Cravath Quarterly Review
M&A, Activism and Corporate Governance

Volume 1 | Issue 4

Q4 2019

PAGES 1-8 Mergers & Acquisitions

PAGES 9-11 Activism

PAGES 12-16 Corporate Governance

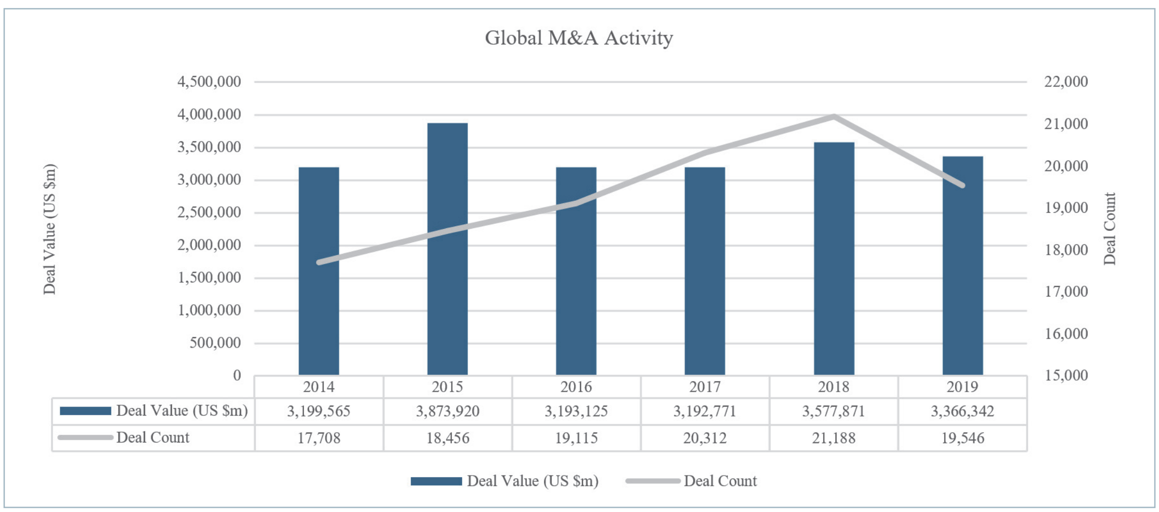
Mergers & Acquisitions

TRENDS[1]

After a slow third quarter, a relatively strong Q4 rounded out a robust year for global M&A activity by deal value in 2019, despite declines in overall deal count relative to 2017 and 2018. For the year, 2019 featured $3.37 trillion worth of deals across 19,546 transactions, a 6% decline in deal value relative to heightened levels in 2018, but still the third highest level of M&A activity in terms of deal value since 2009, and the sixth successive year that global deal values exceeded $3 trillion. However, the number of transactions continued to decline relative to recent historical periods. The 19,546 transactions in 2019 was in line with the average number of transactions from 2014-2018 (19,356), but the number of deals in 2019 was 8% and 4% lower than the number of transactions in 2018 and 2017, respectively. This translated to an M&A market that continues to be driven by larger deals, with 2019 featuring 38 megadeals (greater than $10 billion).

However, despite the strong numbers, M&A activity in 2019 was in many ways a story of two halves. Due in part to the strength of the U.S. market, the global M&A market in H1 2019 was resilient to geopolitical forces that seemed to slow M&A activity in other regions. And while the number of deals in H2 2019 (9,658) remained roughly in line with the number of deals in the first half of the year (9,888), the second half of 2019 saw a 23% decline in global deal value relative to the first half of the year, as the U.S. market began feeling the effects of these global headwinds.

On a regional basis, with 47% of global deal value, the United States continued to capture an outsized share of the global M&A market, posting its second best year in terms of deal value since 2009. In contrast, Europe and Asia Pacific (excl. Japan) experienced significant M&A declines in 2019, with total deal values declining 21% and 22%, respectively, compared to 2018. Deal activity was better in other regions, with the Middle East and Africa (MEA), Latin America and Japan each having strong years in 2019 in terms of deal value, with deal values up 102%, 12% and 60%, respectively, relative to 2018.



	2014	2015	2016	2017	2018	2019
Deal Value (US $m)	3,199,565	3,873,920	3,193,125	3,192,771	3,577,871	3,366,342
Deal Count	17,708	18,456	19,115	20,312	21,188	19,546

Source: Mergermarket

[1] All data regarding M&A activity from Mergermarket unless otherwise indicated. Deal values and volume may vary across our newsletters due to continuous updates to the M&A activity sources.

Despite YoY Declines, 2019 Proves an Otherwise Strong Year for Global M&A; Megadeals Drive Overall M&A Market as the Number of Transactions Declines

As previously mentioned, the second half of 2019 failed to sustain the heightened levels of deal activity seen in the first half of the year. The $1.46 trillion worth of deals globally in the second half of 2019 represented a decline relative to recent historical periods, with deal values in the second half of the year 5% below reduced levels of M&A activity in the second half of 2018, and 17% below average deal values in the second half of the year from 2014-2018.

Taken together, despite the somewhat slow second half and despite being down 6% in terms of global deal value relative to a banner year in 2018, 2019 was another strong year for global M&A in terms of deal value. The $3.37 trillion worth of deals across 19,546 transactions in 2019 was the third highest in terms of deal value since 2009, and 22% greater than average total deal values annually from 2009-2018. But despite the strong year in terms of global deal value, 2019 was characterized by fewer transactions—the 19,546 transactions in 2019 was 8% and 4% lower than the number of transactions in 2018 and 2017, respectively, although in line with the average number of transactions from 2014-2018 (19,356). This overall lower deal count should be viewed in the context of 2019 being a year with larger deals. There were 38 megadeals (greater than $10 billion) in 2019, the highest number of megadeals since 2015 (which was the strongest year for M&A in terms of total deal value in the last decade).

Cross-Border Deals See Continued Declines, Contributing to M&A Declines in Non-U.S. Regions

Cross-border M&A was down in 2019 due to a number of factors, in particular the effect of uncertain political and geopolitical conditions and more uncertain regulatory scrutiny of transactions. For the year, there were ~$1.27 trillion worth of cross-border deals, a ~6.2% reduction relative to 2018. In this context, the impact was particularly pronounced in regions subject to slower economic growth, protectionist trade policies and heightened geopolitical tensions—relative to 2018, European inbound M&A was down ~30.3% in terms of deal value and Asia Pacific (excl. Japan) inbound M&A was down ~14.8% in terms of deal value, with China experiencing particularly low levels of both inbound and outbound M&A in 2019. Not surprisingly, this contributed to decreased deal activity in major non-U.S. regions. In 2019, the dollar value of dealmaking in the two largest non-U.S. regions for M&A activity, Europe ($780 billion) and Asia Pacific (excl. Japan) ($572 billion), was down 21% and 22%, respectively, relative to 2018. For Europe in particular, the fewest number of megadeals (greater than $10 billion) since 2009 contributed to the continent accounting for only ~23% of global deal value, reaching the lowest levels seen in the last decade. And for Asia Pacific (excl. Japan), global market share in terms of deal value sunk to 17% in 2019 relative to 20% in 2018, despite posting its strongest quarter of the year in terms of deal value ($172 billion) and number of transactions (1,090).

