

MAYER • BROWN

Preparing for the 2019 US Proxy and Annual Reporting Season

Robert Gray, Jr.

Partner

+1 713 238 2600

rgray@mayerbrown.com

Candace Jackson

Associate

+1 312 701 8754

crjackson@mayerbrown.com

Laura Richman

Counsel

+1 312 701 7304

lrichman@mayerbrown.com

Michael Hermsen

Partner

+1 312 701 7960

mhermsen@mayerbrown.com

Anna Pinedo

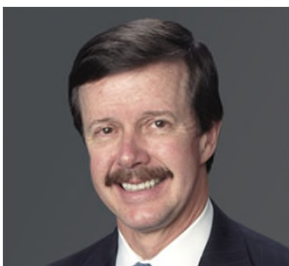
Partner

+1 212 506 2275

apinedo@mayerbrown.com

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Presenters



Robert Gray, Jr.
Partner



Michael Hermsen
Partner



Candace Jackson
Associate



Anna Pinedo
Partner



Laura Richman
Counsel

- Governance Initiatives
- Potential Proxy Advisory Regulatory Changes
- Trend in Proxy Statement Disclosure

Governance Initiatives

- New York City Comptroller and New York City Pension Funds
 - Boardroom Accountability Project 2.0
 - Commenced in September of 2017, involving 151 companies
 - Seeking standardized matrix disclosure to make boards more diverse, independent and climate-competent
 - Previous project focused on proxy access
- <https://comptroller.nyc.gov/wp-content/uploads/2017/09/Example-Board-Matrix.pdf>

Governance Initiatives (*cont'd*)

- Vanguard
 - 2017 Open letter to directors of public companies
 - 2018 Investment Stewardship Annual Report
 - Board Composition
 - Executive Compensation
 - Oversight of Risk and Strategy
 - Governance Structures

Governance Initiatives (*cont'd*)

- Blackrock Investment Stewardship Engagement Priorities for 2018
 - Governance
 - Corporate Strategy
 - Compensation
 - Climate Risk Disclosure
 - Human Capital
- Blackrock Voting Guidelines –
<https://blackrock.com/corporate/literature/fact-sheet/blk-responsible-investment-guidelines-us.pdf>

Governance Initiatives (*cont'd*)

- Others
 - State Street Global Advisors
 - CalPERS Governance & Sustainability Principles
 - CALSTRS
 - Corporate Governance Principles
 - Investment Policy for Mitigating Environmental, Social and Governance Risks
 - Best Practices in Board Composition

Governance Initiatives (*cont'd*)

- Investor Stewardship Group
 - Corporate Governance Principles for US-listed companies
 - Members are 50 US and international institutional investors with over \$22 trillion invested in US markets
- Commonsense Principles 2.0
 - Corporate governance principles for public companies, their boards of directors and their institutional shareholders
 - 21 CEOs and investors

Potential Proxy Advisor Regulatory Changes

- Corporate Governance Reform and Transparency Act of 2017
 - Would amend Section 3(a) of the Exchange Act to create requirements that foster accountability, transparency, responsiveness and competition in the proxy advisory firm industry
- SEC roundtable on proxy process
 - In anticipation of the roundtable, the Division of Investment Management withdrew two no-action letters that addressed proxy advisory firm conflict procedures in the context of investment advisers' proxy voting responsibilities
- Staff Legal Bulletin No. 20
 - Still in effect; covers some of the same items as the withdrawn no-action letters

Trend in Proxy Statement Disclosure

- Use as another means of shareholder engagement, rather than simply a disclosure document
 - Letter from the Board
 - Board oversight function, particularly in areas of ESG and cybersecurity
 - Summaries
 - Executive summary
 - Compensation
 - Issues raised in shareholder outreach

Trend in Proxy Statement Disclosure (*cont'd*)

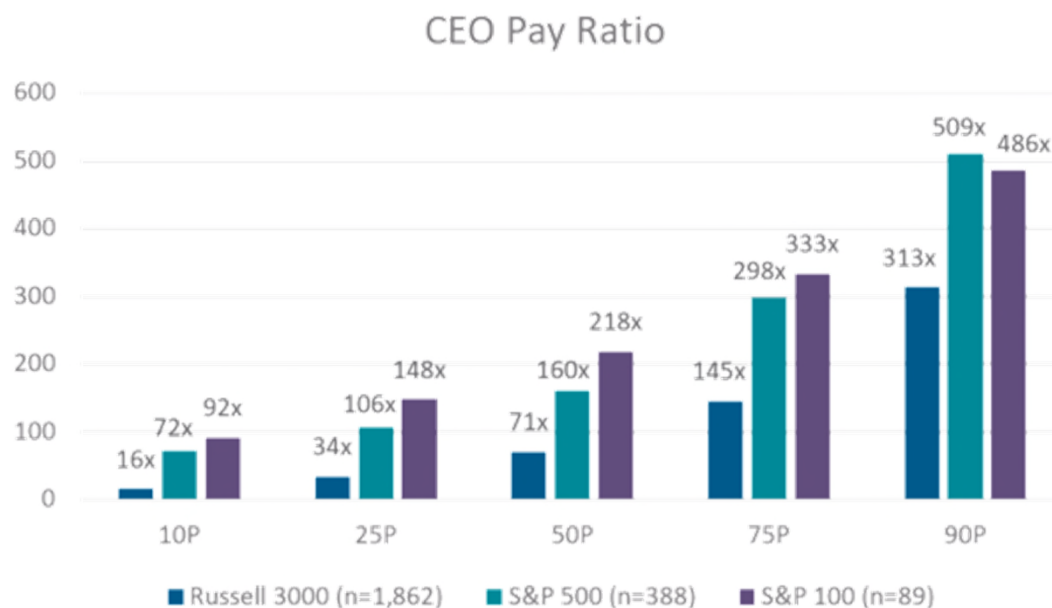
- Convey information in easy-to-read fashion
 - Use plain English
 - Use graphs, charts and other means of presentation
 - Think of areas where textual information may bury the message
 - Director skills
 - Compensation components
 - Operating metrics
- Expanded Audit Committee disclosures

