

Morgan Lewis

RESPONDING TO SHAREHOLDER DEMANDS FOR EQUITY AUDITS

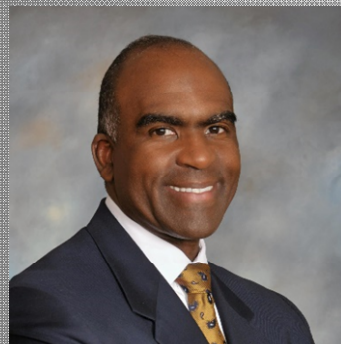
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Presenters



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Shareholder Proposals

- Under SEC Rule 14a-8, a shareholder can petition management to include a topic for vote at the company's annual meeting. Typically, resolutions are opposed by the board of directors, thus the shareholder's insistence for a vote.
- As long as the shareholder meets certain requirements, the company must include the shareholder proposal in its proxy.
 - The company may request "no-action" relief from the SEC to exclude unwelcome proposals.
 - In late 2021, the SEC implemented changes that made it harder for companies to decline to include shareholder proposals in their proxies.
- Virtually all shareholder resolutions are nonbinding because under corporate legal principles, shareholders don't have the right to manage the company. That said, the press can make these proposals a story, and board members may seek to implement the proposals as they could be voted out in future years if they do not act in accordance with the shareholders' will.
- These proposals may be voluntarily withdrawn by shareholders if the company agrees to address the shareholders' concerns.

Shareholder Proposals for ESG-Related Audits

- In recent years, shareholders have requested independent audits of companies' practices related to racial equity and/or civil rights to address racial or civil injustice.
 - Investors and proxy advisors view these audits as a way to measure the success of the company's DEI practices.
- Shareholders have also sought environmental audits on things like emissions, biodiversity, pollution, and deforestation.
- As of February, there have been more than 542 shareholder resolutions filed regarding ESG issues.
 - "Anti-ESG" proposals questioning/criticizing the DEI and environmental programs have also increased.

Equity Audits and Derivative Lawsuits

- Allegations that a company and its executives have fostered a “toxic” workplace and failed to provide its employees with an equitable and inclusive work environment are not just routine “personnel” or “employee relations” issues.
- Corporations are increasingly facing shareholder derivative lawsuits based on their allegedly misleading statements about their commitment to diversity and equity.
- These lawsuits typically allege that the corporation’s directors breached their fiduciary duties by failing to ensure the corporation complied with anti-discrimination laws or by authorizing false statements in public materials regarding the corporation’s commitment to diversity and inclusion.
- An equity audit can proactively mitigate the risk of a derivative lawsuit.