In contrast, the Middle East and Africa had a record year in terms of M&A activity, posting $141.3 billion worth of deals across 463 transactions, a 102% increase in terms of deal value relative to 2018. Of course, these numbers were significantly skewed by Saudi Aramco's $70.4 billion acquisition of 70% of Sabic, which accounted for roughly half of total deal value in the region. But even excluding this transaction, M&A activity in the region was still strong relative to historical levels, which have featured $57.9 billion worth of deals across 430 transactions on average from 2009-2018. Latin America also had a strong year, with $88 billion worth of deals across 674 transactions, a 12% increase in terms of deal value relative to 2018. And although deal values were down relative to historical levels in the region, which on average have featured $105.6 billion worth of deals annually from 2009-2018, Latin America bucked the trend of fewer overall transactions with a ~9% increase in the number of deals relative to the annual average of 620 from 2009-2018. Finally, Japan was another bright spot for the year in terms of M&A activity—the $75.7 billion worth of deals across 465 transactions was 60% greater than total deal values in 2018, ~27% greater than average annual deal values from 2009-2018, and the country's third strongest year since 2009 in terms of deal value.

Strong Year for Private Equity Acquisitions; Europe, Middle East and Africa (EMEA) and the United States Lead Regional Private Equity Activity for 2019

Due in part to a fourth quarter that featured $147 billion worth of private equity acquisitions across 797 transactions, 2019 proved to be a strong year for private equity activity. The

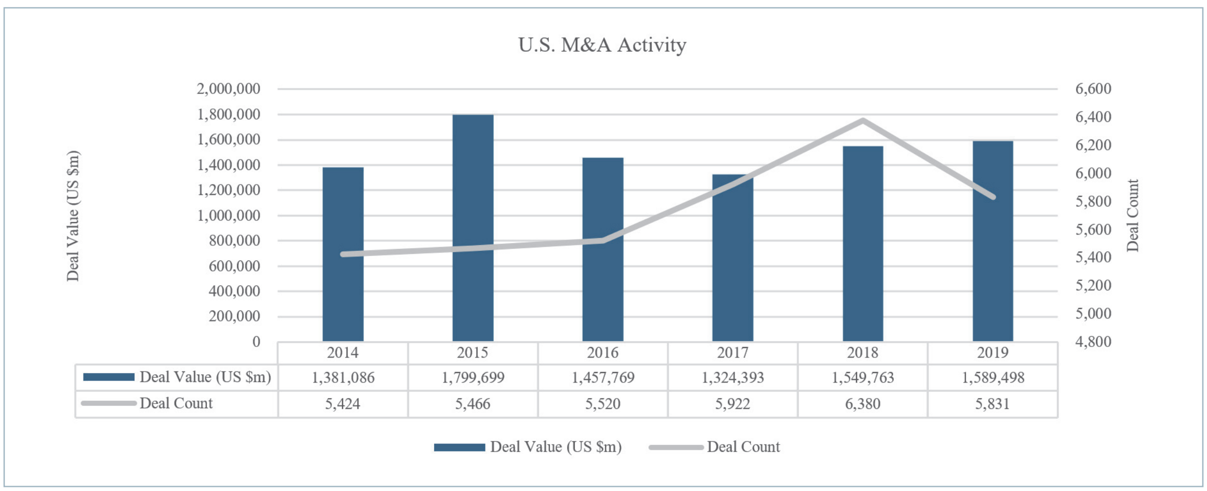
$580 billion worth of private equity acquisitions across 3,545 transactions in 2019 was the highest in terms of deal value since 2009. These figures, which reflect a 60% and 33% increase relative to average private equity deal values and deal counts from 2009-2018, respectively, also reflect a continuing trend since 2016 of private equity acquisitions comprising a greater share of global deal value. In 2019, private equity acquisitions comprised 17% of global M&A deal value, relative to 13% on average from 2009-2018, and the number of deals that involved a private equity sponsor (either on the buy-side or the sell-side) rose to ~27.5% of all global transactions, the third consecutive year this figure was above 25%. Notably, after years of strong private-equity activity that has reduced the number of high-quality private targets, private-equity firms have deployed significant amounts of capital in take-private deals, with the ~$158.3 billion worth of take-private transactions the highest in terms of deal value since 2007.

On a regional basis, Europe and the EMEA led the way in terms of private equity deal count, accounting for ~43% of all private equity acquisitions in 2019, but the United States was the largest market in terms of deal value, with ~$240 billion worth of private equity acquisitions for the year.

Despite a Second Half Affected by the Slowdown in Global M&A, the U.S. M&A Market in 2019 Continued to Claim an Outsized Share of Global Deal Volume

In the United States, despite a slower second half, the strong first half to the year fueled an M&A market that saw $1.6 trillion worth of deals across 5,831 transactions, the second most active year for U.S. M&A in terms of deal value since 2009 and 37% greater than the 2009-2018 average of $1.16 trillion worth of deals from 2009-2019. As a result, the U.S. market continued to be the dominant region for M&A, accounting for ~47% of global deal value in 2019, its highest share since 2001.

M&A activity in the United States was driven by 29 megadeals (greater than $10 billion), as well as by increased inbound investment. Unlike other regions that have been less resilient to headwinds to M&A activity, the United States proved to be a particularly attractive market for international acquirers, with inbound M&A in the United States up ~13% relative to 2018.



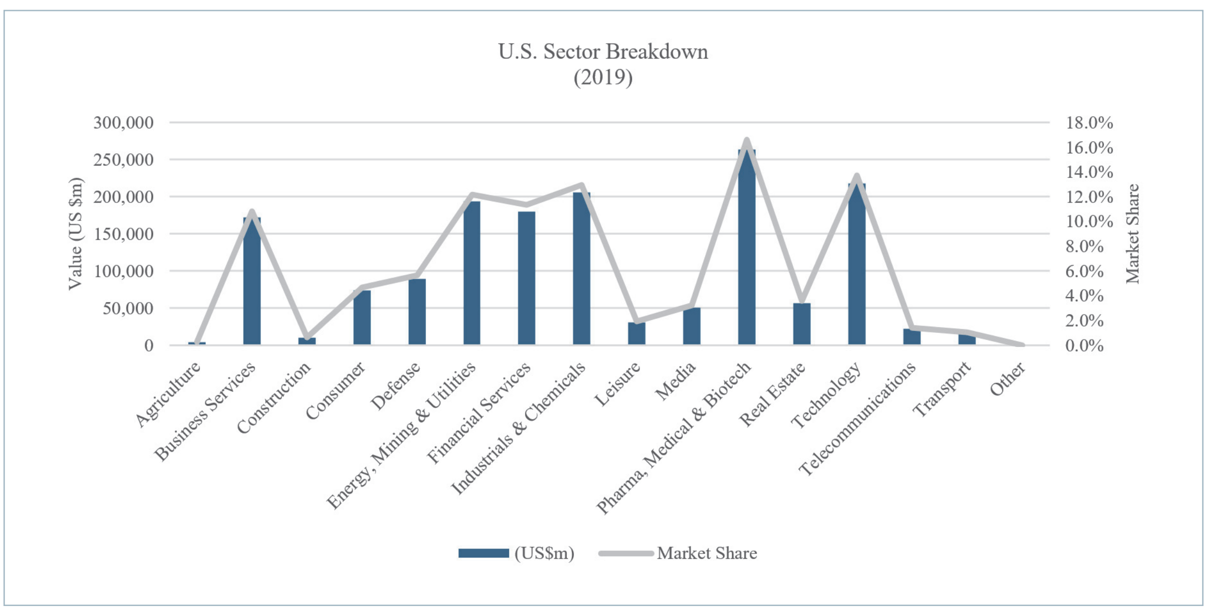
	2014	2015	2016	2017	2018	2019
Deal Value (US $m)	1,381,086	1,799,699	1,457,769	1,324,393	1,549,763	1,589,498
Deal Count	5,424	5,466	5,520	5,922	6,380	5,831