Pay Ratio Disclosure: 2018 Pay Ratio Results

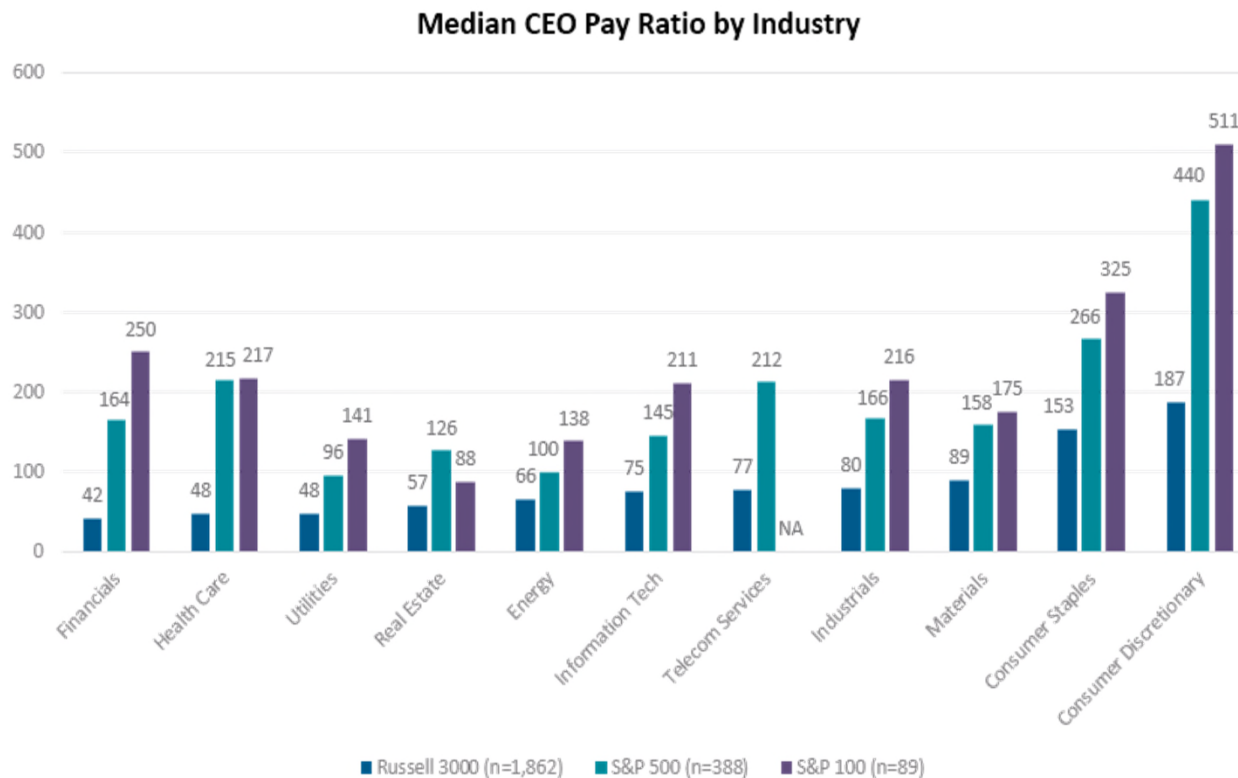
- CEO Pay Ratio ranged from 0x to over 5,000x

- Median Pay Ratio¹

- Russell 3000 = 71x
- S&P 500 = 160x
- S&P 100 = 218x



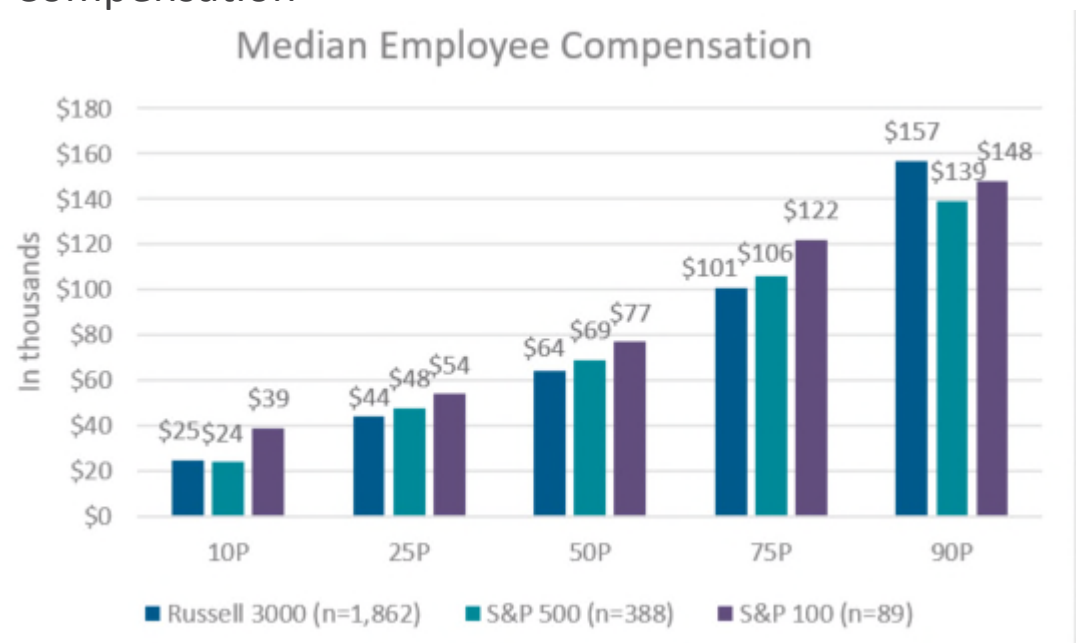
Pay Ratio Disclosure: 2018 Pay Ratio Results



Pay Ratio Disclosure: 2018 Median Employee Compensation Results

- Approximate Median Employee Compensation¹

- Russell 3000 = \$64,000
- S&P 500 = \$69,000
- S&P 100 = \$77,000




1. S&P 100 data source: Mayer Brown data and analysis through September 30, 2018.

Other source: Semler Brossy 2018 Say on Pay and Proxy Results through June 26, 2018. Excludes companies with no employees, no CEO or CEOs with no compensation.

