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Navigating Proxy Season with SEC Disclosure Mandates and Litigation Risks Lurking

April 28, 2022

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Presenters



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SEC ESG-Related Regulations / Proposals

- **Stock Repurchase Proposal**
- **Insider Trading Proposal**
- **Cybersecurity Risk Disclosure Proposal**
- **Talent Management/Human Capital**
 - ▶ Existing requirements
 - ▶ Additional rule-making expected
- **Climate Disclosure Proposal** (March 21, 2022)
 - ▶ (in addition to 2010 Climate Disclosure Guidance and 2021 SEC comment letters)
- **Existing Executive Compensation Rules** (as applied to ESG-related metrics)
- **Existing Disclosure Requirements re: Non-GAAP and Key Performance Indicators** (as applied to ESG-related metrics)
- **E&S Shareholder Proposals**



Litigation and Regulatory/Enforcement Risks

Theme: accuracy of disclosures and marketing claims

Private Litigation Claims

- Antifraud provisions of the securities laws
- Lanham Act and “greenwashing” claims
- Misrepresentation and breach of warranty
- Regulatory and Enforcement Actions

Regulatory and Enforcement Actions

- **SEC**
 - ▶ For issuers, disclosure issues
 - ▶ For advisors, claims of ESG-conscious investing
- **FTC**
 - ▶ Consumer fraud/greenwashing
- **CFTC**
 - ▶ 2021 formation of Climate Risk Unit to “focus on the role of derivatives in understanding, pricing, and addressing climate-related risk and transitioning to a low-carbon economy”

Environmental and Social Shareholder Proposals

2022 E&S Shareholder Proposal Trends¹

Filings are up

- Filings of E&S resolutions have already exceeded the number filed in 2021
 - ▶ Over 500 E&S resolutions have been filed in 2022
 - ▶ 3 of the 4 most common shareholder proposal topics address E&S issues
 - Last year the top 5 most common shareholder proposal topics all addressed traditional governance issues

Diversity and Climate Change take center stage

- Racial justice and carbon emissions are predominant themes
 - ▶ These are the 2nd and 3rd most common shareholder proposal topic in 2022
 - ▶ As of April 1st, there were 55 racial justice/civil rights audit/report and 54 GHG emissions reduction shareholder proposals filed, which would have made them the 2nd and 3rd most common shareholder proposal filed in all of 2021

Governance topics remain a key focus for serial filers

- John Chevedden, Kenneth Steiner, James McRitchie, and Myra Young are focusing on special meeting rights
 - ▶ As of April 1st, special meeting rights was the most common shareholder proposal topic with 78 filed resolutions (up from 39 in all of 2021)
 - ▶ Written consent was the most common shareholder proposal topic in 2021 (84)

Environmental and Social Shareholder Proposals

2022 E&S Shareholder Proposal Trends¹

Early votes suggest 2022 could see record number of majority votes

- As of April 1st, 9 shareholder proposals received majority support
 - ▶ Last year, 39 E&S shareholder proposals received majority support (record number)
 - ▶ 2 special meeting and 2 racial equity/civil rights audit proposals have already received majority support this year

Withdrawals are up, while omissions are down

- No action requests are also down compared to 2021
- Investor and advisory firm policy shifts/changing expectations are leading companies to engage with proponents
- Revised SEC guidance is making ordinary business exclusions more challenging

Surge in new shareholder proposal topics

- Particularly prominent for environmental and social proposals
 - ▶ Some of the new topics include worker rights, employee welfare, concealment clauses in employment contracts, and COVID-19 vaccine distribution

*1 2022 Proxy Season Preview, Shirley Westcott, Alliance Advisors' April 2022 Newsletter,
<https://www.allianceadvisors.com/newsletters/2022-proxy-season-preview>*

Environmental and Social Shareholder Proposals

Top 10 Shareholder Proposal Filings: 2021-2022 ¹

Table 1: Top 10 Shareholder Proposal Filings: 2021-2022

Proposal	2022 (as of April 1)	Proposal	2021 (full year)
Special meetings	78	Written consent	84
Racial justice/civil rights audit/report	55	Independent chairman	47
GHG emissions reduction	54	Supermajority voting	40
Grassroots lobbying	44	Special meetings	39
Independent chairman	37	Proxy access	38
Finance and climate change	27	Workplace diversity (EEO-1 report)	38
Proxy access	25	Grassroots lobbying	37
Workplace diversity (DEI report)	24	Carbon transition planning	32
Political spending	23	Political spending	31
Lobbying alignment on climate change	20	Workplace diversity (DEI report)	30

Source: SEC filings, proponent websites and media reports.

