PAUL HASTINGS

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Public Company Watch

Key Issues Impacting Public Companies

SEC Spotlight

SEC Settles First Cryptocurrency Insider Trading Enforcement Action

On May 30, 2023, the SEC settled charges against a former Coinbase product manager and his brother, in the SEC's first-ever cryptocurrency insider trading case: *SEC v. Wahi*, 2:22-cv-01009 (W.D. Wash., July 21, 2022). This is the first insider trading case based on specific allegations that digital assets on a secondary platform were securities. The defendants had moved to dismiss the SEC's complaint on the grounds that the tokens at issue were not investment contracts, comparing the tokens to baseball cards someone buys on the secondary market. Defendants argued that the developers who created the tokens at issue have no obligations whatsoever to purchasers who later bought those tokens on the secondary market.

In settling with the SEC, the Wahi brothers each agreed not to deny the SEC's allegations, to be permanently enjoined from violating Section 10(b) of the Exchange Act and Rule 10b-5 and to pay disgorgement of ill-gotten gains, plus prejudgment interest. The disgorgement and prejudgment interest in the SEC's case is deemed to be satisfied by the orders of forfeiture of the Wahi brothers' assets in the parallel criminal action. In a **press release** announcing the settlement, the SEC remarked "[w]hile the technologies at issue in this case may be new, the conduct is not. . . The federal securities laws do not exempt crypto asset securities from the prohibition against insider trading, nor does the SEC." The settlement does not reflect a judicial determination on the merits or whether the assets alleged to be securities were in fact securities.

On the heels of this settlement, during the first week of June 2023, the SEC levied charges against Coinbase for operating as an unregistered national securities exchange, broker, and clearing agency, as well as for engaging in the unregistered offering of securities through its staking-as-a-service program, and against Binance, Binance US and its founder for similar securities law violations. Taken together with the SEC's recent release on the reopening of the comment period for its proposed amendments to Rule 3b-16 of the Exchange Act to expand the definition of "exchange", highlighting the SEC's view that certain existing trading systems should fall within the current definition of exchange and that the exchange framework is dependent on the functionality of the trading system rather than the underlying technology, and the SEC's other recent moves to regulate crypto asset trading platforms and its enforcement action against Bittrex, it is clear that the SEC is taking an increasingly aggressive enforcement posture on this sector and ignoring calls from industry and legislators for regulatory clarity.

Clawback Reprieve Continued

Summary: The ongoing compensation clawback saga is nearing completion. For a summary of the clawback-related developments to date, please see the May edition of the Public Company Watch accessible **here**, our client alert on the final SEC rules accessible **here** and our client alert on the exchanges initial proposed listing standards accessible **here**.

Listing Standard Update: On June 5 and 6, 2023, respectively, the NYSE and Nasdaq each amended their proposed listing standards. The main crux of the amended proposals was to delay the effectiveness of the listing standards until October 2, 2023. Issuers will still have 60 days from the effectiveness date, or until December 1, 2023, to adopt a compliant policy. Pursuant to the amended listing standards, clawback-related disclosures will be required to be included in filings on or after October 2, 2023. On June 9, 2023, the SEC approved the listing standards on an accelerated basis, solidifying the effectiveness date of October 2, 2023.

In This Edition

Additional Revisions in NYSE Amended Listing Standards: The NYSE amended listing standards include additional revisions from the initial proposal. In the initial proposal, issuers were afforded a cure period in the event that they did not adopt a compliant policy within 60 days of the rule's effectiveness. However, for other violations of the exchange's clawback rules, trading in the issuer's securities would have been immediately suspended and delisting procedures immediately commenced. Pursuant to the amended listing standards, the cure period and procedures available in the event of the issuer's failure to adopt a compliant policy will be extended to all violations of the NYSE's clawback rules. In addition, the amended listing standards clarify that the exchange's clawback rules are applicable to the following types of issuers: (i) foreign private issuers; (ii) closed-end and open-end funds; (iii) passive business organizations, listed derivative or special purpose securities; and (iv) all companies listing only preferred or debt securities on the NYSE.

