PAUL HASTINGS

May 2023

Public Company Watch

Key Issues Impacting Public Companies

SEC Spotlight

Share Repurchase Disclosure Modernization

Summary: On May 3, 2023, the SEC adopted new disclosure requirements for issuers' repurchases of equity securities.

Daily Repurchase Disclosure: In their Form 10-Qs / Form 10-Ks, corporations will be required to include a new exhibit containing tabular disclosure of daily repurchase activity. The tabular disclosure will contain disclosure of the daily number of shares purchased and the average price paid per share, among other information.

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In addition, the rules introduce a checkbox requirement, whereby issuers must indicate if any of their Section 16 officers and directors purchased or sold securities that are the subject of a share repurchase plan in the four business days preceding and following the announcement of the share repurchase plan or any expansion thereof.

Revision / Expansion of Narrative Discussion: The final rules revise and expand the current disclosure requirements set forth in Item 703 of Regulation S-K, which is implicated in both Form 10-K and Form 10-Q. The expanded narrative disclosure is geared to be viewed in conjunction with the new tabular exhibit in order to provide investors with fulsome qualitative and quantitative information to evaluate issuer share repurchases. Specifically, issuers will be required to provide the following new disclosure:

- Regarding the objectives or rationales behind each share repurchase plan;
- The process or criteria utilized by the issuer to determine the amount of the repurchases; and
- Any policies and procedures related to trading in its securities by officers and directors made concurrently with a repurchase plan (including any prohibitions).

Issuer Disclosure of Adoption / Termination of 10b5-1 Plans: New Item 408(d) will require issuers to provide disclosure regarding the adoption or termination of Rule 10b5-1 plans (similar to the disclosure regarding the adoption / termination of such plans by officers or directors set forth in Item 408(a), which was adopted as part of the insider trading reform rules last fall, described in further detail in our **client alert**).

Timing: Generally, corporations will be required to comply with the amendments on Forms 10-Q and 10-K (for their fourth fiscal quarter) beginning with the first filing that covers the first full fiscal quarter that begins on or after October 1, 2023. Alternative compliance deadlines apply to foreign private issuers (FPIs) filing on FPI forms and listed closed-end funds.

Our full client alert can be found **here**.

SEC Proxy Rules Survive Another Challenge

The current SEC administration's rollback of proxy advice regulations (as described in full detail in our **client alert**) passed another hurdle when a district court in the Middle District of Tennessee held that the SEC could repeal restrictions on proxy advisory firms that were adopted by the SEC under the leadership of former SEC Chair Jay Clayton, rejecting a challenge by the Chamber of Commerce. A related case brought by the National Association of Manufacturers is currently before the Fifth Circuit after the SEC prevailed in a Texas district court. The issue will continue to be litigated for the near future through the multiple parallel actions in progress.

Brief Clawback Reprieve

Summary: In November 2022, the SEC adopted final rules related to the recovery of erroneously awarded incentive-based compensation from current or former executive officers, which are summarized in our **client alert**. While the final rules became effective on January 27, 2023, the NYSE's and Nasdaq's proposed listing standards requiring listed issuers to adopt and adhere to a compliant clawback policy have not been approved by the SEC, and the SEC has provided guidance stating that it does not expect compliance with the disclosure requirements outlined in the rules until issuers are subject to the applicable listing standard. In February 2023, the exchanges each released their proposed listing standards. As further described in our **client alert**, the proposed listing standards generally mirrored the SEC rules, though the consequences for non-compliance varied among the two exchanges.

Listing Standard Update: The SEC had until April 27, 2023 to approve or disapprove the proposed listing standards. However, on April 24, 2023, the SEC decided to delay its decision-making until June 11, 2023. The SEC could make a determination on the rules anytime between now and June 11, 2023, including an election to delay further; but the exchanges' rules must be effective by November 28, 2023. Once the listing rules are effective, issuers will have 60 days to adopt a compliant policy.

SEC Insight on Beneficial Ownership Modernization

Background: In February 2022, the SEC proposed significant amendments to modernize the filing deadlines for initial and amended beneficial ownership reports on Schedules 13D and 13G, which are summarized in our **client alert**. On April 28, 2023, the SEC reopened the comment period for the proposed rules until June 27, 2023 and issued a memorandum providing supplemental data and analysis on certain economic effects of the proposed amendments.

SEC Insight: In the memo, the SEC provides information regarding the historic number and type of Schedule 13D and 13G filings received, distinguishing between "corporate action" triggered filings (i.e., filings driven by an increase in beneficial ownership resulting from corporate actions or off-market transactions like IPOs, restructurings or compensation awards) and "non-corporate-action" triggered filings indicative of activist campaigns. Furthermore, the SEC analyzed the potential impact of shortening the initial Schedule 13D filing deadline from ten days after crossing the requisite 5% ownership threshold to five days. The SEC found that its research indicates that shortening the filing deadline for corporate action driven Schedule 13Ds might result in little added benefits, while increasing compliance costs and having no meaningful change on the activities of the underlying filers. In contrast, the SEC found a pattern of abnormal returns surrounding Schedule 13Ds precipitated by non-corporate-actions, including "meaningful" abnormal returns between days five and ten post-trigger date. The SEC believes that the pattern of abnormal returns translates into tens of millions of dollars in aggregate harm to stockholders that could be prevented by correcting the information asymmetry among investors sooner via the proposed abbreviated filing deadline, thereby promoting trust in the markets. Furthermore, the SEC found that the vast majority of filers acquired most of their respective ownership stakes within five days of crossing the threshold (i.e., 92% of filers acquired 90% of their ultimate ownership stake and 98% acquired 75% of their ultimate ownership stake within five days), thereby limiting the impact of the proposed shortened filing deadline on potential activist filers.