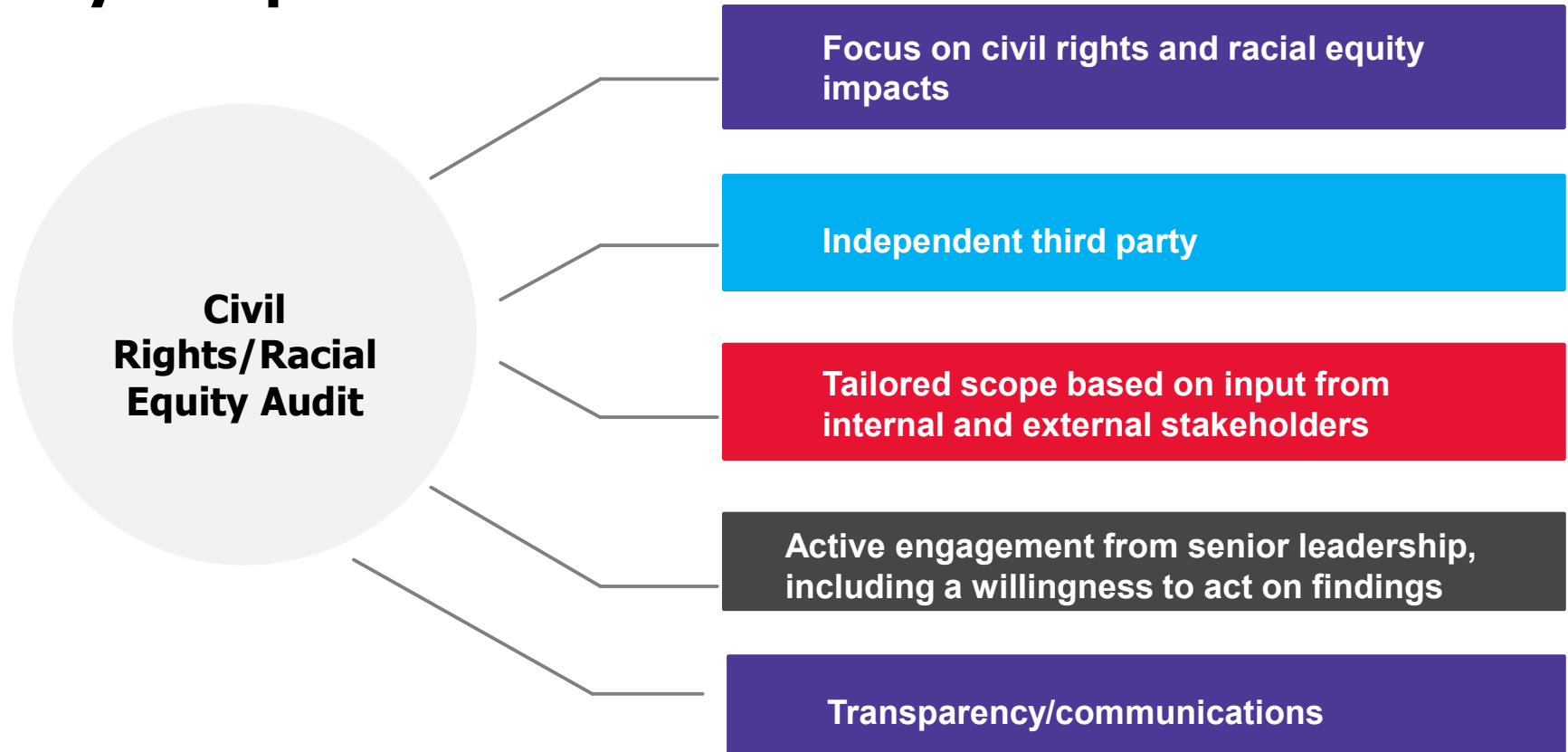
Proactive Equity Audits

- In addition to undertaking equity audits in response to shareholder proposals, some companies may choose to do so proactively.
 - ESG is a central topic for investors and proxy advisors.
 - This focus and the SEC's new requirement that companies disclose their human capital management has led to an increase in disclosure surrounding ESG by public companies.
 - Companies must weigh the need to be transparent about DEI efforts and aspirational goals but also not too specific in setting goals they are unlikely to reach, since once disclosed investors will follow up.

What Is a Civil Rights/Racial Equity Audit?

- An independent assessment of the internal and external impacts of an organization's policies, practices, products, and services to determine whether any practices inadvertently result in unrecognized discriminatory impacts.
 - Evaluates whether a company is reaching its environmental, social, and governance (ESG) and diversity, equity, and inclusion (DEI) objectives.
 - Provides shareholders, employees, and customers a credible and comprehensive evaluation of business representations, while mitigating reputational and legal risk.