Takeaway: Issuers must adopt and adhere to a compliant clawback policy by December 1, 2023 and include related disclosures in the relevant SEC filings as of October 2, 2023.

SEC Rulemaking Tracker and Spring 2023 Regulatory Agenda

On June 13, 2023, the SEC's spring regulatory agenda was released. The agenda updated the timeline for anticipated SEC action on a number of topics, some of which have now been pushed back multiple times, as further explored in the below rulemaking tracker.

Recently Adopted Rulemaking		
Share Repurchase Modernization	Amendments requiring quarterly tabular disclosure of daily share repurchases and related narrative disclosures	Final rule adopted May 2023, effective July 31, 2023 Compliance for corporate issuers who file on domestic forms beginning with the first filing that covers the first full fiscal quarter that begins on or after October 1, 2023
10b5-1 Plans and Insider Trading	Series of changes revamping conditions to be met in order for a person to rely on the affirmative defense from insider trading available under Rule 10b5-1(c)(1), requiring related quarterly and annual disclosures and impacting Form 4 / 5 filings	Amendments to Forms 4 / 5 effective as of April 1, 2023 Compliance with the new disclosure requirements generally required in the first filing that covers the full fiscal period that starts on or after April 1, 2023 (or after October 1, 2023 for SRCs) Clarified in recent C&DI to mean, for December 31 fiscal year-end companies (that are not SRCs): • Quarterly disclosures in Form 10-Q for period ended June 30, 2023 • Annual disclosures in Form 10-K or 20-F for the fiscal year ended December 31, 2024 • Proxy / Information Statement disclosures for first annual meeting for election of directors after the completion of the first full fiscal year beginning on or after April 1, 2023
Pay v. Performance	Requires comprehensive narrative and tabular disclosure regarding the relationship between the compensation actually paid to executives and an issuer's financial performance	Compliance required in proxy and information statements for fiscal years ending on or after December 16, 2022, subject to phased lookback period

Form 144	Requires most Form 144s to be filed via Edgar rather than optionally on paper and extends deadline to 10 pm ET	Effective April 13, 2023
Glossy Annual Report	Requires reporting companies to furnish glossy annual reports on Edgar in PDF form no later than date report is first sent / given to stockholders	Effective January 11, 2023
Proxy Voting Advice	Rescinds rules requiring proxy firms to provide voting recommendations to clients and companies at the same time and to incorporate company responses to the proxy firm recommendations	Effective September 19, 2022
Compensation Clawbacks	Requires adoption of / compliance with clawback policy in connection with erroneously awarded incentive-based compensation	Effective October 2, 2023, meaning issuers will be required to include disclosures in relevant SEC filings after that date and to adopt and adhere to compliant clawback policies as of December 1, 2023
Pending Rulemaking		
Modernization of Beneficial Ownership Reporting	Significant amendments to modernize the filing deadlines for initial and amended beneficial ownership reports on Schedules 13D and 13G	Comment period reopened until June 27, 2023; final action pushed back until October 2023
Climate Change	Comprehensive climate-change-related disclosure overhaul impacting registration statements and periodic reports and related notes to financial statements	Awaiting final action; pushed back until October 2023
Cybersecurity and Risk Governance	Would require current reporting of material cybersecurity incidents and periodic updates as well as additional disclosure related to an issuer's cybersecurity risk management system and the board's cybersecurity oversight of cybersecurity risk and their expertise	Awaiting final action; pushed back until October 2023
SPACs	Comprehensive changes overhauling regulation of SPAC structure	Awaiting final action; pushed back until October 2023
Anticipated Rulemaking		
Corporate Board Diversity	Potential rulemaking requiring disclosure regarding diversity of board members and director nominees	Pushed back until April 2024
Human Capital Management	Additional rulemaking enhancing disclosures regarding human capital management (beyond what is already required by an issuer's Business section)	Pushed back until October 2023
Reg D and Form D Improvements	Updates to Reg. D exemption for private placements, including to definition of "accredited investor" and Form D	Pushed back until October 2023
Revisiting Definition of "Held of Record"	Revisiting definition of "held of record" used in Section 12(g) of Exchange Act (i.e., for determining whether an issuer will need to register its equity securities with the SEC)	Pushed back until October 2023
Rule 144 Holding Period	Potential amendments to resale safe harbor for restricted / control securities	Pushed back until April 2024