Source: Mergermarket

Major Activity in Certain Sectors

In terms of global deal value, Industrials & Chemicals led the way in 2019, posting ~$532.5 billion worth of deals and accounting for ~15.8% of global deal value, of which Saudi Aramco's $70.4 billion acquisition of 70% of Sabic was the largest deal in the sector. Pharma, Medical & Biotech was a close second with ~$479.9 billion worth of deals, accounting for ~14.3% of global deal value and including two of the five largest deals of the year—Bristol-Myers Squibb's $87.8 billion acquisition of Celgene Corporation and AbbVie's $86.3 billion acquisition of Allergan—as well as other transformative deals such as Mylan's $50 billion combination with Upjohn, a division of Pfizer. Energy, Mining & Utilities was the third most active sector in 2019, featuring ~$447.9 billion worth of transactions (~13.3% of deal value), of which Occidental Petroleum's $55 billion acquisition of Anadarko Petroleum in Q2 2019 was the largest deal in the sector, and featuring a notable take private transaction with the acquisition of Buckeye Partners by IFM Investors for $10.3 billion. Technology and Financial Services were the two other most active sectors in terms of deal value in 2019, featuring ~$394.9 billion (11.7% of deal value) and ~$345.2 billion worth of deals (10.3% of deal value), respectively.

Source: Mergermarket



Source: Mergermarket

LEGAL DEVELOPMENTS

Cases

Q4 2019 featured a number of notable cases in the M&A space.

Summary Order, *Stone Key Partners, LLC, Stone Key Securities LLC v. Monster Worldwide, Inc.*, No. 18-2804-cv (2d Cir. October 11, 2019)

In this summary order, the Second Circuit offered a key reminder of the importance of carefully defining the types of qualifying transactions that will entitle financial advisors to fees pursuant to engagement letters. The case also highlights the importance of clearly defining the manner in which an engagement can be terminated, especially when the financial advisor is entitled to fees for transactions that occur within a certain period of time after the engagement concludes (*i.e.*, "tail fees").

In April 2012, Stone Key entered into an agreement (the "Engagement Letter") to provide Monster with financial advisory services in connection with a strategic review. The Engagement Letter specified that Stone Key was entitled to receive compensation in the event of certain qualifying transactions, which included a "Sale Transaction" or a "Partial Sale Transaction," that occurred within a year of the Engagement Letter's termination. Shortly after work on the strategic review concluded, Monster sold 49.99% of its interest in one of its subsidiaries to a private equity buyer, which Stone Key later claimed was a Partial Sale Transaction that entitled it to fees under the Engagement Letter. Monster later also engaged in two additional transactions (the "JobKorea II" and "Randstad" transactions) that Stone Key claimed fell within the one-year tail period that would entitle it to tail fees.

The Second Circuit affirmed the lower court's finding that Monster's sale of 49.99% of its interest in one of its subsidiaries did not satisfy the definition of a Partial Sale Transaction under the Engagement Letter because it did not constitute, "the sale of a material portion of the assets or operations of [Monster] and its subsidiaries taken as a whole." The lower court relied on the following facts to conclude the partial sale of Monster's subsidiary did not satisfy the materiality threshold: "(1) following the consummation of [the subsidiary transaction], Monster retained majority control over the subsidiary and thus did not relinquish a material portion of its operations; and (2) Monster's 49.99% stake in [the subsidiary] constituted less than 4% of Monster's total assets at the time of the transaction." In affirming the holding of the lower court, the Second Circuit dismissed arguments by Stone Key that a broader definition of "operations" that accounts for other qualitative factors (such as profitability and market response) or other metrics to quantify the value of Monster's assets should apply.

The Second Circuit also affirmed the lower court's finding that the JobKorea II and Randstad transactions occurred beyond the Engagement Letter's one-year tail period. The lower court concluded based on extrinsic evidence that Stone Key's engagement concluded on August 1, 2013, "following the parties' failure to secure a potential acquiror for Monster as contemplated by the Engagement Letter and in light of their mutual understanding that the strategic review had, for that reason, reached its conclusion." As a threshold matter, Stone Key argued that the Engagement Letter unambiguously required written notice of termination and that, in the absence of either party having terminated the engagement in writing, the district erred in looking to extrinsic evidence to determine when Stone Key's engagement ended. The Second Circuit concluded that the Engagement Letter's termination provision was ambiguous because it did not identify an exclusive means for the engagement's conclusion, noting that the agreement did not state it "must" be terminated in writing, did not unambiguously establish that the agreement would be ongoing absent written termination, and included other provisions that suggested additional ways the agreement might conclude. As a result, the Second Circuit affirmed that the lower court was entitled to look to extrinsic evidence and concluded that its finding that the engagement concluded on August 1, 2013 was not clearly erroneous. This, in turn, meant the JobKorea II and Randstad transactions occurred outside the one-year tail period, which meant Stone Key was not entitled to fees.

The case also addressed the manner in which out-of-pocket expenses were calculated under the Engagement Letter, concluding that Stone Key was not entitled to reimbursement for expenses incurred before the agreement was executed because reimbursement was limited to expenses incurred, "in connection with Stone Key's rendering its services under this [Engagement Letter]."

***High River Limited Partnership et al. v. Occidental Petroleum Corp.*, C.A. 2019-0403-JRS (Del. Ch. Nov. 14, 2019)**

In this case, the Delaware Court of Chancery rejected a novel application of Section 220 of the Delaware Corporation Law put forth by Carl Icahn to aid him in his threatened proxy contest with Occidental Petroleum Corporation ("Occidental").

The case arose out of Occidental's $55 billion acquisition of Anadarko Petroleum Corporation

("Anadarko") and the related financing and asset sales that were completed by Occidental in connection with the transaction. Affiliates of Carl Icahn holding a substantial stake in Occidental opposed the transaction and sought to elect directors to Occidental's board and achieve certain corporate governance changes. Icahn filed a books and records demand under Section 220 seeking to inspect certain documents related to the Anadarko merger and the board's consideration of a recent stockholder proposal relating to the threshold for calling a special meeting of stockholders. The request was based on two arguments: (1) a "cursory argument", in the words of the court, that the purpose was to investigate corporate wrongdoing or mismanagement, and alternatively, (2) a novel application of Section 220 that would allow stockholders to inspect documents related to non-actionable board-level decisions that the stockholder disagrees with, "when the stockholder states and then demonstrates that his purpose is to communicate with other stockholders in furtherance of a potential, *bona fide* proxy contest."

Under Delaware law, in order to inspect books and records under Section 220 a plaintiff must have "a proper purpose." And when "a stockholder seeks to inspect books and records to investigate corporate wrongdoing," the stockholder must, "demonstrate a credible basis to suspect mismanagement or wrongdoing has occurred before the corporation will be compelled to allow inspection." The court dismissed Icahn's argument of wrongdoing, which the court noted requires "plaintiff provide *some* evidence of wrongdoing," and not just, "[m]ere disagreement with a business decision."

In rejecting Icahn's proposed proxy contest rule for Section 220 books and records demands, the Delaware Court of Chancery distinguished this case from two prior cases cited by plaintiffs in favor of their argument. Specifically, the court distinguished the request in this case from the type of "very narrow demand for purely logistical information" that can constitute a "proper purpose" under Delaware law. In this context, the court noted the difference between the Icahn request (which sought new information) from a request, "seeking information about *how to reach stockholders* to share information" that a stockholder already has in their possession as explanation for why the latter constituted a proper purpose. The court also emphasized the limiting principle that stockholders are entitled to inspect only those documents under Section 220 that are, "'necessary, essential and sufficient' to their stated purpose," concluding that Icahn's request was not necessary for the plaintiffs to advance their claims of dissatisfaction with Occidental's decision to pursue the Anadarko merger and related transactions.

