

Boardroom Blitz: Helping Your Directors Deal with Incoming Hot Issues

Peter Carter	Delta Air Lines, Inc. Executive Vice President, Chief Legal Officer and Corporate Secretary Atlanta, Georgia
Trevor Gunderson	General Mills, Inc. Vice President, Deputy General Counsel Golden Valley, Minnesota
Cam Hoang	Dorsey & Whitney LLP Partner Minneapolis, Minnesota hoang.cam@dorsey.com (612) 492-6109
Robert Rosenbaum	Dorsey & Whitney LLP Partner Minneapolis, Minnesota rosenbaum.robert@dorsey.com (612) 340-5681

Handouts

1. PowerPoint Presentation

Resources available on Dorsey.com

Dorsey Webinar Playback: *Shareholder Proposals: Strategies and Tactics* (September 26, 2019)

Link: <https://www.dorsey.com/newsresources/events/videos/2019/09/dorsey-webinar-shareholder-proposals-2019>

Dorsey & Whitney LLP eUpdate: *Observations and Recommendations on the SEC's Recent Process Changes for Excluding Shareholder Proposals* (September 17, 2019)

Link: <https://www.dorsey.com/newsresources/publications/client-alerts/2019/09/secs-recent-process-changes-shareholder-proposals>

Dorsey & Whitney LLP eUpdate: *SEC Adopts Guidance Impacting Voting Recommendations from Proxy Advisory Firms* (August 26, 2019)

Link: <https://www.dorsey.com/newsresources/publications/client-alerts/2019/08/sec-adopts-guidance-voting-recommendations>

Dorsey & Whitney LLP eUpdate: *SEC Proposes to Modernize Disclosures of Business, Legal Proceedings, and Risk Factors* (August 9, 2019)

Link: <https://www.dorsey.com/newsresources/publications/client-alerts/2019/08/sec-proposes-to-modernize-disclosures-of-business>

Materials are Available on www.dorsey.com at

<https://www.dorsey.com/newsresources/events/event/2019/11/corporate-counsel-symposium-2019-materials>

Dorsey & Whitney LLP eUpdate: *2019 Delaware Entity Statutory Amendments* (August 5, 2019)

Link: <https://www.dorsey.com/newsresources/publications/client-alerts/2019/08/2019-delaware-entity-statutory-amendments>

Dorsey & Whitney LLP eUpdate: *SEC Staff Publishes Statement on Risks of Transition Away from LIBOR* (July 31, 2019)

Link: <https://www.dorsey.com/newsresources/publications/client-alerts/2019/07/risks-of-transition-away-from-libor>

Dorsey & Whitney LLP eUpdate: *What the LIBOR Phase-out Means for Debt Capital Market Participants* (April 30, 2019)

Link: <https://www.dorsey.com/newsresources/publications/client-alerts/2019/04/the-libor-phase-out>

Dorsey & Whitney LLP eUpdate: *SEC Announces New Streamlined Procedure for the Extension of Confidential Treatment* (April 18, 2019)

Link: <https://www.dorsey.com/newsresources/publications/client-alerts/2019/04/sec-announces-new-streamlined-procedure>

Dorsey & Whitney LLP eUpdate: *Summary of SEC's FAST Act Amendments and Additional Guidance on Confidential Treatment Requests* (April 11, 2019)

Link: <https://www.dorsey.com/newsresources/publications/client-alerts/2019/04/sec-fast-act-amendments>

Dorsey & Whitney LLP eUpdate: *Delaware Supreme Court Orders Company To Turn Over Emails To Stockholder In Response To Books And Records Request* (February 21, 2019)

Link: <https://www.dorsey.com/newsresources/publications/client-alerts/2019/02/de-supreme-court-orders-company-turn-over-emails>

Dorsey & Whitney LLP eUpdate: *D&O Insurance and the Two Words to Fear: Capacity Exclusion* (February 5, 2019)

Link: <https://www.dorsey.com/newsresources/publications/client-alerts/2019/02/do-insurance-and-capacity-exclusion>

Dorsey & Whitney LLP eUpdate: *Understanding the SEC's New Mining Disclosure Rules: Questions and Answers* (February 5, 2019)

Link: <https://www.dorsey.com/newsresources/publications/client-alerts/2019/02/new-mining-disclosure-rules-2019>

Dorsey Blogs

Governance & Compliance Insider at <https://governancecomplianceinsider.com/> tracks the latest developments, trends and best practices in compliance, corporate governance, and disclosure.