¹ 2022 Proxy Season Preview, Shirley Westcott, Alliance Advisors' April 2022 Newsletter, <https://www.allianceadvisors.com/newsletters/2022-proxy-season-preview>

Environmental and Social Shareholder Proposals

Shareholder Proposal Majority Votes: 2022 (as of April 1) ¹

Proposal	Company	Vote*
Special meetings	Agilent Technologies	81.7%
Special meetings	Becton, Dickinson	55.1%
Hold virtual meetings	Jack in the Box*	69.0%
Gender/racial pay equity	Walt Disney	59.6%
GHG emissions reduction	Costco Wholesale	69.9%
Sustainable packaging	Jack in the Box	95.4%
Racial equity/civil rights audit	Apple	53.5%
Racial equity/civil rights audit	Maximus	64.2%
Sexual harassment policies	Apple	50.04%

Note: Vote results are calculated as “for” votes as a percentage of “for” and “against” votes.

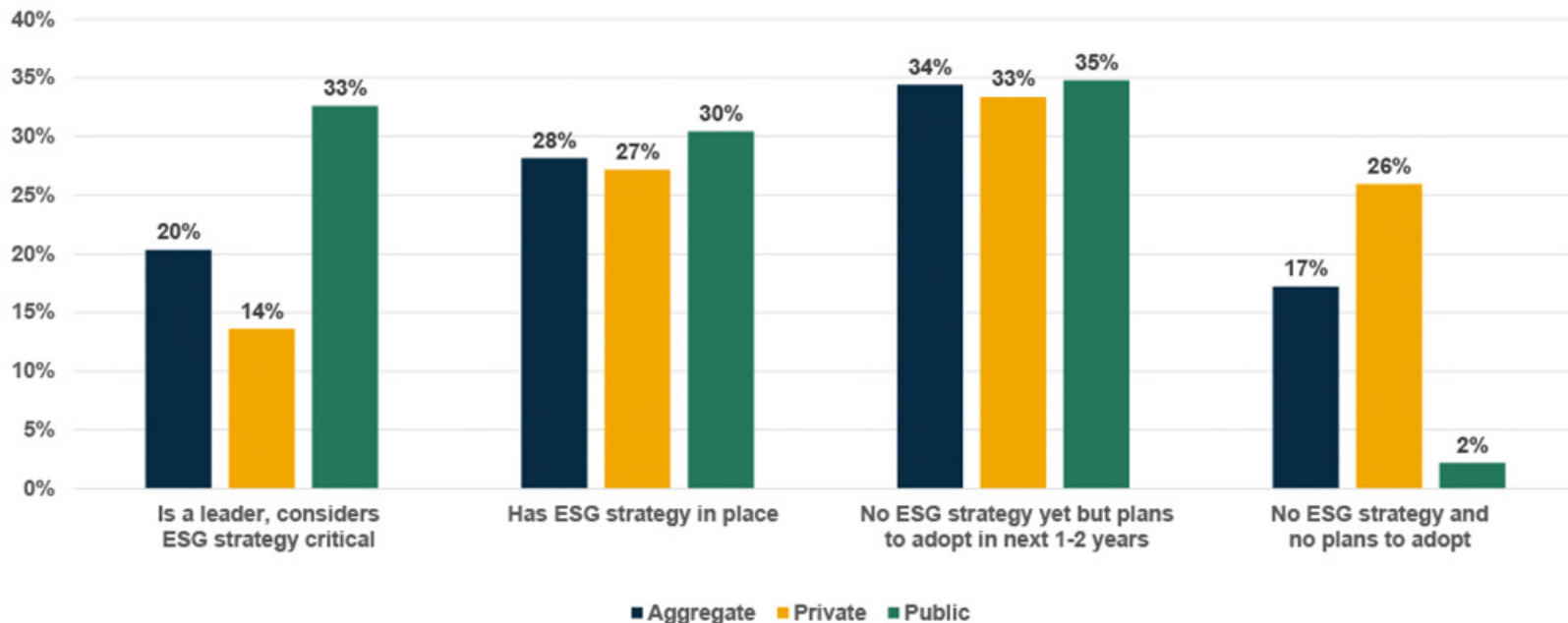
*The board made no recommendation on the proposal.