Pay Ratio Disclosure: Overview

- How and where is the pay ratio disclosed?
 - Generally in narrative form, some companies use tables to highlight main computations

Category	2017 Total Compensation and Ratio
Annual total compensation of Mr. Connor (A)	\$6,200,313
Median employee total compensation (excluding Mr. Connor) (B)	
Ratio of A to B	57:1

Pay Ratio

Following is a reasonable estimate, prepared under applicable SEC rules, of the ratio of the annual total compensation of our CEO to the median of the annual total compensation of our other staff members, calculated in accordance with the requirements of Item 402(c)(2)(x) of Regulation S-K. The Company determined our median employee based on total direct compensation paid to all of our staff members worldwide (consisting of approximately 20,600 individuals) recorded in our global systems as of November 1, 2017. Total direct compensation included base salary (wages earned based on our payroll records), annual cash incentive awards earned for the period (and target sales incentive awards for our sales force), and the

annual grant value of long-term incentive, or LTI, equity awards during 2017. Earnings of our staff members outside of the U.S. were converted to U.S. dollars using the currency exchange rate as of November 1, 2017. No cost-of-living adjustments were made. We then determined the annual total compensation of our median employee for 2017 which was \$132,930. As disclosed in the "Summary Compensation Table" appearing on page 64, our CEO's annual total compensation for 2017 was \$16,899,789. Based on the foregoing, the ratio of the annual total compensation of our CEO to that of the median staff member was 127 to 1.

- Almost always just after change in control payment disclosure and/or equity comp plan table

Pay Ratio Disclosure: Supplemental Pay Ratios

- Supplemental Pay Ratios

- Used by approximately 10% of all filers¹



1. Source: Pearl Meyer Research Report. Data through mid-April 2018.

Pay Ratio Disclosure: Supplemental Pay Ratios (cont'd)

- Supplemental Pay Ratios – to show a lower CEO pay ratio:

For the fiscal year ended June 30, 2018, the annual total compensation of the Chief Executive Officer was \$50,263,861 and the annual total compensation of the median employee of the Company was \$67,809, which resulted in a ratio of 741 to 1. While the CEO pay ratio is intended to provide greater transparency to annual CEO pay and how it compares to the pay of the median employee, a substantial portion of our CEO's annual total compensation for fiscal 2018 reported in the Summary Compensation Table reflects the value of an award and adjustment related to the Transaction and is not comparable to prior year compensation. As a result, this ratio includes the grant date fair value of \$27,005,170 for the Retention RSUs awarded in February 2018 to Mr. J.R. Murdoch (along with the other named executive officers and certain senior executives) as well as the incremental accounting expense associated with the modification of the fiscal 2016-2018 PSU Award. As described in the Compensation Discussion and Analysis, recipients of the Retention RSUs will not be eligible to receive a PSU Award for the fiscal 2019-2021 performance period. If the Retention RSUs and impact of the modification of the 2016-2018 PSU Award were excluded from Mr. J.R. Murdoch's compensation as reported in the Summary Compensation Table of this proxy statement, the ratio would be 343 to 1. We believe that this supplemental ratio reflects a more representative comparison.



2018 Proxy Statement

We understand that the CEO pay ratio is intended to provide greater transparency to annual CEO pay and how it compares to the pay of the median employee. As such, we are providing a supplemental ratio that compares the CEO's regular annual pay, excluding the **special one-time performance-based incentive award** (see "[Special Equity Awards](#)" section), to the pay of the median-paid employee as we believe that this supplemental ratio reflects a more representative comparison. The resulting supplemental CEO pay ratio is 223:1

Annual Total Compensation


Ian Read	\$19,913,773
Median Employee	\$89,206(1)
Supplemental Ratio	223:1

(1) Cash compensation of \$71,187 + all other compensation of \$18,019.

Pay Ratio Disclosure: Supplemental Pay Ratios (cont'd)

- Supplemental Pay Ratios – to show a higher CEO pay ratio:

Note that in 2017 and prior years, a portion of Mr. Merlo's performance-based long-term incentive compensation was cash-denominated at grant and thus not included in the SCT until after the vesting period when the value earned had been determined, per SEC reporting requirements. However, beginning in 2018, this portion of Mr. Merlo's compensation will be denominated in shares and thus will be included the SCT in the year of grant. As shown above in a supplemental table on page 37 in the CD&A, Mr. Merlo's 2017 annual compensation in the SCT would have been \$5,760,000 higher had we historically been denominating this compensation in shares, and the resulting ratio for Mr. Merlo's annual compensation to that of our median employee would have been 470-to-1.

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We also determined to present an alternative pay ratio. Because our CEO received a one-time grant of performance-based equity in 2016 that was intended to cover the 2016 through 2018 performance period, he did not and will not receive a long-term equity award in 2017 or in 2018. We believe the absence of any long-term equity compensation as part of his compensation for 2017 would appear to understate the equity compensation value that he otherwise would have earned for his 2017 performance. Thus, to better reflect his true pay in 2017, **we apportioned an annualized amount of the 2016 grant to 2017 total compensation**, which would have resulted in a more representative CEO pay to median employee pay ratio of 196:1.