Activism Update

General Trends[1]

- U.S. campaigns declined 30% year over year during Q1 2023.
- The trend of multiple activists targeting the same company continued, with 11 such instances in the first quarter alone.
- Almost half of Q1 2023 campaigns included an M&A component, notwithstanding prevailing market conditions.
- Short slates have remained popular (50% of all contests in Q1).
- The vast majority of proxy contests continue to be settled (98% of all seats won by activists in Q1).

Notable Contests

- **Disney** – After agreeing to appoint a new independent director at the urging of **Third Point** in September, **Trian Partners** nominated its founding partner to the board in January, but withdrew the nomination after Disney unveiled a large scale restructuring plan.
- **Salesforce** – In January, facing pressure from **ValueAct Capital**, **Elliott Management**, **Starboard Value** and **Inclusive Capital**, the Company appointed three new directors, including the CEO of ValueAct. Elliott initially decided to proceed with a proxy contest, nominating a slate of directors, but eventually agreed to withdraw its nominations following strong Q1 results and the company announcing it would increase its share buyback program and move away from further acquisitive M&A activity. **Third Point** had also disclosed a stake in the company.
- **Bath & Body Works** – **Third Point** amassed a 6% stake an announced its intention to run a dissident slate. Third Point announced it would not nominate directors in 2023 after the company appointed three new directors, including two proposed by Third Point.
- **Illumina** – **Icahn** nominated three directors, called for rehiring the former CEO, and for the company to abandon/reverse its reacquisition of Grail; Icahn was successful in ousting the chairman and winning one board seat; a few weeks later, the CEO also resigned.

Litigation Corner

The Supreme Court Clarifies Who May Sue Under Section 11 of the Securities Act

On June 1, 2023, the Supreme Court issued a **unanimous decision** in Slack Technologies, LLC v. Pirani, holding that a plaintiff asserting a claim under Section 11 of the Securities Act must plead and prove that the securities they purchased are traceable to an allegedly misleading registration statement, even if the issuer has used a "direct listing" to offer its securities to the public. The opinion confirms that the decades-old tracing requirement will continue to be required for Section 11 claims, though the decision left open whether the same requirement would apply for claims under Section 12 of the Securities Act. A contrary ruling would have significantly expanded the potential scope of liability for issuers, particularly for those who use offerings exempt from the registration requirement. For a fulsome description of the decision, please see our **client alert**.

Delaware Supreme Court Sides with SolarWinds in Shareholder Suit

Summary: On May 17, 2023, the Delaware Supreme Court upheld a September 2022 decision dismissing a shareholder suit against SolarWinds Corporation. In 2021, shareholders sued SolarWinds for a 2020 cybersecurity incident (for additional information on the incident see our **client alert**), claiming that SolarWinds and its executives breached their fiduciary duties by failing to monitor SolarWinds' cyber risks, resulting in one of the biggest breaches in recent times. The Delaware Supreme Court upheld the Chancery

1 Data based on the following Barclays report: Record pace of activist campaigns | Barclays CIB.

Court's dismissal of the suit, holding that SolarWinds and its executives were not liable for negligence or for the breach of their fiduciary duties.