Key Components

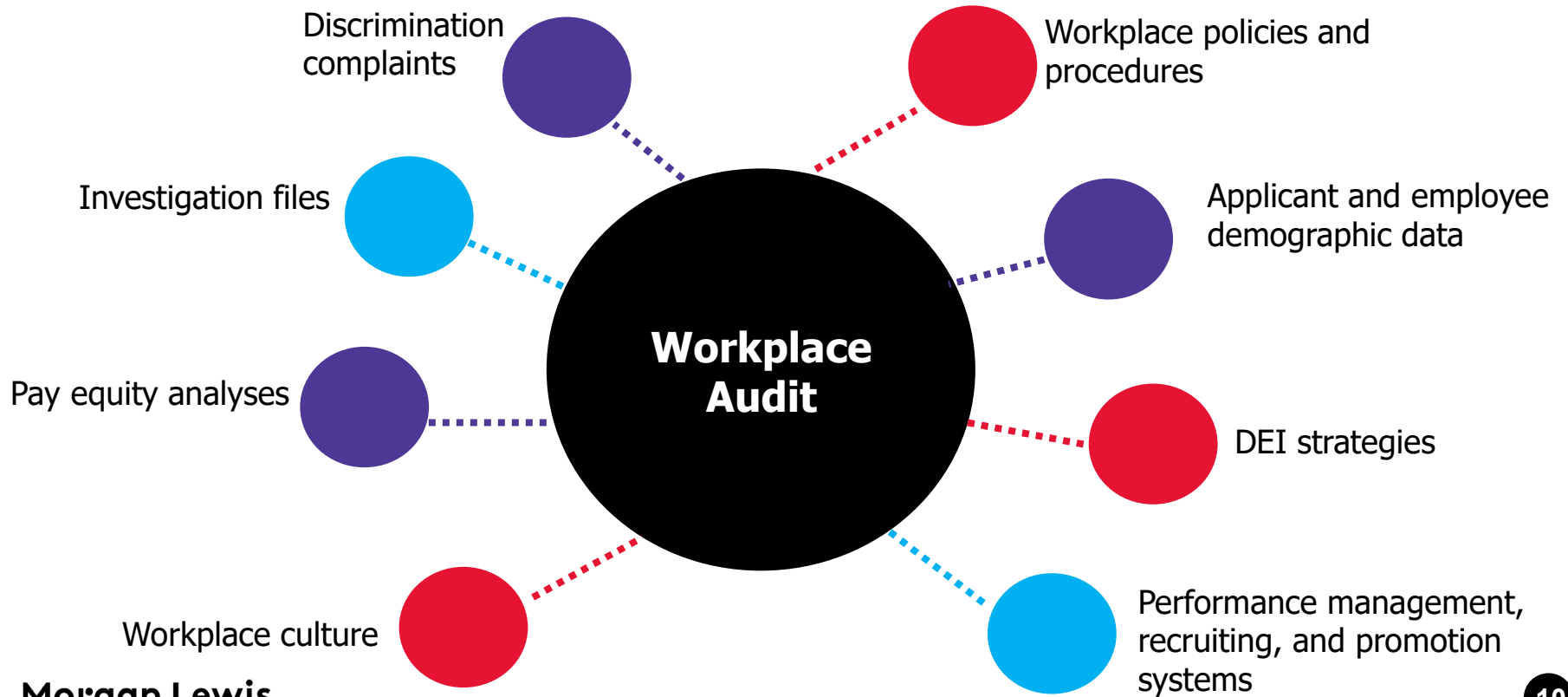


Types of Audits

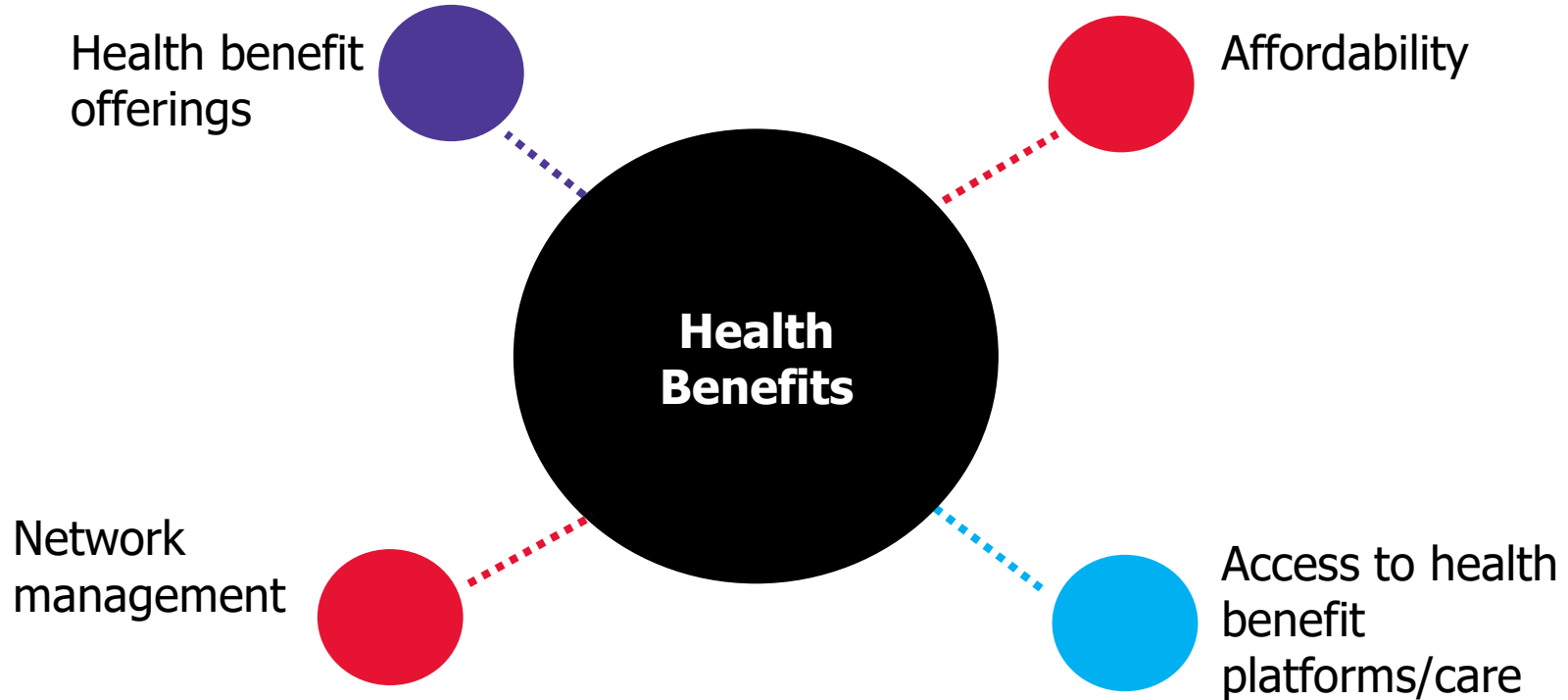
Areas of focus can include, for example:

- Workforce conditions
- Workforce diversity and inclusion
- Health benefits equity
- Environmental impacts of operations
- Corporate philanthropy and its impact on the greater community

Workplace Audit



Health Benefits



Corporate Social Responsibility



Equity Audits and Environmental Justice

- E.O. 13985 Equity Action Plan: US EPA
 - “Given EPA’s mission to protect human health and the environment, the agency’s pursuit of equity must include environmental justice (EJ).”
- Identification of Material EJ Risks and Opportunities
 - Environmental policies and procedures
 - Environmental permitting and compliance
 - Federal, state, and local environmental justice initiatives
 - Community engagement and outreach
 - Environmental disclosure policies and practices
 - Civil Rights Act compliance
 - Environmental/toxic tort litigation

Pros and Cons

Cons

Potential roadmap for action against the company (e.g., discrimination and/or breach of fiduciary duty)

Potential statutory disclosure obligations

Will be held accountable by internal and external stakeholders - Efforts to respond to one group of shareholders may result in anti-ESG proposals from another

Pros

Opportunity to identify issues before they become problems

Demonstrates commitment to these issues

Opportunity to publicize what the company is doing well

Opportunity to develop plans to address material risks and enhance future services and products

Best Practices for Responding to Shareholder Proposals

- Know the regulations that govern communications with shareholders.
- Engage in regular and transparent communication with shareholders.
- Know your largest shareholders' priorities.
- Familiarize yourself with proxy voting recommendations of proxy advisory firms.
- Plan, plan, plan.

Biography



Sharon Perley Masling

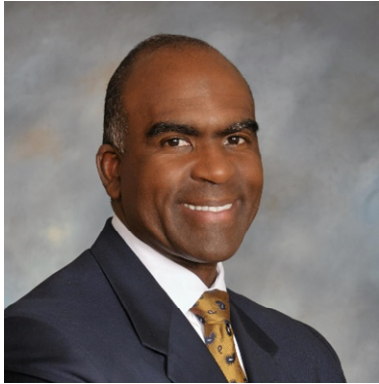
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Sharon, a leader of Morgan Lewis's Workplace Culture Consulting and Training Practice, helps companies and organizations create safe, respectful, diverse, and inclusive workplaces. Sharon also leads the firm's Reproductive Rights Task Force and developed and led the firm's COVID-19 Task Force. Having previously served as chief of staff and senior counsel to a commissioner at the Equal Employment Opportunity Commission (EEOC), Sharon provides insight on the enforcement of all employment civil rights laws and advises employers on employment discrimination issues.