Channel Medsystems, Inc. v. Boston Scientific Corporation and NXT Merger Corp., C.A. 2018-0673-AGB (Del. Ch. Dec. 18, 2019)

In this case, the Delaware Court of Chancery applied long-standing Delaware law to determine whether a target experienced (or was reasonably likely to experience) a Material Adverse Effect ("MAE"). In so doing, the court confirmed that such claims are highly fact-specific and impose a very high and hard-to-meet burden on any party seeking to terminate or avoid its obligations to close under the terms of a merger agreement on the basis of an MAE.

The case arose after Boston Scientific Corporation ("Boston Scientific") entered into a merger agreement with Channel Medsystems, Inc. ("Channel") in November 2017. At the time, Boston Scientific held a 15% stake in Channel, and pursuant to the terms of the merger agreement, among other things, (i) Boston Scientific would increase its equity stake in Channel to 20%, (ii) Boston Scientific would have the right to acquire the remaining equity interests in Channel at any time and (iii) Channel would have the right to "put" the remaining equity interests in Channel to Boston Scientific if it received FDA approval for its only product ("Cerene"), an in-development medical device, by September 30, 2019. The merger agreement also permitted Boston Scientific to designate a director to serve on Channel's board.

Shortly after the parties executed the merger agreement, Channel discovered serious misconduct by an employee that included falsifying expense reports and other documents, including submission of falsified documents to the FDA and other regulators in relation to Channel's clinical study of Cerene. Channel conducted an internal investigation that concluded that the misconduct ultimately did not affect the outcome of the Cerene clinical trial or impact the safety and efficacy of the clinical data, and the findings of the internal investigation, along with a series of other reports and remediation plans, were submitted to the FDA. The FDA accepted Channel's remediation plan and acknowledged that Channel had addressed all of the FDA's concerns.

In addition to the company's communications with the FDA, Channel was also transparent with Boston Scientific regarding the employee misconduct and its remediation efforts, which Boston Scientific for the most part did not respond to. Nonetheless, after the FDA accepted Channel's remediation plan, Boston Scientific began expressing concerns about the findings of Channel's internal investigation and indicated that they were not confident the FDA ultimately would approve Channel's FDA application. Boston Scientific ultimately sent a notice of termination of the merger agreement claiming (among other things), breaches of representations and warranties in the merger agreement that constituted an MAE. The FDA granted its approval for Cerene in March 2019, within the time frame originally contemplated in the merger agreement and six months prior to the September 30, 2019 deadline.

In a lengthy opinion that focused on Boston Scientific's claim that the employee misconduct at Channel breached various representations and warranties in the merger agreement and whether such breaches constituted an MAE, the Court of Chancery found that Boston Scientific failed to prove an MAE. The court in its opinion noted the "heavy burden" to proving an MAE, turning to a qualitative and quantitative analysis of whether there had been a material adverse effect. Both Boston Scientific's qualitative and quantitative arguments were primarily based on claims by Boston Scientific that they would need to remediate and retest Cerene before putting it on the market. The court viewed these claims with skepticism due to the fact it marked a "shift in strategy" by Boston Scientific now that it could no longer claim Cerene's FDA approval prospects were jeopardized, and ultimately rejected these claims as not credible due to, among other things, the fact that Boston Scientific had not even evaluated the remediation work Channel had done.

Among other things, the Court of Chancery also found that Boston Scientific breached its duty to use commercially reasonable efforts to consummate the transaction and that Boston Scientific demonstrated a lack of good faith based on its failure to take steps to cooperate with Channel or investigate the conclusions of Channel's outside experts. Thus, Channel was entitled to specific performance and Boston Scientific was required to close the deal.

Overall, the case applies long-standing Delaware jurisprudence to the assessment of whether an MAE occurred. The case also provides a useful reminder of the importance of contemporaneous analysis and documentation for buyers who seek to invoke an MAE to justify termination. While the facts of this case seemed to the court to present a case for buyer's remorse, one significant reason the court was skeptical of Boston Scientific's claims was because there was no contemporaneous analysis or evaluation of why Boston Scientific believed an MAE occurred or was likely to occur.

Robert Garfield v. BlackRock Mortgage et al., C.A. 2018-0917-KSJM (Del. Ch. Dec. 20, 2019)

In this case, the Delaware Court of Chancery denied a motion to dismiss claims that challenged the fairness of a transaction that restructured PennyMac, Inc. ("PennyMac") from an "Up-C" structure to a simple corporate form. The court rejected defendants' arguments that they should obtain the benefit of the business judgment rule under *Corwin* because the transaction was approved by a majority of disinterested shareholders, and also rejected defendant's alternative argument that the claims should be dismissed because it was fair under entire fairness review. Instead, the court found that *Corwin* was inapplicable because the complaint supported a pleading-stage inference that BlackRock and HC Partners constituted a controller group that benefited from the transaction, and that the plaintiff had adequately pled a claim under the entire fairness standard.

The case arose following a capital structure reorganization (the "Reorganization") designed to allow the defendants who held units in PennyMac's operating subsidiary (the "Unitholders") to receive certain tax benefits. Under the Up-C structure prior to the Reorganization, public shareholders held Class A common stock in PennyMac constituting 15% of the voting rights and 100% of the economic interests, while the Unitholders, including BlackRock, HC Partners and PennyMac management, held Class B shares with no economic interest but the remaining 85% of the PennyMac voting rights. The Up-C structure was originally designed in part to allow the Unitholders to more easily achieve certain tax benefits, but those benefits never materialized due to changes in federal tax laws and the operating subsidiary's business. In response, the PennyMac CEO introduced the idea of a capital structure reorganization to the board. The Reorganization was designed to allow the Unitholders to exchange their units for PennyMac Class A common stock in a tax-free exchange that would allow them to receive long-term capital gains treatment on the future sale of their newly acquired Class A common stock if they held those shares for longer than a year. The PennyMac board established a special committee that was authorized to recommend (but not approve) the Reorganization to the entire board, which the special committee did and the board subsequently approved. The Reorganization was approved by the PennyMac stockholders on October 24, 2018, and closed on November 1, 2018.

After the closing, a Class A shareholder brought direct and derivate claims alleging fiduciary duty violations by BlackRock, HC Partners and certain PennyMac directors—all of whom owned significantly more units in PennyMac's operating subsidiary than Class A shares—that challenged the fairness of the Reorganization because it created benefits for the Unitholders and not the holders of Class A shares. In support of its motion to dismiss, defendants argued that, "the business judgment standard of review applies under *Corwin* because a fully informed, uncoerced majority vote of disinterested stockholders approved the Reorganization," and alternatively, that the plaintiff, "ha[d] not alleged facts to suggest the Reorganization was not entirely fair."

The Delaware Court of Chancery rejected both arguments for a motion to dismiss. Under Delaware law, "[a] stockholder vote cannot restore the business judgment rule under *Corwin* when there is 'a controlling stockholder that extract[s] personal benefits' from the transaction."[2] And since the *MFW* procedures—which provide that a conflicted controller transaction can receive business judgment if, at the outset, the transaction is conditioned on the approval of both an independent special committee and a majority of the minority stockholders—were not invoked, the court undertook an analysis to determine whether the plaintiff had adequately pled the existence of a conflicted controller or controller group.