Boardroom Blitz: Helping Your Directors Deal with Incoming Hot Issues

Peter Carter, Executive Vice President, Chief Legal Officer and Corporate Secretary, Delta Air Lines, Inc.

Trevor Gunderson, Vice President, Deputy General Counsel, General Mills, Inc.

Robert Rosenbaum and Cam Hoang, Dorsey & Whitney LLP

Wednesday, November 6, 2019

1

Agenda

- **Corporate Citizenship**
- **CEO Activism**
- **Traversing the Risk and Compliance Landscape**
- **Diverse and Effective Boards**

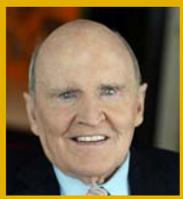
2

Corporate Citizenship

The primacy of shareholder interests, and whether corporations have social responsibilities that may conflict with shareholder interests, are long-standing debates:



“...there is one and only one social responsibility of business--to use its resources and engage in activities designed to increase its profits so long as it stays within the rules of the game, which is to say, engages in open and free competition without deception or fraud.” Milton Friedman in *Capitalism and Freedom* (1962)



“On the face of it, shareholder value is the dumbest idea in the world. Shareholder value is a result, not a strategy... your main constituencies are your employees, your customers and your products... Short-term profits should be allied with an increase in the long-term value of a company.” Former GE CEO Jack Welch’s interview with Francesco Guerrera of the *Financial Times* (2009)

3

Corporate Citizenship

Fast forward to 2019, when investors are supporting social responsibility, and the Business Roundtable issues its *Statement on the Purpose of a Corporation*:



“While each of our individual companies serves its own corporate purpose, we share a fundamental commitment to all of our stakeholders.” Business Roundtable’s *Statement on the Purpose of a Corporation* (August 19, 2019)



Followed by a response by the Council of Institutional Investors:

“...boards and managers need to sustain a focus on long-term shareholder value. To achieve long-term shareholder value, it is critical to respect stakeholders, but also to have clear accountability to company owners. Accountability to everyone means accountability to no one.” *Council of Institutional Investors Responds to Business Roundtable Statement on Corporate Purpose* (August 19, 2019)

4

Corporate Citizenship

- The fundamental corporate law of fiduciary duties has not changed.
- The business judgment rule (“BJR”) has not changed.
- On the other hand, Minnesota has had a permissive “other constituencies” statute on its books since 1987 (Section 302a.251, Subd. 5)

5

Corporate Citizenship

Delaware courts have long held that boards must serve the best interests of shareholders first and foremost:



“The corporate form ... is not an appropriate vehicle for purely philanthropic ends, at least not when there are other stockholders interested in realizing a return on its investment...Having chosen a for-profit corporate form ... directors are bound by the fiduciary duties and standards that accompany that form...” Chancellor Chandler in *eBay Domestic Holdings, Inc. v. Newmark*, 16 A.3d 1, 34 (Del. Ch. 2010).

6

Corporate Citizenship

But Delaware courts will typically defer to board decisions on what it means to promote shareholder value:



“When director decisions are reviewed under the business judgment rule, this Court will not question rational judgments about how promoting non-stockholder interests — be it through making a charitable contribution, paying employees higher salaries and benefits, or more general norms like promoting a particular corporate culture — ultimately promote stockholder value.”
Chancellor Chandler in *eBay Domestic Holdings, Inc. v. Newmark*, 16 A.3d 1, 34 (Del. Ch. 2010).