Takeaway: It would not be surprising if the SEC decides to bifurcate the new Schedule 13D filing deadline in the final rule given the SEC's distinction between corporate action and non-corporate-action Schedule 13D filings, their willingness to point out the harm to unequally informed investors that could be solved by instituting a five-day filing deadline for non-corporate-action filings and their reluctance to conclude that shortening the filing deadline would cause the few activist investors who accumulate a significant amount of their ownership position after the proposed deadline to instead abandon those campaigns. Regardless, it is likely that a five-day initial filing deadline for non-corporate-action filings will be adopted at some point in the near-term.

SEC 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 60 days after publication in the Federal Register 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)
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
Pending Rulemaking		
Compensation Clawbacks	Requires adoption of / compliance with clawback policy in connection with erroneously awarded incentive-based compensation	Compliance date pending SEC approval of NYSE / Nasdaq listing rules, but exchanges' rules must be effective by November 28, 2023 leaving issuers to comply by January 27, 2024 at the latest
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
Climate Change	Comprehensive climate-change-related disclosure overhaul impacting registration statements and periodic reports and related notes to financial statements	Awaiting final action
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
SPACs	Comprehensive changes overhauling regulation of SPAC structure	Awaiting final action
Anticipated Rulemaking		
Corporate Board Diversity		
Human Capital Management		
Reg D and Form D Improvements		
Revisiting Definition of "Held of Record"		
Rule 144 Holding Period		

Litigation Corner

Recent Delaware M&A Litigation

A recent decision implicating the level of scrutiny for agreements governed by Delaware law, which may impact stockholder activism, should be top-of-mind for companies undergoing or considering M&A processes: ***In re Edgio, Inc. Stockholders Litigation*, Consol. C.A. No. 2022-0624-MTZ, 2023 WL 3167648 (Del. Ch. May 1, 2023) (Unpublished)**.

In *Edgio*, the Delaware Court of Chancery denied a motion to dismiss a public company's stockholders' lawsuit that sought to enjoin contractual restrictions imposed on an incoming large stockholder, which prohibited stock transfers to anyone identified on a particular list of the fifty "most significant" activist investors.

- *Background*: Edgio, Inc., a publicly-traded telecommunications company, negotiated a strategic transaction with a PE firm, which involved acquiring one of the firm's portfolio companies in exchange for a 35% stake in the public company. The transaction was approved by a majority of the public company's stockholders. Following closing, certain of those stockholders sought to enjoin provisions in an accompanying stockholder agreement signed by the public company with the PE firm, including a restriction on the PE firm's selling or transferring shares in the public company to a list of activist investors. Principally, the plaintiff stockholders argued that the stockholder agreement was improper because it had terms that would entrench the board and protect it from stockholder activism, which analysts had been predicting might occur due to poor financial performance. Defendants countered that because the stock issuance had been approved by a majority of the public company's stockholders, the decision to negotiate and execute the stockholder agreement with the investor was entitled to deference under the business judgment rule.
- *The Opinion*: The court denied defendant's motion to dismiss, specifically holding that a claim to enjoin enduring alleged entrenchment devices is not entitled to business judgment deference. Instead, the Court opined that as long as a plaintiff pleads facts sufficient to support a reasonable inference that a board acted defensively in response to a perceived threat, a reviewing court applying Delaware law to a motion for injunctive relief (as opposed to damages) should more closely scrutinize the transaction under the *Unocal* standard, rather than give it simple business judgment deference.
- *Key Takeaway*: Activist stockholders and the plaintiffs' bar are actively challenging corporate actions that can be deemed to have a direct or indirect impact on any pending or future activism. Boards of directors and their advisors need to be mindful of such potential litigation and the possibility that a Board's action may become subject of enhanced scrutiny under the *Unocal* standard.

Other Regulatory Developments

Antitrust Regulators Focused on Labor Markets

Overview: The Antitrust Division of DOJ and the FTC under the current administration have demonstrated their intention to regulate and bring enforcement actions targeting alleged anticompetitive behavior in the labor markets. The DOJ has brought several criminal cases alleging anticompetitive "no-poach" agreements against firms and individuals. Thus far, the DOJ has been largely unsuccessful in this effort, including a recent loss in a high-profile criminal case against aerospace engineering managers. The FTC, for its part, has similarly engaged in enforcement actions to challenge employer non-compete restrictions, requiring companies to sign consent agreements prohibiting their use. Additionally, in early January the FTC proposed regulations that would impose a near total ban on non-compete agreements, which the agency says affect 1 in 5 US workers (for an overview of the ban visit this **client alert** and for an overview of the ban in the M&A realm see this **client alert**).