Since BlackRock and HC Partners controlled approximately 46.1% of PennyMac's voting stock and each had a unilateral right to block the Reorganization under the terms of an LLC Agreement with PennyMac's operating subsidiary, the court concluded that there was a reasonable inference that BlackRock and HC Partners at least could exercise transaction-specific control over the Reorganization if they worked together. This in turn required an analysis of whether these two shareholders constituted a group, which the court also found reasonably conceivable. Applying the "legally significant connection" test, the court found that:

> BlackRock and HC Partners' voting power, concurrence of interests, historical ties, and transaction-specific coordination give rise to a reasonably conceivable inference that the alleged group had more than a "mere concurrence of self-interest" and an "actual agreement" to work together in connection with the Reorganization.[3]

Among the factors the court looked to in reaching this conclusion were BlackRock's and HC Partners' 10-year co-investment history in which they were the founding sponsors of the PennyMac operating subsidiary, public disclosures that described them as "strategic partners", as well as the fact that PennyMac management presented the Reorganization plan to them as a "collective unit."

In addition, the court also found that the plaintiff alleged facts to support a pleading-stage inference that the transaction was not entirely fair. Noting the two basic aspects of fairness—fair dealing and fair price—the court emphasized its previous findings of a reasonable inference that BlackRock and HC Partners exercised control over the Reorganization and also emphasized the fact that the special committee was only given authority to recommend, but not give final approval for, the Reorganization. From the perspective of the court, it was also, "reasonably conceivable that the alleged defects in the negotiation process 'infected' the Reorganization's exchange ratio." Thus, taken together, the court found these facts adequately supported a pleading-stage inference of unfair dealing and unfair price.

Notable Moves

On January 15, 2020, Paul Fioravanti, Jr. was confirmed by the Delaware Senate to serve as Vice Chancellor of the Delaware Court of Chancery. Fioravanti, a Democrat, was previously a partner at the Delaware law firm Prickett, Jones & Elliott, P.A., where he focused on corporate and commercial litigation in a variety of business matters, including mergers and acquisitions, fiduciary duty obligations, corporate governance, and limited liability company litigation.[4] Delaware Gov. John Carney nominated Fioravanti in early January to fill the seat vacated by Justice Tamika Montgomery-Reeves, who was sworn in to serve on the Delaware Supreme Court on January 3, 2020.

[2] *Garfield* at *20.
[3] *Id.* at *26-27.
[4] Press Release, Office of the Governor, Governor Carney Announces Nomination of Paul Fioravanti, Jr. to Court of Chancery (January 3, 2020) *available at* https://news.delaware.gov/2020/01/03/governor-carney-announces-nomination-of-paul-fioravanti-jr-to-court-of-chancery/.

Activism[5]

In January 2020, Lazard released its 2019 Review of Shareholder Activism, which offers key observations regarding activist activity levels and shareholder engagement from 2019.

Key findings / insights from the report include:

- The number of companies targeted (187) was down 17% compared to a record 2018 but in line with recent historical levels, while aggregate capital deployed in new activist positions ($42.2 billion) also declined relative to elevated levels in 2017 ($63.8 billion) and 2018 ($66.4 billion);

- 147 investors launched new campaigns in 2019, 43 of whom were first-time activists;

- Activists continued to exert influence outside the United States—Japan for the first time was the most targeted non-U.S. jurisdiction, but overall activity in Europe declined relative to 2018;

- Record number of M&A-related campaigns, accounting for 47% of campaign activity and ~60% of total capital deployed in 2019;

- Activists continued to push for change at the board level, securing 122 board seats in 2019 (consistent with historical averages), and continuing the trend of primarily securing board seats via settlements; and

- Increased outflows from actively managed funds bolster "Big 3" influence.

TRENDS

Full-Year 2019 Was Down Relative to Record Levels of Activism in 2018, But Overall Activism Remains In Line with Historical Levels; Elliott and Starboard Lead the Way in Terms of Activist Activity, with 43 "First Timers" With No History of Activism Launching Campaigns

The year 2019 featured 209 campaigns against 187 companies, down relative to the record pace in 2018, which featured 248 campaigns against 226 companies globally, but generally on par with recent years, which have featured on average 213 campaigns against ~193 companies from 2015-2018.

Elliott and Starboard were the leading activists in terms of campaign activity, launching 14 and 13 campaigns, respectively, and together accounting for ~13% of global campaign activity. Notably, despite the prominence of well-known activists in 2019, the year also featured a record 147 investors launching activist campaigns. Of these, 43 were investors with no history of activism launching campaigns for the first time, a significant increase relative to an average of 29 "first timers" per year from 2015-2018, with the percentage of campaigns launched by "first timers" in 2019 (29%) slightly above the historical average from 2015-2018 (26%).

Finally, 2019 was a year that featured less capital deployed towards new campaigns relative to prior years—the $42.2 billion of capital deployed in 2019 was the second lowest since 2015, significantly below the $63.8 billion and $66.4 billion deployed in 2017 and 2018, respectively, and 23% lower than the average amount of capital deployed towards new campaigns ($54.6 billion) from 2015-2018.

Despite a Record Third Quarter, European Activism On the Whole Was Down in 2019 Relative to 2018; APAC Activism Remained Strong; Japan for the First Time Was the Busiest Non-U.S. Jurisdiction, Setting Local Records for Number of Campaigns and Capital Deployed

In 2019, non-U.S. activism accounted for ~40% of all global campaigns and capital deployed, consistent with prior years. However, Europe, which saw a record Q3 2019 in terms of newly initiated campaigns, ended the year with decreased levels of activism relative to 2018. For the year, 2019 featured 48 campaigns against 44 European companies—a 16% decrease in terms of number of campaigns relative to peak activity in 2018, which featured 57 campaigns against 54 European targets, driven primarily by a 38% decline in the number of campaigns in the U.K. in 2019 (16) relative to 2018 (26). However, on the whole, activism in Europe remained in line with historical levels, which have featured on average ~48 campaigns against ~45 European targets from 2015-2018.

In contrast, despite a slow third quarter, in 2019 the APAC region (including all of Asia, Australia and New Zealand) continued to see elevated levels of activism. Driven by a robust fourth quarter, the 28 campaigns targeting 27 APAC companies in 2019 was just below peak levels in 2018, and 33% greater than the average number of campaigns in the region from 2015-2018.

[5] Activism data from Lazard, *2019 Review of Shareholder Activism*, which includes all data for campaigns conducted globally by activists at companies with market capitalizations greater than $500 million at the time of campaign announcement; companies that are spun off as part of the campaign process are counted separately.

In this context, 2019 proved to be a record year for shareholder activism in Japan, both in terms of campaigns launched and capital deployed against Japanese companies. Driven by a strong Q4, full-year 2019 featured 19 campaigns against Japanese companies, a notable increase relative to peak levels of campaign activity in 2018 (16 campaigns), and significantly more than the average number of campaigns against Japanese companies from 2015-2018 (~9 campaigns). Capital deployed in Japan also saw major increases relative to historical figures. Driven primarily by Third Point's campaign at Sony, capital deployed against Japanese companies totaled $4.5 billion for the year, $2 billion greater than the $2.5 billion deployed in 2018, and ~216% greater than average capital deployed from 2015-2018. As a result, for the first time Japan became the busiest non-U.S. jurisdiction for shareholder activism, accounting for 23% of all non-U.S. campaigns and 27% of capital deployed against non-U.S. targets in 2019.