7

Corporate Citizenship

Minnesota is more explicit in allowing directors to consider the interests of stakeholders besides shareholders:

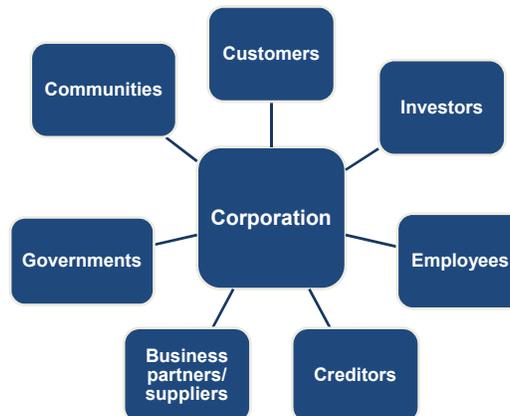


MN Statutes 302A.251, Subdivision 5: In discharging the duties of the position of director, a director may, in considering the best interests of the corporation, consider the interests of the corporation's employees, customers, suppliers, and creditors, the economy of the state and nation, community and societal considerations, and the long-term as well as short-term interests of the corporation and its shareholders including the possibility that these interests may be best served by the continued independence of the corporation.

8

Corporate Citizenship

The stakeholder galaxy is potentially limitless, and in a world of limited resources, companies must not only weigh tradeoffs between shareholders and stakeholders, but also among stakeholders.



9

Corporate Citizenship

Recently, there have been outspoken advocates for employee ownership and employee representation on boards.

Elizabeth Warren's Accountable Capitalism Act



- » Create an Office of United States Corporations and require any corporation with revenue over \$1 billion to obtain a federal charter of corporate citizenship, which tells directors to consider the interests of all relevant stakeholders (shareholders, customers, employees, communities in which the company operates) when making decisions
- » Allow workers to elect 40% of the membership of the board of directors
- » Limit directors' and executives' ability to sell shares of stock that they receive as pay for at least five years after they are received and at least three years after a share buyback
- » Require corporate political activity to be authorized by both 75% of shareholders and 75% of board members

10

CEO Activism

What do these CEOs have in common??

- **Ken Frazier (Merck)**
- **Tim Cook (Apple)**
- **Marc Benioff (SalesForce.Com)**
- **Dan Cathy (Chick-fil-A)**
- **Ed Stack (Dick's Sporting Goods)**
- **Ken Powell (General Mills)**
- **Ed Bastian (Delta Air Lines)**

CEO Activism

INSEAD's *New Framework for Corporate Activism*

Figure 1: A Framework for Corporate Political Positions - *Omitted*

Read more at <https://knowledge.insead.edu/blog/insead-blog/a-new-framework-for-corporate-activism-12556#Su2TGUUczcbSFheK.99>

Traversing the Risk and Compliance Landscape

The risk management landscape is rapidly evolving, with boards having to plan for, and react quickly to, developing risks.

***In re Caremark Int'l Inc. Deriv. Litig.*, 698 A.2d 959 (Del. Ch. 1996) was a wake-up call for boards that in order to fulfill their duty of care, they must be mindful in their oversight of risk and compliance programs:**

- Directors can't passively wait for "red flags"
- Directors have a duty of active supervision and monitoring "information and reporting systems . . . reasonably designed to provide to senior management and to the board itself timely, accurate information sufficient to allow management and the board, each within its scope, to reach informed judgments concerning both the corporation's compliance with law and its business performance"
- Reduction in sanctions if effective compliance programs are in place - 1991 Federal Organizational Sentencing Guidelines

13

Traversing the Risk and Compliance Landscape

- **Two kinds of potential *Caremark* oversight failures have developed:**
 - Failure to implement any board oversight policies
 - Failure to actively monitor policies adopted by the board
- **Delaware judges have noted that proving a *Caremark* claim is the most difficult fiduciary duty breach to find**
 - Because it requires a showing of "bad faith" on the part of directors
- **Nonetheless, in recent months, two different Delaware courts have refused to dismiss claims that they found to be credible involving each line of *Caremark* cases.**

Traversing the Risk and Compliance Landscape

- ***Marchand v. Barnhill* (De. S. Ct., 6/19) (the “Blue Bell” case): *failure to develop any relevant oversight policies case***
 - Underlying facts: ice cream manufacturer had outbreak of listeria that resulted in three consumer deaths, product recalls, complete plant shutdown and laying off of 1/3 of workforce
 - Plaintiffs brought derivative action against board and two executives, claiming that the board failed to develop any food safety oversight policies
 - Delaware Supreme Court overruled the lower court’s (Chancery Ct) dismissal of the claim, finding that there was no:
 - Board committee focused in food safety
 - No regular process requiring management to keep the Board informed of food safety compliance practices or risks
 - Board minutes in period of time prior to deaths showing any discussion of risks, although management had received “yellow” or “red” flag reports
 - Evidence in Board minutes there was any regular discussion of food safety issues

