand futility with the requisite particularity because the plaintiff failed to allege facts adequately demonstrating that:
 - the board would face substantial liability for ignoring 'red flags';
 - the board would face substantial liability for having approved the representations in Facebook's proxy statements about its commitment to DEI; or
 - Facebook's leadership was unable to 'exercise independent and disinterested judgment'.
- Second, the court dismissed the plaintiff's state law claims because Facebook's certificate of incorporation contained a forum selection clause requiring such claims to be filed in Delaware.
- Third, in analysing the federal claim, the court held that the alleged misrepresentations were 'non-actionable puffery or aspirational (and hence immaterial)', 'the plaintiff did not plead plausible facts about discriminatory practices in advertising, hiring, and pay that render[ed] the statements misleading', and the plaintiff failed to demonstrate a causal connection between those statements and her alleged losses.⁴⁰

Following the Facebook court

Other courts have followed the *Facebook* court's lead and dismissed these recent actions on similar grounds.⁴¹ These cases exemplify the difficulty (and in some cases viability) of using litigation to force company boards to engage in ESG initiatives. These cases suggest that:

- demand futility is a high hurdle for plaintiffs;
- aspirational statements about DEI may be non-actionable puffery; and
- forum selection clauses in company charters and by-laws are likely to be enforceable.

38 *Ocegueda v Zuckerberg*, No. 20-cv-04444, F Supp 3d, 2021 WL 1056611 (ND Cal, 19 March 2021); Facebook Compl at ¶¶54-89.

39 *Ocegueda v Zuckerberg*, as footnote 38.

40 *ibid*. After the plaintiff confirmed that she did not intend to amend her complaint, the court entered judgment in favour of the defendants. See *Ocegueda v Zuckerberg*, No. 20-cv-04444 (ND Cal, 2 June 2021).

41 See, for example, *Lee v Fisher*, No. 20-cv-06163, 2021 WL 1659842 (ND Cal, 27 April 2021) (The Gap; dismissed owing to forum selection clause); *Klein v Ellison*, No. 20-cv-04439, 2021 WL 2075591 (ND Cal, 24 May 2021) (Oracle; dismissed on grounds of failure to demonstrate demand futility (including that aspirational DEI-related statements were non-actionable) and a forum selection clause for state law claims); *In re Danaher Corp Shareholder Deriv Litig*, Nos. 20-cv-02445, 20-cv-02846, F Supp 3d, 2021 WL 2652367 (DDC, 28 June 2021) (Danaher; dismissed for failure to adequately plead demand futility).

Despite these successes, however, boards should continue to focus on DEI disclosures.

Takeaways for boards

Boards, and those who advise them, should expect a continued focus on DEI initiatives from all stakeholders. Directors should consider the allegations in the recent derivative actions and assess how their company would fare if subjected to similar criticisms. Even if a shareholder derivative action were ultimately unsuccessful, it would not be without its costs, including:

- costs and fees associated with mounting a defence;
- the risk of negative publicity and potential reputational harm and loss of goodwill;
- employee reactions to any allegations; and
- consumer reactions to negative publicity, including risks of consumer boycotts that could have an impact on a company's bottom line.

In assessing how a company would fare in a diversity-driven derivative action, board members should consider a variety of factors that may precede such a suit.

Books and records demands

Boards may encounter an increasing number of shareholder demands for books and records concerning DEI, which may be a precursor to a shareholder derivative action. To inspect books and records, a plaintiff must prove by a preponderance of evidence that he or she is a stockholder; that he or she has complied with the technical requirements of Delaware General Corporation Law Section 220, including affirming his or her status as a stockholder under oath with documentation; and that he or she has a proper purpose.⁴² Under Section 220, stockholders of a Delaware corporation can inspect the corporation's stock ledger, a list of its stockholders, its other books and records and a subsidiary's books and records.