Peak Levels of M&A-Related Campaigns

The year 2019 featured 99 M&A-related campaigns, a record number that accounted for ~47% of all campaign activity. Notably, these figures were significantly higher than the record number of M&A-related campaigns in 2018, which featured 82 campaigns accounting for 33% of all campaign activity, and far greater than recent historical averages, which have featured 74 M&A-related campaigns accounting for 35% of all campaigns from 2015-2018. The most common M&A objectives were relatively evenly split across three categories in 2019—"bumpitrage" and opposition to deals (32%), break-up / divestiture (33%) and sale of the company (35%).

Notable examples of M&A-related campaigns include:

- Icahn pushing Hewlett-Packard (HP) to accept a takeover offer from Xerox and sending a letter to shareholders seeking their support after HP rejected the offer;
- Elliott seeking a break-up of Marathon Petroleum, after which Marathon announced it would spin off its Speedway unit and launched a comprehensive review;
- Elliott opposing Capgemini SE's proposed takeover of Altran Technologies and publicly criticizing the deal, but later saying it would consider selling its stake if Capgemini increases its bid; and
- Mantle Ridge reportedly seeking a sale of Aramark and considering building a consortium to submit a takeover proposal, ultimately settling with the company for board changes, including Mantle Ridge representation on the board.

Activists Continue to Push for Board-Level Change and Continue the Trend of Securing Board Seats Primarily via Settlement

In 2019, activists targeted 65 companies for board seats, with 122 board seats won. These figures are somewhat below historical levels, which have featured on average ~67 companies targeted for board seats, with activists securing an average of ~136 board seats per year from 2015-2018.

Interestingly, 2019 was a record year for activists nominating directors to replace 50% or more of the board ("long-slate" campaigns), as 2019 featured 20 long-slates, a dramatic increase relative to the 13 long-slate campaigns in 2018, and dwarfing the two long-slate campaigns from 2017. In this context, activists have won board seats in 67% of long-slate campaigns for a total of 34 board seats, which is down relative to the 45 board seats that were won in long-slate campaigns in 2018. However, the success of these campaigns in terms of board seats won remains to be seen, as battles for 39 board seats remain ongoing as of the end of 2019.

Finally, 2019 continued the trend of activists securing board seats primarily via settlement. For the year, settlements accounted for 84% of board seats won, with the majority of settlements occurring outside the proxy process.

Increased Outflows from Actively Managed Funds Bolster "Big 3" Influence

The trend of net outflows from actively managed funds increased in 2019, with ~$176 billion in net outflows through the first three quarters of the year relative to ~$105 billion in net outflows over that same period in 2018. Not surprisingly, the three largest asset managers—Vanguard, BlackRock and State Street—have been the main beneficiaries of these outflows as capital has moved away from actively managed funds towards passive investment strategies. Collectively, these three funds own 19.2% of the S&P 500, relative to ~16% in 2014. More broadly speaking, this trend extends beyond the Big 3, as the top five largest shareholders collectively own ~24.4% of the S&P 500, with the top 10 shareholders cumulatively holding 31%. As noted previously, as the "Big 3" and other large institutional investors have grown in size many have become more vocal on governance-related issues. As a result, understanding particular focus areas for these leading governance-focused investors is important for corporations to be able to meet the needs and expectations of their shareholders.

SELECT CAMPAIGNS / DEVELOPMENTS

Company	Market Capitalization ($ in billions)[6]	Activist	Outcome
AT&T	$268.8	Elliott	• Elliott discloses $3.2 billion stake in AT&T and argues that AT&T could unlock value by divesting assets, taking a more disciplined approach to M&A, de-levering its balance sheet, and overhauling the company's leadership / oversight • In October 2019, AT&T announces a 3-year business plan that includes new long-term financial targets, a review of its portfolio and commitment to no more major acquisitions, changes to the company's capital allocation (including share buybacks), the addition of two new independent directors, and the separation of the CEO / chairman roles when the current CEO retires, all of which are endorsed by Elliott
EssilorLuxottica	$63.7	Investor group (7 investors) / Third Point	• In Q2 2019, in the midst of a CEO succession dispute, Fidelity International, Baillie Gifford and five other investors nominate two directors to the company's board; two dissident nominees fail to get elected • After reportedly building a stake in the company, Third Point discloses in its Q3 letter to investors that it had been engaged with the company seeking governance improvements and for the company to accelerate its integration of Essilor and Luxottica
Emerson	$39.5	D.E. Shaw	• After engaging in private dialogue with the company, D.E. Shaw sends a letter to the board and publishes a white paper that criticizes the company's capital allocation and cost structure, calls for a separation of the company and improved corporate governance / executive compensation, and seeks an independent strategic review • Emerson and D.E. Shaw reach an informal settlement whereby the company will appoint an independent director and review its compensation program
Marathon Petroleum	$36.5	Elliott	• After Elliott calls for Marathon to be broken up into three separate companies, Marathon announces that it will spin off its Speedway unit • Marathon and Elliott reach a settlement in December under which the company will declassify its board and replace an outgoing board member with an Elliott-approved director
Seven & i	$34.1	Oasis	• Oasis sends a letter to Seven & i, a Japanese diversified retail group, seeking the company to divest non-core units and improve corporate governance and capital return
Hewlett-Packard	$29.8	Icahn Enterprises L.P	• Icahn pushes Hewlett-Packard (HP) to accept a takeover offer from Xerox, citing potential cost savings of $2 billion • After HP rejects Xerox's acquisition proposal, Icahn sends a letter to shareholders seeking their support
Unizo	$1.1	Elliott	• After Unizo rejects initial takeover proposals from Fortress and Blackstone, Elliott issues a public letter seeking an explanation from the company • Several competing tender offers remain outstanding as of year-end 2019

[6] Market capitalization as of campaign announcement.

Corporate Governance

POLICY

Institutional Shareholders Services (ISS) Files Complaint Against the Securities and Exchange Commission (SEC) Regarding New Guidance on Proxy Advisory Firms

In response to the SEC's interpretive guidance in August 2019 regarding the applicability of the federal proxy rules to proxy voting advice—which articulated the view that proxy voting advice generally constitutes a solicitation subject to the federal proxy rules—ISS filed suit alleging the issuance of the guidance was improper under the Administrative Procedure Act (APA), seeking to set aside the release on a number of different grounds.

In the complaint, ISS primarily seeks to distinguish "proxy solicitation," which ISS argues, "involves activities that seek to achieve a certain outcome in a shareholder vote," from "proxy advice" provided by ISS, which it argues, "involve providing independent research and analysis to a client for a fee." Thus, according to the complaint, proxy voting advice is properly regulated under the Investment Advisers Act of 1940—which offers protection against fraud and abuse by imposing a fiduciary standard and prohibiting advisers from engaging in fraudulent or deceptive conduct—and should not be regulated as a solicitation under Section 14(a) of the Securities and Exchange Act of 1934.

ISS's claims for relief are based on a series of alleged failures by the SEC under the APA, including allegations that the issued guidance: (1) is contrary to law; (2) was issued without following proper notice-and-comment rulemaking procedures; and (3) is arbitrary and capricious.

The SEC Proposes Rule Amendments to Proxy Voting Advice and the Shareholder Proposal Rule

<u>SEC Proposes Rule Amendments to Proxy Voting Advice</u>

In November, the agency proposed new rules that would (among other things) codify the SEC's interpretation that proxy voting advice generally constitutes a solicitation subject to the federal proxy rules.