Takeaway: This holding is a change of pace from more recent developments highlighting executive liability in the cybersecurity context. Still, data privacy and cybersecurity is an area that is increasingly scrutinized by courts, federal regulators, and administrative agencies. Officers and directors must continue to be transparent with their company, senior leaders, and regulators to ensure that risks are addressed at the most senior level necessary.

Other Regulatory Updates

The Growing Anti-ESG Movement

Overview: As companies respond to increasing investor demand for ESG-related initiatives and disclosures, certain lawmakers in Congress, state governors and attorneys general, interest groups, and investors have launched an organized and concerted pushback against companies' ESG commitments and activities — coined as the "anti-ESG" or "anti-Woke" movement. It is increasingly gaining momentum and visibility, particularly in states where conservative policies remain popular, including Texas, Florida, South Carolina, Montana, Indiana, Kentucky, and Missouri, to name a few.

Current Trends: Several states have passed laws prohibiting state financial institutions from investing public money to promote ESG goals, and certain state treasurers have withdrawn public pension funds from investment companies accused of promoting a "woke" political agenda above the financial interests of their customers. Industry climate initiatives like the Net Zero Asset Managers Initiative (NZAM) and the Net Zero Insurance Alliance (NZIA) have also been under attack as violating antitrust rules, resulting in a number of member companies discontinuing their participation.

Recently, in March 2023, 19 Republican governors established an anti-ESG coalition to block the Biden administration's ESG policymaking and impose a state-level crackdown on ESG-related investment decisions and company practices that they view as ideologically driven. This follows an earlier series of warnings issued by state attorneys general to investment companies, which raised fiduciary and antitrust concerns regarding the companies' approach to ESG investing. Further, in recent weeks there has been an increase in instances of state attorneys general issuing Civil Investigative Demands (CIDs) to companies under their broad unfair and deceptive acts and practices authority, inquiring about their ESG practices. A CID is an administrative subpoena that allows federal government agencies to request substantial information from companies without going through formal court procedures. We are seeing an increase in that trend which could lead to widespread enforcement actions.

Takeaway: The anti-ESG movement is expected to accelerate, and we anticipate an increase in ESG and Anti-ESG shareholder activism overall. Given that ESG and Anti-ESG challenges could lead to reputational or financial impacts on the business, companies should seek immediate counsel to review and prepare relevant strategies, particularly if they receive inquiries or CIDs from state attorneys general. Companies also should ensure that their ESG-related initiatives are backed by careful analysis and data, such as key performance indicators (KPIs) and materiality assessments that identify and substantiate the connection between ESG-related risks and financial performance.

Non-Compete News

Summary: : In the past few weeks, we have seen a continuation of the shifting regulatory landscape surrounding non-competes in favor of employees. On May 24, 2023, Minnesota was the latest state to significantly restrict the use of non-compete agreements. At the federal level, on May 30, 2023, the General Counsel of the National Labor Relations Board, Jennifer Abruzzo, issued a memorandum asserting that non-compete agreements generally violate the National Labor Relations Act. The memorandum is described in further detail in our **client alert**.

M&A Considerations: As prohibitions against non-compete agreements continue to spread at the federal and state level, employers should be aware of the changing landscape and the potential for future implications, including in the M&A context, where covenants not to compete are often a critical component of the underlying deal. Currently, most states, including the Minnesota legislation, distinguish between the laws governing covenants not to compete when incident to the sale of a business, as does the FTC's proposed rule (see our **client alert** for more information), but it is unclear how this issue will evolve. Accordingly, transactions

requiring such covenants should be carefully crafted in a manner to stand up to increased regulatory scrutiny.

Expanded Protections under the Pregnant Workers Fairness Act

Summary: On June 27, 2023, the Pregnant Workers Fairness Act (the "PWFA") will go into effect, which expands existing federal law with respect to the accommodation of pregnant employees.

Background: The Pregnancy Discrimination Act of 1978 (the "PDA") prohibits pregnancy discrimination and requires covered employers to treat employees affected by pregnancy, childbirth, or related medical conditions the same as other similarly situated employees. In addition, the Americans with Disabilities Act of 1990 (the "ADA") prohibits discrimination on the basis of disabilities and requires covered employers to provide reasonable accommodations to qualified employees with disabilities.