Recent developments in Delaware reflect a trend of shareholder-friendly jurisprudence. This trend can be seen through recent Delaware case law, which lowers the stockholder's burden of proving a proper purpose.⁴³ Additionally, recent Delaware case law has permitted stockholders to use Section 220 demands as a vehicle for discovery before even filing a complaint.⁴⁴ Books and records should be taken seriously and boards should consult legal counsel and other advisers in carefully considering their response to such demands.

42 *Woods Tr of Avery L Woods Tr v Sahara Enters Inc*, 238 A.3d 879 (Del Ch, 2020); DGCL §220.

43 See *AmerisourceBergen Corp v Lebanon Cty Emps' Ret Fund*, 243 A.3d 417 (Del, 2020); see also Sullivan & Cromwell LLP Memorandum, Delaware Supreme Court Affirms Order to Produce Documents and Submit to Deposition in Section 220 Litigation, 21 December 2020, www.sullcrom.com/files/upload/SC-Publication-Delaware-Supreme-Court-Order-Produce-Documents-Deposition-Section-220-Litigation.pdf.

44 William Savitt, Sarah K Eddy and Cynthia Fernandez Lumermann, Section 220 as Pre-Complaint Discovery – Recent Developments, Harv L Sch Forum on Corp Governance, 15 December 2020, <https://corpgov.law.harvard.edu/2020/12/15/section-220-as-pre-complaint-discovery-recent-developments/>.

Record-keeping

In anticipation of books and records demands, boards should assess their record-keeping practices to ensure they are sufficient to respond to shareholder demands. This includes keeping and reviewing for accuracy contemporaneous board minutes.

Privilege

In the same vein, boards should evaluate whether any discussions or reviews of DEI efforts should include their in-house or outside counsel and, if so, how to ensure privilege over such conversations.

DEI statements

Boards should bear in mind a few issues when reviewing past statements concerning DEI. First, boards should consider whether their statements concerning commitments to DEI align with what the company is willing – and able – to do. Second, boards may want to assess whether prior statements express general support for DEI efforts or are promises of specific action. In other words, are they non-actionable aspirational statements, as in the *Facebook* case, or are they guarantees of specific actions and outcomes? If the latter, the board should consider whether these actions are being taken and the company is on track to meet the outcomes. Third, boards should also consider whether these statements contain appropriate disclosures.

Going forward, boards should bear each of these in mind when making future commitments to DEI. This is not to say that boards and companies should shy away from DEI efforts. These are laudable commitments, which some may argue are necessary for a company to continue to operate in the current climate. But, once boards make commitments to DEI, they must follow through. Mere platitudes are insufficient to protect a company and, in fact, may do more harm than good.

When assessing their current DEI commitments and potential future ones, boards should consider several possible actions. The relief sought in the diversity-driven derivative actions already filed provides a helpful guide to boards on possible next steps to improve DEI.

Statutory and regulatory requirements

At a minimum, companies need to comply with applicable federal, state and local employment laws and disclosure requirements. In anticipation of increased scrutiny from regulators regarding compliance with these laws, companies should undertake a review of their current policies and procedures to ensure compliance with the most recent laws and regulations. Companies may also want to review their compliance programmes to ensure they are functioning as intended. If any issues are identified, companies should promptly remedy them.

Periodic reviews of progress

Once a company commits to DEI efforts, it should implement a process, including board review, for periodic reporting and review of progress towards DEI goals.

Policies and procedures

In addition to regular training, boards should review their company's policies and procedures surrounding DEI, including employment practices, complaints concerning and investigations of misconduct and anti-retaliation. Boards should consider whether such policies and procedures

are being effectively implemented and enforced throughout the company – in each business group or division and at all levels of seniority. Boards should regularly undertake these reviews – once is not enough.