Highlights from the proposed amendments include:

- <u>Rule 14a-1(l).</u> Amendments to Exchange Act Rule 14a-1(l) to clarify that the terms "solicit" and "solicitation" include, "[a]ny proxy voting advice that makes a recommendation to a security holder as to its vote, consent, or authorization on a specific matter for which security holder approval is solicited, and that is furnished by a person that markets its expertise as a provider of such proxy voting advice, separately from other forms of investment advice, and sells such proxy voting advice for a fee."

- <u>Rule 14a-2(b).</u> Amendments to Rules 14a-2(b)(1) and 14a-2(b)(3), which provide exemptions from the information and filing requirements of the proxy rules, that would subject proxy advisors relying on these exemptions to new conditions, including:
    - Requiring disclosure of material conflicts of interest in proxy voting advice;
    - Providing registrants and certain other soliciting persons an opportunity to review and provide feedback on proxy voting advice before it is issued, as well as final notice of the proxy advisory firm's recommendation at least two business days prior to delivery of the proxy voting advice to clients; and
    - Allowing registrants and certain other soliciting persons to request that proxy advisors include in their voting advice a link that allows the recipient of the advice to view a written statement with the registrant's or soliciting person's views on the proxy voting advice.[7]

- <u>Rule 14a-9.</u> Amendments to Rule 14a-9 would include examples of when the failure to disclose certain information in proxy voting advice—such as the proxy advisors methodology, sources of information and conflicts of interest—could be considered misleading.[8]

If adopted, the proposed rule amendments would provide a one-year transition period after the publication of a final rule in the Federal Register to allow affected parties sufficient time to comply with the proposed new requirements.[9]

[7] Press Release, Securities and Exchange Commission, SEC Proposes Rule Amendments to Improve Accuracy and Transparency of Proxy Voting Advice (November 5, 2019) *available at* https://www.sec.gov/news/press-release/2019-231.

[8] *See id.*; 17 CFR Part 240, Release No. 34-87457; File No. S7-22-19 at 70.

[9] 17 CFR Part 240, Release No. 34-87457; File No. S7-22-19 at 74.

SEC Proposes Amendments to the Shareholder Proposal Rule

On the same day that the SEC released proposed amendments to the proxy solicitation rules, the SEC also voted to propose amendments to Exchange Act Rule 14a-8 (the "Shareholder Proposal Rule"), which allows a company to exclude shareholder proposals from its proxy statement if the proposal does not meet specified substantive or procedural requirements, and similarly allows exclusion if the shareholder proponent fails to meet certain eligibility or procedural requirements.

Among other things, the proposed amendments would amend the criteria that a shareholder must satisfy in order to be able to require a company to include a proposal in its proxy statement, clarify the "one-proposal limit", and also change the levels of shareholder support a proposal must receive in order to be eligible for resubmission at the company's future meetings.[10] Highlights from the proposed rule amendments include:

- Eligibility Requirements under Rule 14a-8(b). Updating the requirement that a shareholder proponent hold at least $2,000 or 1 percent of a company's securities for at least one year to be eligible to submit a proposal for inclusion in a company's proxy materials to provide that a shareholder could satisfy any one of the following three ownership requirements to be eligible to submit a proposal: (1) continuous ownership of at least $2,000 of the company's securities for at least three years; (2) continuous ownership of at least $15,000 of the company's securities for at least two years; or (3) continuous ownership of at least $25,000 of the company's securities for at least one year.[11] Under the new thresholds, shareholders would be unable to aggregate their securities with other shareholders in order to meet the applicable ownership eligibility requirements, but would still be able to co-file or co-sponsor proposals as a group if each shareholder proponent in the group meets an eligibility requirement.

- One-Proposal Limit Under Rule 14a-8(c). Applying the one-proposal rule to "each person" rather than "each shareholder" who submits a proposal to clarify that a single person may not submit multiple proposals at the same shareholder meeting on behalf of different shareholders.[12] Thus, a shareholder-proponent would not be permitted to submit one proposal on their own behalf and simultaneously serve as a representative to submit a different proposal on another shareholder's behalf at the same meeting, and similarly, a representative would be unable to submit more than one proposal at the same meeting, even if the representative were to submit each proposal on behalf of different shareholders.[13]

- Resubmission Thresholds Under Rule 14a-8(i)(12). Providing that (1) a proposal would need to achieve support from at least 5 percent of the voting shareholders (instead of 3 percent) in its first submission in order to be eligible for resubmission in the following three years; (2) proposals previously included in a company's proxy materials or dealing substantially with the same subject matter submitted two times in the preceding five years would need to achieve at least 15 percent support (instead of 6 percent) in the most recent vote in order to be eligible for resubmission in the following three years; and (3) proposals previously included in a company's proxy materials or dealing substantially with the same subject matter submitted three times in the prior five years would need to achieve 25 percent support (instead of 10 percent) in the most recent vote in order to be eligible for resubmission in the following three years.[14] The proposed amendments would also allow a company to exclude a shareholder proposal that has been previously voted on three or more times in the last five years (even if it received at least 25 percent support in its most recent submission) if the most recently voted on proposal (i) received less than 50 percent of the votes cast and (ii) experienced a decline in shareholder support of 10 percent or more compared to the immediately preceding vote.[15]

Comments to both proposed rule amendments are due February 3, 2020.

[10] Press Release, Securities and Exchange Commission, SEC Proposes Amendments to Modernize Shareholder Proposal Rule (November 5, 2019) *available at* https://www.sec.gov/news/press-release/2019-232.

[11] *Id.*

[12] *Id.*

[13] *Id.*

[14] *Id.*; 17 CFR Part 240, Release No. 34-87458; File No. S7-23-19 at 51 ("Under proposed Rule 14a-8(i)(12), a shareholder proposal may be excluded from a company's proxy materials if it deals with substantially the same subject matter as a proposal, or proposals, previously included in a company's proxy materials within the preceding five calendar years if the most recent vote occurred within the preceding three calendar years and that vote was: [l]ess than 5 percent of the votes cast if previously voted on once; [l]ess than 15 percent of the votes cast if previously voted on twice; or [l]ess than 25 percent of the votes cast if previously voted on three times or more.")

[15] 17 CFR Part 240, Release No. 34-87458; File No. S7-23-19 at 58.

SEC's Division of Corporate Finance Issues Staff Legal Bulletin No. 14K Providing Guidance on the Excludability of Rule 14a-8 Shareholder Proposals Under the "Ordinary Business" Exception

In October 2019, the SEC's Division of Corporate Finance (the "Division") provided additional guidance on the excludability of shareholder proposals under Rule 14a-8(i)(7)—referred to as the "ordinary business" exception—which allows a company to exclude a shareholder proposal that "deals with a matter relating to the company's ordinary business operations." The guidance focuses on two central considerations underlying the ordinary business exception: (1) the significance of the proposal's subject matter and (2) the extent to which the proposal "micromanages" the company.

Significance

The guidance explains that the SEC staff takes a company-specific approach to evaluating the significance of a shareholder proposal for purposes of determining whether it should be excluded from a company's proxy materials under the ordinary business exception, instead of recognizing particular issues or categories of issues as universally significant. For example, the guidance notes that, "although a climate change proposal submitted to an energy company may raise significant policy issues for that company, a similar proposal submitted to a software development company may not raise significant policy issues for that company."[16] As a result, companies seeking to exclude shareholder proposals under Rule 14a-8(i)(7) should articulate why a particular proposal is not significant to their specific business operations.