Source: SEC filings

¹ 2022 Proxy Season Preview, Shirley Westcott, Alliance Advisors' April 2022 Newsletter, <https://www.allianceadvisors.com/newsletters/2022-proxy-season-preview>

Thompson Hine ESG Survey: Status of ESG Strategy – Public vs. Private

48% of respondents have an ESG strategy in place, with 33% of public and 14% of private companies characterizing ESG as critical to their business objectives

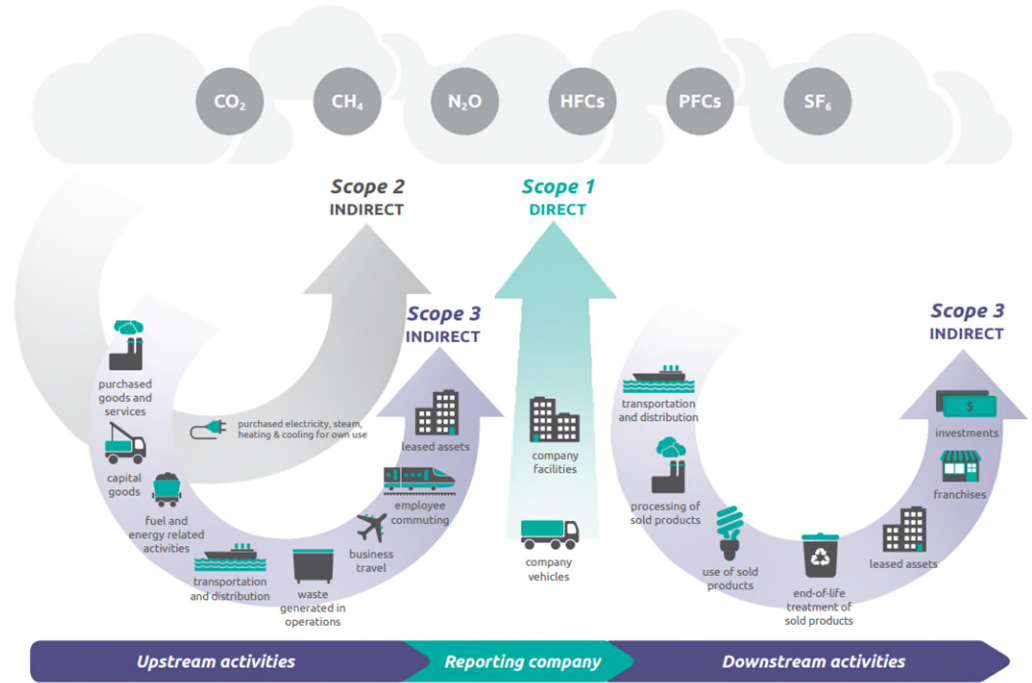


SEC's Climate Disclosure Proposal

- *Broad, complex and detailed rule-making proposal* (500 plus pages) – the first time that companies in the U.S. will be mandated to make substantive climate disclosures in their SEC filings
- Based in part on the Task Force on Climate-Related Financial Disclosures (*TCFD*) and Greenhouse Gas (*GHG*) protocol frameworks
- *Extensive Narrative Disclosures; Climate Financial Metrics*
- *Disclosure of Scope 1* (direct) *and Scope 2* (indirect/purchased energy) greenhouse gas (GHG) emissions
- Disclosure of *Scope 3* (indirect from upstream or downstream activities), if material to the company or if included in the company's targets (smaller companies exempt from Scope 3 (non-affiliate public float <\$250M, or < \$100M in revenues and no public float or < than \$700M))

Reporting Emissions

GHG Protocol Scopes & Emissions Across the Value Chain



Source: https://ghgprotocol.org/sites/default/files/standards/Corporate-Value-Chain-Accounting-Reporting-Standard_041613_2.pdf

SEC's Climate Disclosure Proposal

- *Climate-related financial risks* (physical and transition) over the short, medium and long term, including impact on the company's value chain
- *Strategic planning* around climate-related risks (incl. scenario analysis)
- *Net Zero and other targets* (water, waste, biodiversity, etc.) – detail, extent to which carbon credits utilized, progress towards targets, interim targets, time horizon, etc.
- *ESG governance disclosures* (board and management), frequency of reporting to the board/committees, *and director qualifications* (including how expertise in climate-related risks was obtained)
- *Financial Statement Impacts of climate-related events and transition activities* (disaggregated if 1% impact on a line item, absolute values), plus expenditures, financial estimates and assumptions impacted by such activities; all subject to audit