Pay Ratio Disclosure: The Median Employee (*cont'd*)

- “Employee” is an individual employed by the company or any of its consolidated subsidiaries:
 - US employees
 - Non-US employees *with two exceptions*
 - *Data privacy exception*
 - *de minimis exception*
 - Full-time, part-time, seasonal or temporary employees
 - NOT independent contractors or “leased” workers, unless the company determines their compensation
- Median employee can be determined on any day within the last three months of the fiscal year

Pay Ratio Disclosure: Supplemental Pay Ratios (cont'd)

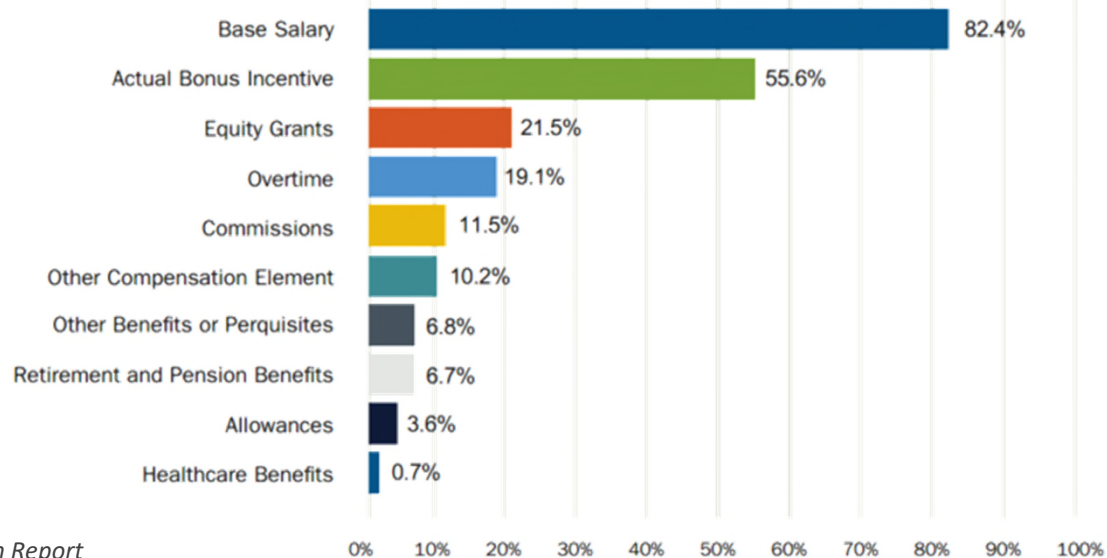
- Identify the “median employee” using a method based on the company’s own facts and circumstances
 - May identify the median employee based on total compensation of the full employee population or may use a statistical sample or another reasonable method
 - Companies generally using the full employee population
 - Some statistical sampling used – 2% of all filers¹ and 13% of S&P 100²

1. Source: Pearl Meyer Research Report.

2. Source: Mayer Brown data and analysis through September 30, 2018. ²⁰

Pay Ratio Disclosure: The Median Employee (cont'd)

- Identify the “median employee” using a method based on the company’s own facts and circumstances
 - Based on any Consistently Applied Compensation Measure (CACM)



1. Source: Pearl Meyer Research Report

Pay Ratio Disclosure: Non-US Employee Data Privacy Exception

- May exclude employees in jurisdictions with data privacy laws that make the company unable to comply with the rule without violating those laws
- The company must exercise reasonable efforts to comply with the disclosure requirements including, at a minimum:
 - Seeking or using an exemption from compliance with the data privacy law, and obtaining a legal opinion if no exemption granted (include as an exhibit)
- If the company uses an exception:
 - It must list excluded jurisdictions and the approximate number of employees excluded, identify the specific data privacy law, exclude all non-US employees in the jurisdiction, explain how complying with the rule violates such law and disclose the company's efforts to seek or use an exemption
- No companies have taken advantage of this exception¹

1. Source: Pearl Meyer Research Report and Mayer Brown data and analysis.

Pay Ratio Disclosure: Non-US Employee *de minimis* Exception

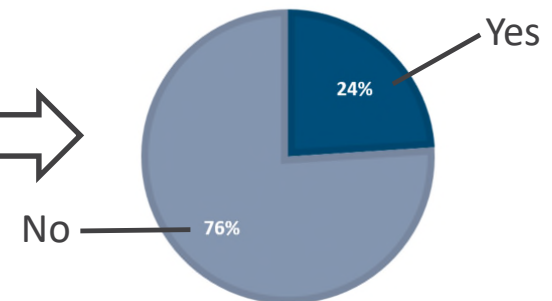
- If a company's non-US employees equal 5% or less of the company's total employees, the company may exclude **all** non-US employees
- **or**
- If a company's non-US employees exceed 5% of the company's total employees, the company may exclude **up to 5%** of its total employees who are non-US employees
- A company using the *de minimis* exception must disclose:
 - The jurisdiction(s) involved, approximate number of employees excluded in each jurisdiction, total number of US and non-US employees irrespective of the exception (*de minimis* or data privacy), and total number of US and non-US employees used for the *de minimis* calculation
- Employees excluded pursuant to the data privacy exception count toward the 5% *de minimis* exception

Pay Ratio Disclosure: Non-US Employee *de minimis* Exception (*cont'd*)

- Approximately 1/4 of all filers used this exemption¹



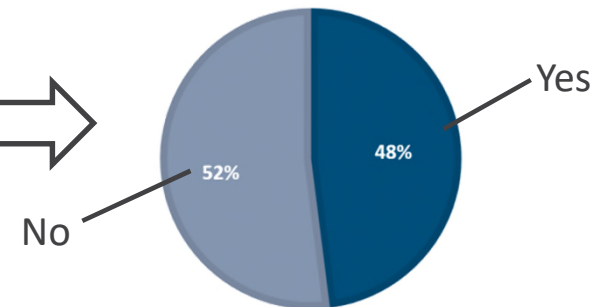
All filers through June 30, 2018



- Approximately 1/2 of the S&P 100 used this exemption²



S&P 100 through September 30, 2018



1. Source: Pearl Meyer Research Report and Mayer Brown data and analysis.

2. Source: Mayer Brown data and analysis.

Pay Ratio Disclosure: Non-US Employee *de minimis* Exception (*cont'd*)