Complaints and misconduct

As an extension of their review of current policies and procedures, boards should assess the process for handling complaints of alleged misconduct and findings of misconduct. A company should have a process for employees to report allegations of misconduct, including complaints of discrimination, harassment or retaliation. If possible, employees should have various reporting channels, such as their manager and a human resources contact, in case the complaint concerns one of these individuals. Companies should endeavour to keep such complaints confidential, as much as possible, and should reassure employees of the same. Companies should also have procedures in place for investigating such allegations. In certain instances, a company may want to engage an outside law firm to conduct the investigation.

If a complaint is substantiated, companies should address the misconduct – regardless of who the perpetrator is and his or her rank in the company. Discipline, up to and including dismissal, should be doled out consistently for the same or similar instances of misconduct. One of the issues in recent litigation involving Google was that punishments were inconsistently meted out, seemingly dependent on an employee's position.⁴⁵

By punishing misconduct, companies demonstrate a commitment to DEI and send a message to employees that the company will not tolerate discrimination, harassment or retaliation – regardless of an employee's role within the company.

Board diversity

Current (and probably forthcoming) regulations and laws focus on the diversity of the board itself.⁴⁶ Boards should self-reflect and determine whether they have racial and gender diversity among them and, if not, steps to take to increase their own diversity, such as opening or creating seats for diverse directors. When recruiting new board members, boards should recruit from a diverse pool of candidates and, if necessary, should hire an outside consultant or recruitment firm to assist them in these efforts.

Compensation benchmarks

Boards may want to consider tying a portion of executive compensation to the achievement of DEI goals. In the *Facebook* action, the plaintiff demanded 30 per cent of an executive's compensation be tied to the achievement of such goals.⁴⁷

45 Julia Carrie Wong, Google Board Tried to Cover Up Sexual Misconduct, Shareholders Allege, *Guardian*, 10 January 2019, www.theguardian.com/technology/2019/jan/10/google-sexual-harassment-shareholder-lawsuit-alphabet.

46 See footnotes 12 to 24.

47 See Facebook Compl at ¶30(f).

DEI training

Boards also may want to implement periodic training on DEI topics, including anti-discrimination, anti-harassment and anti-retaliation. Such training should be given to all departments and all levels of the company, including executives. Boards should further consider receiving DEI training themselves. As with many of these steps, once is not enough– training should recur periodically.

Chief diversity officer

If their company does not already have a chief diversity officer, boards may want to consider hiring one. A chief diversity officer is tasked with advancing DEI within the company. If hired, the chief diversity officer must be more than just a figurehead; he or she should be given the authority and resources to advance the company's DEI goals.

DEI committee

Additionally, boards may want to create a board committee with a DEI focus. This committee could lead the board's periodic review of the company's DEI progress and be tasked with any follow-up items. It also could undertake the recommended periodic reviews of company statements, policies and procedures and complaints and misconduct.

Conclusion

With the heightened focus on DEI across corporate America, boards should expect increased calls to action from various stakeholders. When determining how to foster diverse, equal and inclusive workplaces and promote DEI within their company, boards should bear in mind the risks that come from making broad commitments to diversity without concrete plans to act. Boards should be prepared to act on their DEI commitments and, in doing so, should bear in mind the various legal, reputational and other risks if they fail to meet such commitments.

Appendix 1

About the Authors

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Tim Chow is the chief business integrity officer and general counsel commercial at Diageo plc. Since joining Diageo in 2004, he has held a number of corporate and geographically specific accountabilities at the company, most recently as general counsel for Diageo's Latin American and Caribbean and Global Travel operations. Mr Chow has been involved in various causes aimed at advancing issues of concern to the LGBTQ+ community and, from 2010 to 2019, he served as a board and executive committee member of the Lesbian, Gay, Bisexual and Transgender Community Center of New York. In 2018 he was recognised by the *Financial Times* and *OUTstanding* as one of the LGBTQ+ 100 Leading Executives and, in 2019, received the *Chambers* LGBTQ+ Equality Lawyer of the Year Award.

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