SEC's Climate Disclosure Proposal

- Third-Party Assurance for at least Scope 1 and Scope 2 for larger companies
- Disclosures to be included in Annual Reports (Form 10-K), with material changes in Quarterly Reports (Form 10-Q), as well as in registration statements
- XBRL tagging
- Timing Pressures; Resources; Costs
- Comment Period; Challenges Expected
- "SEC Releases Long-Awaited Proposed Climate Disclosure Rules," Thompson Hine ESG Collaborative Update, March 22, 2022.

Phase-In Disclosure Compliance Dates

The table assumes that the proposed rules will be adopted with an effective date in December 2022 and that the filer has a December 31st fiscal year end.

Companies with a different fiscal year-end date that results in their fiscal year 2023 commencing before the effective date of the rules would not be required to comply with the proposed rules until the following fiscal year. (For example, a large accelerated filer with a March 31 fiscal year-end would not be required to comply with the proposed climate disclosure rules until its Form 10-K for fiscal year 2024, filed in June 2024.)

Filer Type	Disclosure Compliance Date		Financial Statement Metrics Audit Compliance Date
	All proposed disclosures, including GHG emissions metrics: Scope 1, Scope 2 , and associated intensity metric, but excluding Scope 3	GHG emissions metrics: Scope 3 and associated intensity metric	
Large Accelerated Filer	Fiscal year 2023 (filed in 2024)	Fiscal year 2024 (filed in 2025)	Same as the disclosure compliance date
Accelerated Filer Non-Accelerated Filer	Fiscal year 2024 (filed in 2025)	Fiscal year 2025 (filed in 2026)	
SRC	Fiscal year 2025 (filed in 2026)	Exempted	

Phase-In for Third-Party Assurance Reports

The third-party attestation report would be subject to the following phase-in periods

Non-accelerated filers (smaller companies) are not required to obtain it

Filer Type	Scopes 1 and 2 GHG Disclosure Compliance Date	Limited Assurance	Reasonable Assurance
Large Accelerated Filer	Fiscal year 2023 (filed in 2024)	Fiscal year 2024 (filed in 2025)	Fiscal year 2026 (filed in 2027)
Accelerated Filer	Fiscal year 2024 (filed in 2025)	Fiscal year 2025 (filed in 2026)	Fiscal year 2027 (filed in 2028)

SEC Enforcement Underway

- March 2021 establishment of Climate and ESG Task Force in Enforcement to scrutinize disclosure claims
 - ▶ Designed to “proactively identify ESG-related misconduct”
 - ▶ Is SEC coming to a position that ESG issues are generally “material” and that statements about them are relied upon by reasonable investors?
- No reported Section 10(b) actions (yet) based solely on climate disclosures
- Already gets in on the action on ESG-like issues that have made headlines:
 - ▶ Fiat Chrysler Automobiles N.V.
 - Cease-and-Desist Order and \$9.5M civil penalty imposed (September 2020)
 - Arose from disclosures about internal investigation of, and compliance with, applicable emissions regulations for its diesel vehicles following VW “Dieselgate scandal”
 - Certain “Leaks”; Regulation FD; Review Prior Disclosures (FLS; “full” disclosure; corrective disclosure)

SEC Enforcement Underway

ESG Implications for asset managers and investment advisors

- Deutsche Bank AG asset management arm, DWS Group, under investigation by DOJ, SEC
 - ▶ Former head of sustainability said it overstated its sustainable investing efforts, painting rosier picture to investors
 - ▶ DWS has @ \$1 trillion in assets under management
 - ▶ At issue is whether it overstated how much it used sustainable investing criteria to manage assets
 - ▶ Followed WSJ report that statements on its sustainable investing efforts were inaccurate
 - ▶ Similar reviews and investigations expected of other investment managers (per Commissioner statements)
- April 2021 Division of Examinations ESG Risk Alert regarding advisers, RICs and private funds.
 - ▶ Highlighted observations from recent exams, provided examples of problematic conduct, and best practices.