Non-U.S. Employee Country Exclusions

Country	Headcount	Country	Headcount	Country	Headcount	Country	Headcount
Ecuador	442	Cameroon	55	Chile	17	Ukraine	4
Azerbaijan	417	Panama	51	Spain	14	Hungary	3
Kazakhstan	378	Poland	48	Belgium	11	Kenya	3
Congo	158	Romania	46	Philippines	11	Uganda	3
Germany	113	France	35	Mozambique	10	Switzerland	2
Italy	113	Papua New Guinea	31	Turkmenistan	7	Equatorial Guinea	2
Netherlands	110	Bangladesh	28	Tanzania	7	Turkey	2
Bolivia	109	Denmark	27	Austria	6	South Africa	2
Trinidad & Tobago	84	Peru	23	Cyprus	6	Albania	1
Ghana	64	Suriname	23	Israel	5	Bulgaria	1
New Zealand	59	Cote d'Ivoire	21	South Korea	4	Gabon	1
Vietnam	57	Japan	19	Myanmar	4		

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Employee Population. We identified the median employee from Occidental's employee population as of October 1, 2017. After excluding employees under the "de minimis exemption" (as described below), Occidental's employee population consisted of 6,960 employees located in the U.S.; 557 in Colombia; 2,647 in Oman; and 466 in Qatar. For purposes of identifying the median employee, Occidental was permitted to exclude up to 5% of its total employees who are non-U.S. employees. Occidental relied on this exemption to exclude the employee populations of the following jurisdictions, which collectively accounted for less than 5% of Occidental's total employee population of 10,978 as of October 1, 2017: Abu Dhabi (64); Belgium (2); Bolivia (65); Brazil (1); Canada (88); Chile (111); Hong Kong (4); Japan (2); Libya (1); Mexico (3); The Netherlands (1); and Singapore (6).

Pay Ratio Disclosure: Practical Considerations

- *Liability*
- *Reception by employees, investors and press*
- *Comparison of ratio year over year*
- *Recognition of pay equality as a political issue*
- *SEC comment letters*
- *Tax legislation tied to SEC pay ratio disclosure*

Hedging Disclosure Proposal

- Hedging rule was proposed in 2015 pursuant to Dodd-Frank
- While in the final rulemaking process, not clear whether the final rule will be approved and become effective in time for 2019 proxy season
- When the final rule is issued, it may be advisable to:
 - Amend hedging policies
 - Revise D&O questionnaires
- The proposed rule would require companies to disclose whether they permit employees and directors to hedge the company's securities. Many companies already discuss hedging policies in their CD&A

Clawback Proposal

- Section 954 of the Dodd-Frank Act
- SEC proposed rules on July 1, 2015
- Comment period ended on September 14, 2015
- The proposal directs the stock exchanges to establish listing standards that prohibit the listing of any security of a company that does not adopt and implement a written policy requiring the recovery of certain incentive-based executive compensation
- Private ordering resulting from concerns of proxy advisory firms

Pay-for-Performance Proposal

- Section 953(a) of the Dodd-Frank Act
- SEC proposed rules on April 29, 2015
- Comment period ended on July 6, 2015
- The proposed rule would require companies to include a new table in their proxy statements showing the relationship between compensation actually paid and performance, with performance measured both by company TSR and peer group TSR

SAY-ON-PAY

2018 Say-On-Pay Results ^{1/}

Of the 2,548 companies that held Say-On-Pay Votes – 60 companies (2.4%) failed

- Average “Against” vote – 61% / with Media of 58%
- 17 companies with failed votes in previous years (13 were in 2017)
- 34 companies had negative 1-year total shareholder returns

^{1/} Steven Hall Partners – “Companies that Failed Say-on-Pay 2018”

CD&A – Preparation Items to Consider

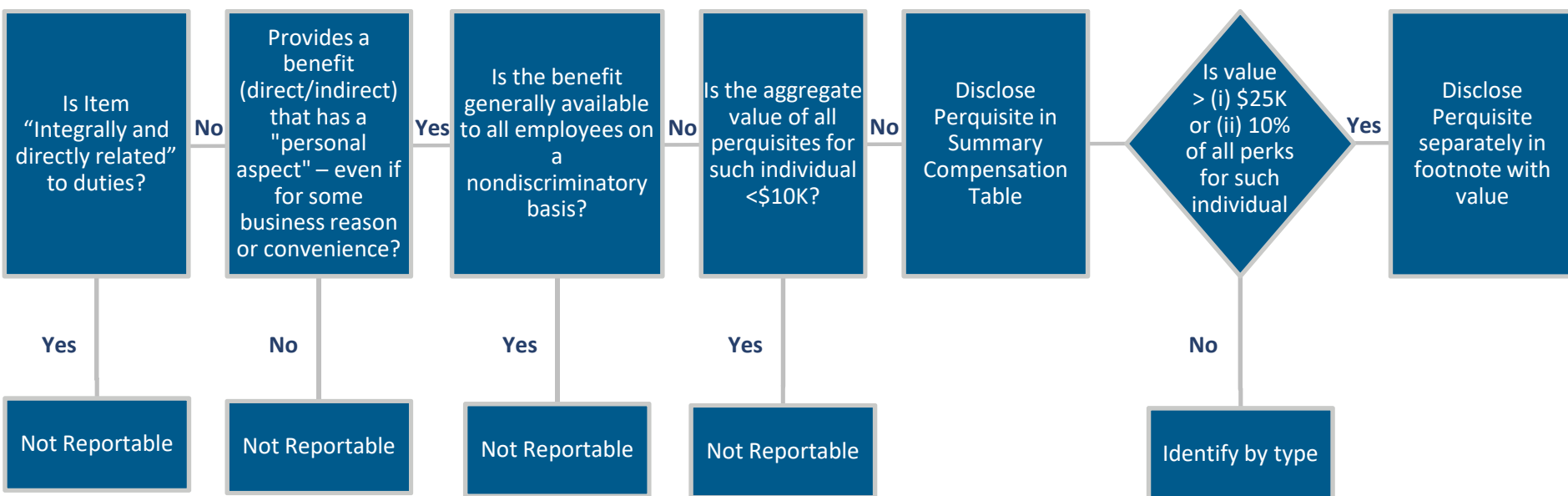
- Provide rationale for how the compensation program ties to and supports shareholder value and strategic goals;
- Highlight any improvements made, in response to feedback or otherwise;
- Discuss any “hot buttons” directly and how they support shareholder value; and
- If appropriate, set forth a quantitative analysis of historical pay-versus-performance.