In addition, the guidance also re-affirms the SEC staff's expectation that no-action letters contain well-developed board analysis of whether a particular policy issue raised by a shareholder proposal is sufficiently insignificant in relation to the company to warrant exclusion. The guidance re-affirms the SEC staff's expectation that such an analysis describe in detail specific substantive factors considered by the board and provides examples of how an analysis of certain of these factors could assist the SEC in making a determination regarding excludability. Such examples include:

- Whether the company has already addressed in some manner the policy issue raised by the proposal. For example, the guidance notes that an analysis that provides an explanation of the differences—or the delta—between the proposal's specific request and the actions the company has already taken could be useful for companies that have already addressed the policy issue in some manner but may not have substantially implemented the proposal's specific request to allow for exclusion under Rule 14-8(i)(10).[17] In this context, the SEC staff noted the company can seek exclusion on the basis that the company's prior actions have diminished the significance of the policy issue to such an extent that the proposal does not present a policy issue that is significant to the company.[18]

- Whether the company's shareholders have previously voted on the matter and the board's views on the results.[19] The guidance also re-affirmed the SEC staff's expectation that where a company's shareholders have previously voted on a matter, they would expect the voting results to be addressed as a part of the board's analysis.[20] The guidance provides examples of arguments for exclusion that the Division found unpersuasive following a prior shareholder vote because the discussion failed to demonstrate that the policy issue was no longer significant to the company. The guidance notes that the board's analysis of a prior shareholder vote would be more helpful if it included a robust explanation of how the company's subsequent actions, intervening events or other indicators of shareholder engagement on the issue relate to the significance of the underlying issue to the company. For example, this could include how shareholder engagement on an issue that received significant support has informed the board's views on its significance or an explanation of actions the board has taken to address concerns expressed in the proposal.[21]

Micromanagement

Whether a shareholder proposal may be excluded under the "ordinary business" exception because it "micromanages" the company hinges on an analysis of "the manner in which a proposal seeks to address the subject matter raised, rather than the subject matter itself."

[16] Shareholder Proposals: Staff Legal Bulletin No. 14K (CF), Division of Corporate Finance, Securities and Exchange Commission (October 16, 2019) *available at* https://www.sec.gov/corpfin/staff-legal-bulletin-14k-shareholder-proposals at footnote 6.

[17] *Id.*

[18] *Id.*

[19] *Id.*

[20] *Id.*

[21] *Id.*

The SEC staff "look[s] to whether the proposal seeks intricate detail or imposes a specific strategy, method, action, outcome or timeline for addressing an issue, thereby supplanting the judgment of management and the board" to determine whether the proposal "micromanages". In contrast, proposals framed as considerations for the company or that discuss the feasibility of, or evaluate the potential for a particular issue generally would not be viewed as "micromanaging."

Proxy Advisory Firms ISS and Glass Lewis Publish 2020 Proxy Voting Guidelines

In November 2019, ISS and Glass Lewis published updates to their proxy voting policies for the 2020 proxy season. Included below is a summary of key updates to voting policies covering the United States from both proxy advisory firms.

<u>ISS Benchmark Policy Updates</u>

- *Problematic Governance Structure – Newly Public Companies.* ISS will generally recommend a vote against or withhold from directors or boards that adopt provisions in their organizational documents that: (1) impose supermajority vote requirements to amend the bylaws or charter; (2) create a classified board structure; or (3) include "other egregious provisions." ISS will consider a reasonable sunset provision as a mitigating factor for newly public companies that contain these provisions in their organizational documents.

- *Independent Board Chair.* ISS updated its policy to provide the following specific factors that will increase the likelihood it will vote in favor of shareholder proposals that require the board chair to be filled by an independent director:

    - A majority non-independent board and/or the presence of non-independent directors on key board committees;
    - A weak or poorly defined lead independent director role that fails to serve as an appropriate counterbalance to a combined CEO/chair role;
    - The presence of an executive or non-independent chair in addition to the CEO, a recent recombination of the role of CEO and chair, and/or departure from a structure with an independent chair;
    - Evidence that the board has failed to oversee and address material risks facing the company;
    - A material governance failure, particularly if the board has failed to adequately respond to shareholder concerns or if the board has materially diminished shareholder rights; or
    - Evidence that the board has failed to intervene when management's interests are contrary to shareholders' interests.[22]

- *Board Composition – Diversity.* Now that the one-year transition period has passed for ISS's U.S. gender diversity policy, ISS will generally recommend voting against or withholding from the chair of the nominating committee (or other directors on a case-by-case basis) at Russell 3000 or S&P 1500 companies if the board lacks a female director.

- *Equity-Based and Other Incentive Plans – Evergreen Provision.* ISS will generally recommend against equity-based and other compensation plans that contain an evergreen (automatic share replenishment) feature.

- *Diversity – Labor Force Pay Gap Reporting.* ISS updated its policy related to proposals to provide reports on gender pay gap data to also address requests for pay data by race or ethnicity. ISS will generally vote case-by-case on requests for reports on a company's pay data by gender, race, or ethnicity, or a report on a company's policies and goals to reduce any gender, race, or ethnicity pay gap, taking into account a number of factors, including the company's current policies, practices and disclosures related to these matters, whether the company has been subject to recent controversy, litigation or regulatory actions, and whether the company's reporting on these matters lags behind its peers.

ISS's policy updates will be effective for shareholder meetings on or after February 1, 2020.

<u>Glass Lewis Updates to Proxy Guidelines</u>

- *Nominating and Governance Committee Performance.* Key updates regarding the evaluation of nominating and governance committee members relate to Glass Lewis' approach to: (1) the exclusion of Rule 14a-8 shareholder proposals and (2) director attendance.

[22] Institutional Shareholder Services, Americas Proxy Voting Guidelines Updates for 2020 (November 11, 2019) at 10-11 *available at* https://www.issgovernance.com/file/policy/latest/updates/Americas-Policy-Updates.pdf.

- Rule 14a-8 Proposals. Glass Lewis has clarified that it believes companies should only omit proposals when the SEC has *explicitly* agreed with the company's asserted basis for exclusion. Failure to do so will likely result in a recommendation that shareholders vote against the members of the governance committee.

- Director Attendance. Glass Lewis also codified additional factors that it will consider when evaluating the performance of governance committee members. In this context, Glass Lewis will generally recommend voting against the governance committee chair when (i) directors' records for board and committee meeting attendance are not disclosed; or (ii) when it is indicated that a director attended less than 75% of board and committee meetings but disclosure is sufficiently vague that it is not possible to determine which specific director's attendance was lacking.[23]

- *Compensation Committee Performance and Standards for Assessing the Audit Committee.* Glass Lewis's updated guidance regarding compensation committee performance and standards for assessing the audit committee codifies additional factors Glass Lewis will consider when evaluating the performance of members of these committees.

- *Say-on-Pay Proposals and Contractual Payments and Arrangements.* Glass Lewis's 2020 updates clarify the proxy advisory firm's expectations of company responsiveness following low shareholder support for say-on-pay proposals, clarifies the firm's approach to assessing how well companies link executive compensation to performance, and updates how the proxy advisory firm will analyze new and ongoing contractual payments and entitlements.

- *Gender Pay Equity.* Glass Lewis' updated guidance also clarifies the proxy advisory firm's approach to shareholder proposals seeking for companies to provide more disclosure on the actions they are taking to ensure men and women receive equal pay.

Glass Lewis's new policies will be effective for meetings held on or after January 1, 2020.

This review relates to general information only and does not constitute legal advice.
Facts and circumstances vary. We make no undertaking to advise recipients of any legal changes or developments.

[23] Glass Lewis, 2020 Proxy Paper Guidelines, An Overview of the Glass Lewis Approach to Proxy Advice, United States at 1.