Is the FTC Gearing Up?

- New “Green Guide” Expected Later in 2022
 - ▶ Last update in 2012
 - ▶ Will “set forth the [FTC’s] current views about environmental claims. The guides help marketers avoid making environmental marketing claims that are unfair or deceptive”
 - ▶ “[I]t is deceptive to misrepresent, directly or by implication, that a product, package, or service offers a general environmental benefit.”

ESG Litigation: Main Buckets of Current Litigation



**Corporate
Action/Inaction**



**GHG Emissions
Regulation**



**Contract
Disputes**

Current ESG Litigation: Corporate Action/Inaction



ESG Litigation: What to Watch



Investor Litigation or Other Actions

(Exxon)

Govt. Claims for ESG Exaggerations

*Commonwealth of
Mass. v. Exxon*

Royal Dutch Shell PLC

(May 26, 2021)

Dutch court ordered Shell to
cut global GHG emissions by
45%

Growing Areas for Disputes

Breach of contract actions (PP, cap and
trade, purchase of renewables, etc.)

False environmental claims

Board Diversity Suits:

UNIFORMLY UNSUCCESSFUL (SO FAR)

- **FACEBOOK:** *Ocegueda v. Zuckerberg*, 526 F. Supp. 3d 637 (N.D. Cal. Mar. 19, 2021).
- **THE GAP:** *Lee v. Fisher*, 2021 WL 1659842 (N.D. Cal. Apr. 27, 2021).
- **ORACLE:** *Klein v. Ellison*, 2021 WL 2075591 (N.D. Cal. May 21, 2021).
- **DANAHER:** *In re Danaher Corp. S'holder Deriv. Litig.*, 2021 WL 2652367 (D.D.C. June 28, 2021).
- **NORTONLIFELOCK:** *EllieMaria Toronto ESA v. NortonLifeLock Inc.*, 2021 WL 3861434 (N.D. Cal. Aug. 30, 2021).
- **OPKO:** *Lee v. Frost*, 2021 WL 3912651 (S.D. Fla. Sept. 1, 2021).
- **QUALCOMM:** *Kiger v. Mollenkopf*, 2021 WL 5299581 (D. Del. Nov. 15, 2021).

Generic Statements: Lessons from *Goldman Sachs*

- ***Not an ESG case***—involves generic statements about Goldman’s business practices and conflict-of-interest policies.
- But has big implications for ESG litigation, which often involves generic statements.
- On remand, SDNY held that presumption not rebutted and certified the class (12/8/2021).
 - ▶ While generic statements may have less price impact, defendants failed to show that statements had no price impact.
 - ▶ Just b/c everyone is making them, doesn’t mean they’re not material. “This Court is hard-pressed to understand why statements such as those at issue here would have achieved such ubiquity in the first place were they incapable of influencing (including by maintaining) a company’s stock price.”
 - ▶ Reiterates that subsequent events may shed new light on “generic” statements.

What to Do Next?

- If no ESG Program, start one
- If ESG team doesn't include finance, add
- Conduct priority assessment of ESG issues; risks & opportunities; ERM
- Measure GHG emissions
 - ▶ Create inventory of GHG emissions in accordance with the GHG Protocol (disaggregate by gas)
 - ▶ Software; technology; other tools
 - ▶ Will need to assess Scope 3 too, at the minimum to determine if it is material to the company
- Take care when setting GHG Reduction Targets

What to Do Next?

- ESG report can be a good start, but not sufficient for SEC reporting
 - ▶ Evaluate what data is available and what will need to be collected and assessed (“gap” analysis)
 - ▶ Evaluate internal and external resources; understand timing pressures
- Data Verification and Disclosure Controls (COSO, sub-certifications, disclosure committee, etc.)
- Board Education, Reporting & Director Qualifications (climate, cyber, etc.)
- Interaction with Other Laws (e.g., Texas laws, banks, etc.); Potential Litigation (e.g., *Caremark*, net zero definitions, greenwashing, etc.)



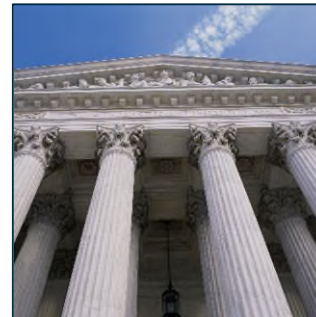
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