PERQUISITE DISCLOSURE/ ENFORCEMENT

Potential Items That Could Constitute Perquisites

- Personal use of company airplane;
- Club memberships (unless used solely for company-related purposes);
- Automobile allowances;
- Tax gross-ups;
- Tax and financial planning services;
- Personal/home security services;
- Use of company residences;
- Welfare benefit premiums (e.g., medical, life insurance, disability);
- Discounts on company products or services;
- Home office expenses;
- Moving expenses for new executives; and
- Parking expenses.

What is a Perquisite and What Must be Disclosed?



VIRTUAL MEETINGS

Virtual Meetings Under State Laws

Virtual-Only allowed in 30 states, including:

- Delaware;
- Texas;
- Minnesota;
- Ohio; and
- Pennsylvania

Hybrid (participation via Internet in a physical meeting) allowed in 42 states, including:

- New Jersey; and
- Connecticut

Virtual-Only are precluded in nine states, including:

- New York;
- Georgia; and
- Idaho

Advantages and Disadvantages of Virtual-Only Meetings

Advantages:

- Potential to increase shareholder participation;
- Enhance “retail participation” by allowing online voting during the meeting;
- Reduce environmental impact by lowering carbon footprint of travel by board, management and shareholders;
- Save company money – travel, facility, security, etc.; and
- Save shareholder money – travel and possibly lodging.

Advantages and Disadvantages of Virtual-Only Meetings (*cont'd*)

Disadvantages:

- Limits shareholder in-person interaction with the company's executive and board;
- Ability of company to avoid certain questions;
- Shareholder discomfort using technology; and
- May not allow ample discussion of contentious proposals.

“Principles and Best Practices for Virtual Shareholder Meeting”^{2/}

1. Ensure equal access to raise and discuss concerns;
2. Ensure access visual and via voice to directors;
3. Ensure scalable technology and technical support during the meeting;
4. Publish clear format rules of conduct – e.g., order of question better in-person and virtually, as well as establishing limits for questions and how questions received on-line will be posted, answered and available on the company’s website;
5. Ensure adequate archival of the virtual component for future viewing; and
6. Solicit feedback post-meeting.

^{2/} The Best Practice Committee for Shareholder Participation in Virtual Annual Meetings. April 2018

What Should Directors Ask About Virtual Meetings?

- Allowed by state law?
- Advantages and disadvantages for this company?
- What are the cost savings?
- Do we know what our most significant shareholders think about a virtual-only or hybrid meeting?
- What guidelines will be adopted for the conduct of the meeting? – handling questions received remotely, and before the meeting.
- Is our technology adequate, reliable and sealable?
- Have we/will we conduct a practice run?

PROXY C&DIs

SEC's 2018 Update of C&DIs re Proxy Rules and Schedule 14A/14C

The six “substantive changes” to *Manual of Publicly Available Telephone Interpretations*:

- 1. Corporate Name Changes** [C&DI 126.02]: Corporate name change added to list of proposals excluded from requiring the filing of preliminary proxy materials.
- 2. Omitting “O” Benefit Persons from New Plan Benefits Table** [C&DI 161.03]: Permits omission of a person with no benefits from the table so long as the information is set forth in the narrative disclosure.
- 3. Note A Disclosure of Additional Securities** [C&DI 151.01]: Absent cash proceeds from common stock issuance being authorized by shareholders expected to be used to fund a material portion of an acquisition, the certain acquisition-related information under Note A of Schedule 14A in a proxy will not be required IF the company can otherwise fully finance the acquisition.

SEC's 2018 Update of C&DIs re Proxy Rules and Schedule 14A/14C (*cont'd*)

- 4. Schedule 14A Item 13 Financials and Elimination of Preemptive Right [C&DI 163.01]:** Elimination of preemptive rights alone would require the financial and other information “to the extent required by Item 13 of Schedule 14A.” No language re “tantamount to the creation of a new security.”
- 5. Discretionary Authority for Cumulative Voting [C&DI 124.01]:** In an election for directors with cumulative voting allowed, a proxy holder may cumulate votes among nominees so long as it indicates that it may do so on the proxy and in bold-faced type.
- 6. Preliminary Proxy Statement for Non-Rule 14a-8 Matters [C&DI 124.07]:** A company that does not have discretionary authority over a non-Rule 14a8 matter (e.g., if a shareholder proponent timely informs the company that it intends to deliver its own proxy statement), then notwithstanding previous SEC guidance, the company must file preliminary proxy materials.