Expansion of Rights: Under the PWFA, employers with 15 or more employees are required to make reasonable accommodation for "the known limitations related to pregnancy, childbirth and related medical conditions of a qualified employee" unless the accommodation would impose an "undue hardship" on the employer's operation. The PWFA constitutes a significant expansion of rights because federal law currently only requires employers to accommodate pregnant employees who qualify as "disabled" within the meaning of the ADA, but under the PWFA employers must provide reasonable accommodations for pregnancy-related medical conditions irrespective of whether those conditions rise to the level of a disability (so long as the accommodations do not impose an undue hardship). The PWFA also defines a "qualified employee" more expansively, as it includes not only employees who, with or without reasonable accommodation, can perform the essential functions of a job, but also employees who are temporarily unable to perform an essential job function due to pregnancy, childbirth, or a related condition.

Interactive Process: The PWFA adopts the same meaning of "reasonable accommodation" and "undue hardship" as used in the ADA, including the "interactive process," which is the good-faith discussion between the employer and employee to try to identify an appropriate reasonable accommodation. The PWFA expressly prohibits employers from requiring covered employees to "accept an accommodation other than any reasonable accommodation arrived at through the interactive process." Importantly, employers also cannot force employees "to take leave, whether paid or unpaid, if another reasonable accommodation can be provided." In other words, leave is a last resort if there are no other reasonable workplace accommodations that can be provided absent undue hardship.

Remedies: The PWFA incorporates Title VII's enforcement procedures and remedies. A charge must be filed with the EEOC before filing suit, which has authority to investigate and litigate claims for individual and class action claims. Like Title VII, an aggrieved individual can recover back pay, front pay, compensatory and punitive damages, and attorneys' fees and costs.

Takeaway: In light of the expansion of rights provided under the PWFA, employers should consider reviewing and updating their reasonable accommodation policies to comply with the PWFA and train human resources and management personnel involved in handling accommodation requests on the PWFA's requirements. The EEOC is required to issue regulations to provide examples of reasonable accommodations that address known limitations related to pregnancy, childbirth, and related medical conditions. Until it does so, employers should consider the types of reasonable accommodations that they can make for their pregnant employees consistent with the PWFA.

Annual DGCL Amendments

The Delaware Senate recently passed a bill providing for certain amendments to the Delaware General Corporation Law (DGCL), which, if adopted by the Delaware House of Representatives and signed into law by the governor of Delaware, will generally by effective on August 1, 2023.

The proposed amendments include a number of changes which would simplify pertinent matters for corporations, particularly public companies and companies seeking to go public in the future. For example, the amendments include a provision which would enable a corporation to implement a forward stock split (and any necessary proportional increase in authorized stock incident thereto) without stockholder approval, and another which would reduce the stockholder vote needed in order to implement a reverse stock split for listed companies in certain circumstances—which is especially significant to issuers seeking to implement a reverse stock split in order to maintain their listed status on Nasdaq or the NYSE in light of the recent trend of brokerage firms declining to exercise their discretionary voting in routine proposals and resulting difficulty for issuers in passing such proposals. In addition, the proposed amendments would simplify the process for the ratification of defective corporate acts, as well as further empower a company's

board of directors to delegate to officers (or others) certain powers in connection with the issuance of rights and options. A fulsome explanation of the proposed changes is set forth in Richard Layton's publication on the topic: 2023 Proposed Amendments to the General Corporation Law of the State of Delaware accessible **here**.

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About Paul Hastings

With widely recognized elite teams in finance, mergers & acquisitions, private equity, restructuring and special situations, litigation, employment, and real estate, Paul Hastings is a premier law firm providing intellectual capital and superior execution globally to the world's leading investment banks, asset managers, and corporations.