Merger Review Process: In the M&A context, there are growing calls for the agencies to more closely examine labor concerns during the merger review process. The FTC Bureau of Competition Director Holly Vedova recently said that the FTC is "laser focused" on harms to labor markets resulting from mergers, suggesting the agency has begun to target such competitive harms "like a heat sinking missile." Vedova, speaking in her own capacity, said that labor markets should be treated separately, and somewhat differently, from output markets for products or services. While the analytical framework for labor and product markets is essentially the same, "labor markets have unique characteristics that product markets on the sell side sometimes lack," with the concern being lower quality of jobs available, employee lack of mobility, and dampened wages. She noted that because the labor market and output market are analyzed separately, there could be a situation where there is no competitive overlap in the products or services offered by the merging parties, but the merger could nonetheless hamper competition in the labor market, particularly in rural areas where there may be few employers.

This is not the first indication that the FTC is fixated on labor markets in merger reviews. FTC Chair Khan and Commissioner Slaughter noted in February 2022 that they were prepared to proceed with a merger challenge on the basis of effects in a labor market. In 2020, the FTC stated that it closed its investigation into the proposed merger of Aveanna Healthcare and Maxim Healthcare, a deal the parties had abandoned, noting a concern that the transaction could harm competition in the nursing care labor market. The FTC is looking at labor in every single merger they examine. Many transactions will likely take longer to proceed through the regulatory review process, and should proactively address this by having appropriate provisions in purchase agreements to address potential delays and intentionally approaching the creation of any documents that might be turned over during a regulatory review process.

The EU's Proposed Corporate Sustainability Due Diligence Directive Continues to Progress

Overview: A European legislative initiative aimed at requiring companies to undertake human rights and environmental due diligence is gradually but steadily making its way through the EU institutions, with potentially significant impacts on non-EU companies as well.

Summary: The Corporate Sustainability Due Diligence Directive ("CSDD"), as proposed by the European Commission on March 10, 2021, requires **EU and non-EU companies with significant EU operations** to identify, assess, and mitigate adverse human rights and environmental impacts arising from their operations, as well as those of their upstream and downstream value chains, as described in further detail in our **client alert**. On April 25, 2023, the European Parliament's Committee on Legal Affairs ("JURI Committee") announced that it had adopted a compromise text in response to the European Commission's proposed CSDD, with substantial amendments to expand the scope of companies and sectors to be covered under the legislation. While that text has not yet been formally issued, the JURI Committee's draft proposals portend a potentially contentious "trilogue" among the European Commission, the Council of the European Union, and the European Parliament, each of which have staked out different negotiating positions on key aspects of the CSDD.

Differences: The differences between the proposals are anticipated to have significant consequences for the scope of covered companies, the extent of due diligence obligations, and exemptions from civil liability.

- *European Commission's Proposal*: Under the European Commission's proposal, the CSDD would **apply to non-EU companies** that generated (i) more than €150 million in net turnover in the EU in the past year; or (ii) more than €40 million in net turnover in the EU in the past year, if at least 50% of their net worldwide turnover was generated in one or more of the defined high-impact sectors, including manufacture and wholesale trade of textiles, clothing and footwear, agriculture, manufacture of food products, and extraction and wholesale trade of mineral resources.

- *JURI Committee Proposal*: The JURI Committee, however, seeks to lower these thresholds, such that non-EU companies would be covered under the CSDD if they generated (i) more than €40 million in net turnover in the EU in the past year; or (ii) more than €8 million in net turnover in the EU in the past year, if at least 30% of their net worldwide turnover was generated in one or more of the high-impact sectors. Further, the JURI Committee's draft proposal seeks to expand the list of high-impact sectors to include apparel, marketing and advertising of foods and beverages, animal products, energy, construction, and information and communication technologies, among others. The proposals also omit the Commission's proposed safeguard to protect companies from civil liability when damages were caused by adverse impacts arising from activities of an indirect business partner.

Key Takeaway: These latest developments signal that U.S. companies operating in the EU will need to carefully monitor their continuously evolving human rights and environmental due diligence obligations. With key differences among the European Commission, the Council of the European Union, and the European Parliament in their approaches to the CSDD, companies can expect tense negotiations and active stakeholder participation in the coming months. While the specifics of the final text of the CSDD are likely to change, when taken together with current and pending domestic due diligence legislation, such as the German Supply Chain Due Diligence Act, it is expected to have broad impact—either directly or indirectly—on EU and non-EU companies doing business in the EU or within the value chains of companies within scope. For more information, please see our **client alert**.

Next Steps: It is anticipated that the European Parliament will vote to finalize its position on the CSDD in June 2023. Our ESG practice will host a webinar reviewing the Parliament's final negotiation position and the potential impact for companies with operations in the EU, so keep an eye out for an invite on the topic.