Biography



Larry L. Turner

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Larry serves as co-leader of the Morgan Lewis Workplace Culture Consulting and Training Practice and is the former co-leader of the firm's Diversity Committee. Based on decades of experience in defending employers in various types of employment litigations, he counsels employers on corporate diversity initiatives, including best practices and litigation avoidance. He advises employers on building, maintaining, and evaluating diversity and inclusion efforts in a variety of industries, including but not limited to pharmaceutical, medical device, financial, and retail.

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Duke's practice focuses on environmental law and complex litigation. He represents clients in contribution actions, enforcement proceedings, citizen suits, toxic tort litigation, and regulatory matters, including actions brought under the Comprehensive Environmental Response, Compensation, and Liability Act (Superfund), the Clean Water Act, the Clean Air Act, the Resource Conservation and Recovery Act, and analogous state laws.

Biography



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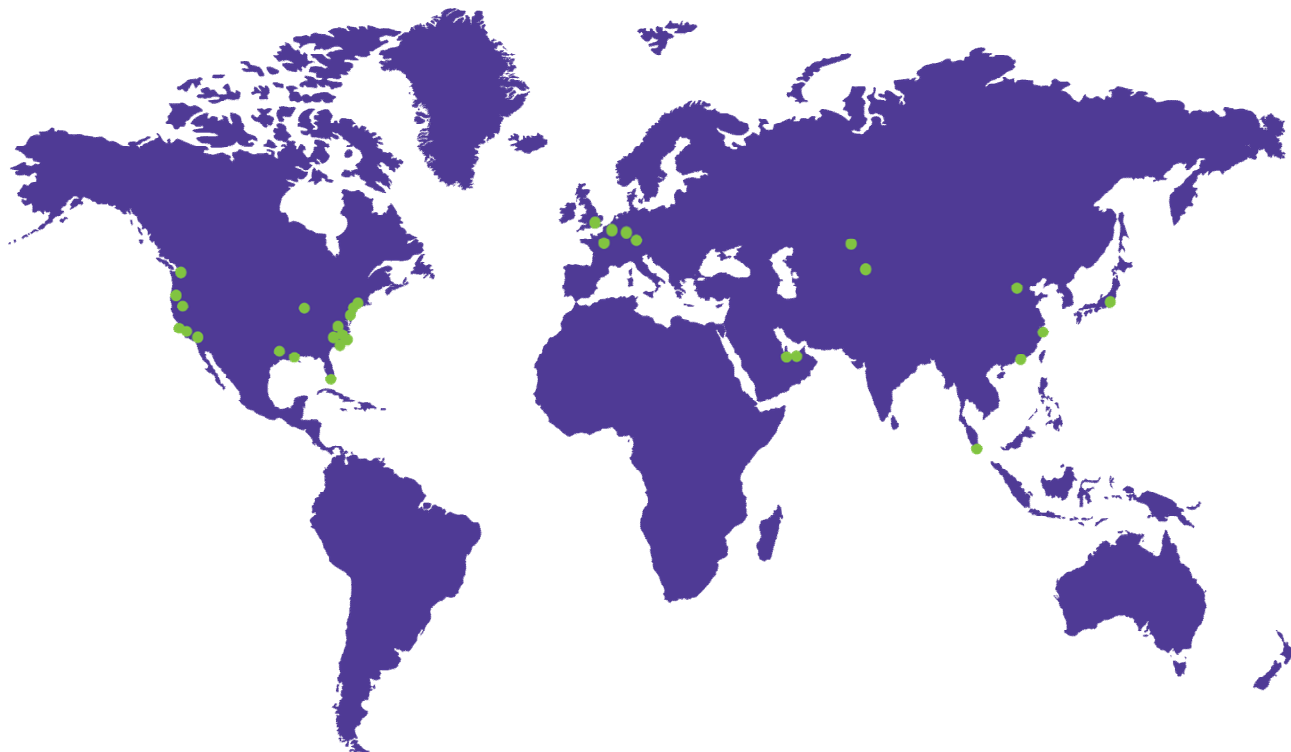
Karen has more than 25 years of experience defending class actions asserting violations of the federal securities law, derivative suits, claims arising from mergers and acquisitions, and appraisal actions. Karen has worked on numerous successful motions to dismiss or case dispositive motions with more than 30 granted since 2009, including appellate victories in the Third, Sixth, Seventh, Ninth, and Eleventh Circuits, and the Delaware Supreme Court. She has also tried several cases in federal and state courts, including the Delaware Court of Chancery.

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