Shareholder Proposals

- Shareholders may submit a proposal for inclusion in a company's proxy statement for voting at annual meeting
- SEC rules specify procedural and substantive bases for exclusion of proposals
 - Companies may submit no-action requests to the SEC if any grounds for exclusion
 - Check incoming no-action requests: <https://www.sec.gov/divisions/corpfin/cf-noaction/14a-8-incoming.shtml>
- Negotiations with proponent sometimes lead to withdrawal
- Company may include a statement of opposition

Staff Legal Bulletin 14I

- SLB 14I issued in November 2017 addressed four topics:
 - Ordinary business exclusion under Rule 14a-8(i)(7)
 - Exception for policy issue that is sufficiently significant
 - Economic relevance exclusion under Rule 14a-8(i)(5)
 - Less than 5% of total assets, net earnings and gross sales
 - Unless otherwise significantly related to company
 - Proposal by proxy
 - The impact of graphs and images on 500-word limit

Board Analysis for No-Action Requests

- SLB 14I suggested no-action requests under 14a-8(i)(7) could include board analysis of significance of policy issue
- SLB 14I suggested no-action requests under 14a-8(i)(5) could include board analysis of significance to company's business
- SLB 14I phrased the board analysis as an expectation
- Later staff statements clarified board analysis was optional

Rule 14a-8(i)(7) and (i)(5) No-Action Letters 2018

- No-action requests containing board analyses not automatically granted
 - No-action requests rejected if staff found board analysis did not have sufficient level of detail
 - No-action requests rejected where substantial votes cast in support of similar proposals in prior years
- Staff granted no-action requests without board analyses
- Extent to which a board analysis influenced favorable outcome not necessarily clear from no-action letters

Staff Legal Bulletin 14J

- SLB 14J issued October 23, 2018 addressed three topics:
 - Additional guidance on board analyses for Rule 14a-8(i)(5) or Rule 14a-8(i)(7) no-action requests
 - Scope and application of micromanagement under 14a-8(i)(7)
 - Scope and application of Rule 14a-8(i)(7) for proposals touching on senior executive and/or director compensation matters

SLB 14J—Sufficient Detail for Board Analysis

- How proposal relates to core business activities
- Quantitative data, including financial statement impact, illustrating significance of matter to the company
- Whether company already addressed issue in some manner
 - Analysis of whether company’s differences in approach from proposal present a significant policy issue for the company

SLB 14J—Sufficient Detail for Board Analysis (*cont'd*)

- Extent of company shareholder engagement on the issue
 - Level of shareholder interest expressed through engagement
- Whether anyone other than the proponent has requested the type of action or information sought by the proposal
- Whether the company's shareholders previously voted on the matter
 - Board's views as to the related voting results

Should Board Analyses be Included?

- SLB 14J states board analyses help evaluation of requests
- Consider what a board analysis can contribute and other demands on the board's time
 - Facts about business SEC staff may not know
 - Strength of arguments for exclusion without board analysis
 - Level of recent favorable vote on similar proposal
- If used, provide sufficient details specific to the company
 - Have board consider factors along the lines outlined in SLB 14J

Other SLB 14J Rule 14a-8(i)(7) Topics

- Micromanagement

- Degree to which proposal seeks to micromanage
- Framework applies to proposals for intricately detailed reports

- Senior Executive and/or Director Compensation

- Excludable if focused on ordinary business, even if senior executive/director compensation raised
- Excludable if targeted aspect of compensation is broadly available or applicable to general workforce and company demonstrates that executive/director eligibility not significant
- Excludable if seeking to micromanage senior executive/director compensation

Proxy Access

- Proxy Access at more than 2/3 of S&P 500
- Market standard
 - 3% for 3 years
 - Aggregate up to 20 shareholders
 - Limit of 20% of board (often with minimum of 2 nominees)
- “Fix-It” Proposals
 - Included in proxy statements but not receiving majority support

Special Meetings

- Rise in number of proposals on threshold for shareholders to call special meeting
- No-action letters permitting exclusion where company proposal sought shareholder ratification of higher threshold in existing by-laws

ESG Proposals

- Major category of shareholder proposals
- Growing support for ESG proposals
 - Environmental: climate change and sustainability
 - Social: political activity, human rights, pay equity and opioid crisis
 - Other governance: shareholder consents, independent chair and board diversity
- ESG metrics for compensation proposals

Examples of Proposals Receiving Majority Approval

• Environmental

- Global warming
- Sustainability
- Methane emissions
- Greenhouse gas emissions
- Coal

• Governance

- Written consent
- Board declassification
- Supermajority voting
- Special meetings
- Proxy access adoption
- Majority voting

• Social

- Firearms
- Opioid abuse

(Source: Alliance Advisors June 2018 newsletter)

Notice of Exempt Solicitations

- In 2018, individual investors filed voluntary notices of exempt solicitations
 - Filed pursuant to Rule 14a-6(g) and Rule 14a-103
 - Very little cost to the individual filer
 - No word limit
- These notices appear on appear on a company's EDGAR page identified as a "PX14A6G" filing type
- CD&Is 126.06 and 126.07 permit this practice and specify requirements for cover information

SEC FOCUS ON CYBERSECURITY

Cybersecurity Guidance

- The Staff published guidance on cybersecurity in 2011, CF Disclosure Guidance: Topic No. 2, Cybersecurity
- In February 2018, the Commission published an interpretive release
 - The release reaffirms the prior guidance
 - A registrant should consider disclosures in:
 - Risk Factors
 - Management’s Discussion and Analysis (MD&A)
 - Business (regulatory and legal proceedings)
 - Financial statements
- Registrants should consider whether cybersecurity risks are material
 - Materiality of risks may depend on company’s industry sector and business model, the harm that a breach may have on company’s reputation, effect on financial performance, risk of regulatory investigations, litigation risk, customer and vendor relationships, and reputational risk

Cybersecurity Guidance *(cont'd)*

- How does management and the board manage the risks?
- Tailored disclosures, not generic disclosures
 - Disclosures should reference actual breaches to the extent these have occurred

Sample SEC Comment

We note your disclosure that you continue to face a host of cyber threats; your disclosure that cyber-crimes and denial of service attacks have increased; and your identification of cyber-attacks as a key risk. Please clarify whether you have knowledge of the occurrence of any such attacks in the past. If attacks have occurred, and were material either individually or in the aggregate, revise to discuss the related costs and consequences. Also, describe the particular aspects of your business and operations that give rise to material cybersecurity risks and the potential costs and other consequences of such risks to those businesses and operations. For additional guidance, please refer to CF Disclosure Guidance Topic No. 2 on Cybersecurity.