Traversing the Risk and Compliance Landscape

- ***Marchand v. Barnhill* (De. S. Ct., 6/19) (the “Blue Bell” case):**
 - In addition, the factual record revealed that federal food inspections found systemic food safety issues at plants that any reasonable monitoring system would have resulted in a report to the board
 - The fact that this was a single product company played a key role in the Supreme Court’s decision; food safety, in its view, should have been critical to the Board’s oversight responsibility

Traversing the Risk and Compliance Landscape

- ***In re Clovis Oncology Deriv. Litig.* (DE. Ch. Ct., 10/19): *failure to actively monitor case***
 - Underlying facts: company undergoing clinical trials for its experimental lung cancer drug had Board policies in place to oversee and monitor the progress of the clinical trials. Early results were promising, but later results led to conclusion by FDA not to approve the drug
 - Plaintiffs brought a claim that, due to the Board's ignoring "red flags" that management was not adhering to strict protocols during the clinical trials, it allowed Clovis to mislead the market (and regulators) in its public statements about the drug's efficacy
 - They also made subsidiary claims of insider trading by certain board members and executives prior to the correcting announcement

Traversing the Risk and Compliance Landscape

- ***In re Clovis Oncology Deriv. Litig.* (DE. Ch. Ct., 10/19): *failure to actively monitor case***
 - The Chancery Court refused to dismiss the claim, finding that, particularly in a highly regulated environment, the Board's duty to oversee compliance with "positive law" is greater than oversight of normal business risk in a business plan, because violations of law and resulting liability can occur
 - The Court also emphasized that here, as in the *Blue Bell* case, the failure occurred with respect to "mission critical regulatory compliance risk"
 - Unlike the *Blue Bell* case, the Court found that, while there was an adequate system of reporting and controls in place, the Board ignored "red flags" that the company was not complying with its own strict trials protocols

Traversing the Risk and Compliance Landscape

- **Some take-aways from both recent cases:**
 - Failing to have *any* reasonable policies, procedures or controls in place to ensure timely reporting “up” to the Board of material risks is dangerous
 - Ignoring “red flags” about material risks reported up to the Board is dangerous
 - Having solid controls in place for important business operations that are highly regulated is very important
- **Cautionary note: neither case has been fully litigated yet. These were decisions at the motion to dismiss stage (when the court is required to accept all well-pled allegations as being accurate)**

Diverse and Effective Boards

- **As of July 2019, every S&P 500 company board had at least one female member, and women held 27% of all board seats.**
 - Only 13.1% (376) companies in the Russell 3000 have all-male boards.
 - In Q1 of 2019, 46.8% of all new directors were female.
- **Ethnic diversity is also increasing, though more slowly than gender.**
 - In 2019, 21.1% of new directors appointed to S&P 500 companies were ethnic minorities
 - In 2019, ethnic minorities serving on Russell 300 boards exceeded 10% for first time
- **But according to some projections, it will take nearly 40 years for the Russell 3000 companies nationwide to reach gender parity — the year 2055.**



Diverse and Effective Boards

Board gender diversity has been an area of significant and controversial legislation:



- Last year, California passed SB 826. The legislation requires that public companies with principal executive offices located in California, no matter where they are incorporated, include a “representative number” of women on their boards of directors.
- Illinois has pending legislation requiring disclosure of board and management diversity by 2021. Similar legislation is being considered by other states.
- However, these statutes are vulnerable to legal challenge under the Equal Protection Clause of the US Constitution, and companies headquartered but not incorporated in these states may contend that they are not subject to these statutes under the internal affairs doctrine.

21

Diverse and Effective Boards

The diversity push has been expanding from the boardroom into the C-Suite. On October 11, 2019, NYC Comptroller announced its “Boardroom Accountability Project 3.0.”



- Sent letter to 56 S&P 500 companies to adopt the “Rooney Rule” when conducting searches for directors and CEOs.
- Will file shareholder proposals at companies with lack of apparent racial diversity at the “highest levels.”

Unlike in Europe, the future of diverse boards in the US remains by in large a matter of private ordering.

22

Questions?