Cybersecurity Guidance *(cont'd)*

- When does a duty to update or correct arise?
- What are the triggers for a disclosure?
 - Are there specific regulations requiring disclosure of a breach even while a company is still investigating and assessing?
- MD&A disclosures should address financial consequences such as:
 - Loss of customer relationships
 - Costs related to remedial efforts
 - Costs associated with investigations
 - Loss contingencies

Sample SEC Comment

With respect to the cyber-security incident and related assessments and litigation, please tell us your consideration of the requirement in ASC 450-20-50-4.b. to disclose an estimate of the possible loss or range of loss or to disclose that such an estimate cannot be made.

Cybersecurity Guidance *(cont'd)*

- The Commission has focused on enforcement in connection with cybersecurity
 - Failure to adequately disclose a cybersecurity breach
 - Risk factors that were generic and spoke to future or possible risks were misleading given an actual breach had occurred
 - MD&A discussion omitted disclosures relating to consequences of breach
 - Failure of disclosure controls and procedures
 - Insider trading – trading while in possession of material non-public information regarding a cybersecurity incident
 - Boards and audit committees should consider disclosure controls and procedures, duties to disclose, and the application of Regulation FD

Report of Investigation Pursuant to Exchange Act Section 21(a)

- Earlier this month, the Division of Enforcement released its Report of Investigation that detailed the Division's review of nine public issuers that were victims of cyber-related frauds
- At issue was whether the issuers complied with Sections 13(b)(2)(B)(i) and (iii) of the Exchange Act requiring public companies to implement and maintain a system of internal accounting controls sufficient to provide reasonable assurance that transactions are executed with, or that access to company assets is permitted only with, management's general or specific authorization

Policies and Procedures

- Year-end provides an opportunity for management, the board and the audit and/or risk committees to review and consider the company's
 - Disclosure controls and procedures
 - Internal accounting controls
 - Cybersecurity policies and procedures, including the company's
 - Risks and controls
 - Cybersecurity expertise
 - Management and board oversight approach
 - Awareness and training programs
 - Communications policy (Regulation FD and blackout/insider trading policy)
 - Incident response plan

ANNUAL REPORT DISCLOSURE CONSIDERATIONS

Disclosure Considerations

- As many studies have shown, the overall number of SEC reviews with comment letters has declined. That being said, a review of recent SEC comment letters, SEC Staff guidance and statements from SEC Staff provide a roadmap to guide Form 10-K preparers
- We will highlight some areas of focus, especially as these relate to the Risk Factors and MD&A sections

Risk Factors

- ***Cybersecurity and cyberbreaches***: as discussed earlier, the Staff has emphasized the importance of tailored (rather than generic) risks that reflect a company's actual experiences, including the occurrence of breaches, as well as related investigations, litigation and costs
- ***Brexit disclosures***: depending on the company's industry and its geographic reach, it may be appropriate to consider disclosing risks associated with Brexit, such as regulatory approvals and licenses, costs associated with redomiciling, costs associated with moving headquarters and staff, etc.
- ***Tariff disclosures***: again, depending upon the company's industry, tariff-related risk factors addressing increased costs, other impacts on revenues, demand for products, etc. may be appropriate

M&D Disclosures

- ***Non-GAAP financial measures***: while the focus on the use of non-GAAP financial measures may have died down, companies should continue to review filings for the use of any non-GAAP liquidity measures or “tailored” measures of performance
- ***Revenue recognition***: SEC Staff comments issued to early adopters have provided useful insights. Companies will want to review their prior disclosures and provide additional detail regarding: areas that involved judgment; performance obligations embedded in contracts; payment terms; amortization of capitalized contract costs; etc.
- ***Known trends***: Staff comments continue to request more detailed discussion of the factors that may impact revenues, for example, as well as more insight regarding future financial condition and results of operation. Depending on the company, a discussion of some of the topics we addressed earlier (cyber, tariffs, etc.) may have an effect on the company’s prospects

M&D Disclosures *(cont'd)*

- ***Tax reform***: SEC Accounting Bulletin (SAB) 118 provided companies with up to one year to analyze the tax effects of the Tax Cuts and Jobs Act. This 10-K season, the Staff will expect to see additional disclosures
- ***Loss contingencies***: This has been a frequent area of Staff comment but the Staff's concerns related to cyberbreach-related remediation and litigation costs may now make this a priority

DISCLOSURE UPDATE AND SIMPLIFICATION AMENDMENTS

Disclosure Update and Simplification

- The Commission's Disclosure Update and Simplification Amendments become effective in early November and will affect the Form 10-K (or Form 20-F). Below is a summary:
 - The Form 10-K cover page
 - Business – R&D investments no longer required to be detailed
 - Business – certain segment information no longer required
 - Business – financial information by geographic area is longer required
 - Reference to SEC public reference room deleted
 - Mandated disclosure of company website
 - Part II – eliminating market price disclosures
 - Part II – eliminating dividend information
 - Certain technical Item 302 changes

OTHER ACCOUNTING DEVELOPMENTS

Accounting Matters

- Lease accounting: as the effective date approaches, audit committees should be briefed on the impacts of adoption of the new leases standard
- Critical Audit Matters (CAMs): audit committees will want to discuss CAM reporting with the auditors and begin the planning process

QUESTIONS?

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