King & Spalding

Public Companies Practice

The Insider: Key Developments for Chief Legal Officers and Corporate Legal Teams

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Introducing *The Insider*

Welcome!

Welcome to the inaugural issue of *The Insider*. This new publication from King & Spalding's Public Companies Practice, which will be produced periodically, is focused on key developments for chief legal officers and their corporate legal teams.

In each issue, our dedicated Public Companies team will provide updates on relevant developments with practical advice that is intended to help position you to give up-to-date and considered advice to your internal clients.

Speak business, not legalese

Our clients want clear and actionable advice, not long demonstrations of our legal knowledge. We speak business, not legalese.

Our Public Companies Practice

King & Spalding's dedicated cross-practice Public Companies team advises clients on the unique challenges that arise from operating as public companies with disclosure obligations and governance requirements coupled with scrutiny from regulators, institutional investors and other significant stakeholders, stock exchanges and the media.

Our experienced team advises public companies and their boards of directors, executive management and legal teams as they navigate complex corporate transactions, high-stakes disputes and other corporate, securities, strategic and business-related matters, including corporate governance, stockholder and compliance matters, SEC and stock exchange reporting obligations and disclosure issues, regulatory matters, and general corporate and commercial matters.

Our core, multi-disciplinary team regularly advises public companies on, among other topics: Activism; Corporate Finance; Corporate Governance, Disclosure and Stakeholder Engagement, including Environmental, Social & Governance (ESG) matters; Mergers & Acquisitions; Proxy Access; and Special Purpose Acquisition Companies (SPACs).

In addition, we draw on cross-firm solutions in substantive legal areas relevant to public companies, such as: Antitrust; Benefits, Compensation & Employment; Crisis Management; Data, Privacy and Security; Environmental matters; Global Human Capital & Compliance; Labor; Intellectual Property; Securities Enforcement and Regulation and Securities Litigation.

PRACTICAL ADVICE

- We recognize that constant demands on corporate legal teams make time a precious commodity.
- With that in mind, we have designed *The Insider* with a focus on developments that are relevant to your day-to-day work and presenting takeaways intended to give straightforward, practical advice that is easy to implement.
- As always, we invite you to contact members of our Public Companies Practice identified on the last page of this issue or your regular K&S contact with any questions concerning the topics presented herein.
- This is our first edition, and we look forward to your feedback. In the meantime, we hope you find *The Insider* to be a useful reference.

Don’t Jeopardize Attorney-Client Privilege by Using the Wrong E-mail Account

In re WeWork Litigation

(2020 WL 7624636, at *2 (Del. Ch. Dec. 22, 2020))

In December 2020, the Delaware Court of Chancery ruled that the attorney-client privilege protecting e-mails between counsel and outside directors was waived because the directors had used their (third party) work e-mail accounts.

In discovery related to the case, WeWork sought materials SoftBank withheld based on attorney-client privilege. The materials, which involved confidential WeWork matters, were sent between SoftBank’s internal and external counsel and the Sprint e-mail accounts for individuals with roles at both WeWork and Sprint. Like WeWork, Sprint was controlled by SoftBank, but Sprint was not a party to the litigation.

In the decision, Chancellor Bouchard applied the four-part test regarding whether there was an objectively reasonable expectation of privacy in the communications from *In re Asia Global Crossing, Ltd.* (322 B.R. 247 (Bankr. S.D.N.Y. 2005)), which asks (1) does the corporation maintain a policy banning personal or other objectionable use on its computer or e-mail systems, (2) does the corporation monitor the use of the employee's computer or e-mail, (3) do third parties have a right of access to the computer or e-mails, and (4) did the corporation notify the employee, or was the employee aware, of the use and monitoring policies? While cases relating to work e-mail privilege typically arise in disputes between an employer and its employee, the Court found no reason not to apply the same analysis where an outside third party is seeking protection.

The Court found that the attorney-client privilege was waived as the employees should not have had a reasonable expectation of privacy in their Sprint e-mail accounts, noting that Sprint’s Code of Conduct stated employees should not have an expectation of privacy when sending, receiving, accessing or storing information via Sprint’s system and that Sprint reserved the right to review workplace communications, including e-mails.

Ultimately, communications between SoftBank’s legal counsel and a Softbank employee on WeWork’s Board could not be protected by the attorney-client privilege because the director had used a Sprint e-mail account.

PRACTICAL ADVICE

- Outside directors should be encouraged to avoid using their work e-mail accounts (i.e., of their primary employer) to send or receive Board materials that otherwise may be privileged.
- Consider establishing a confidential Board portal for director communications. E-mail communications can then be limited to a notice of materials having been posted to the portal.
- If a Board portal is not used, create dedicated company e-mail addresses for non-employee directors or have those directors use personal e-mails (or, better yet, create dedicated private e-mail addresses) for Board communications.
- This issue may be particularly acute for special committees, which are likely reluctant to use a Board portal or a company e-mail address for communications with committee counsel. Proper communications protocol should be addressed at an early meeting of the special committee and personal e-mail addresses should be created and used (consider whether the committee financial or legal advisor can create appropriate addresses for such limited purpose).

Board Diversity Matters and So Does Diversity Disclosure

Pressure from All Sides, Including Plaintiffs' Bar

While a focus on diversity in the boardroom is not new, the spotlight has perhaps never been brighter on public companies than it is now, with a variety of stakeholders putting pressure on companies to do and say more.

After years of extolling the virtues of Board diversity without meaningful enforcement mechanisms, investors are now demanding both disclosure of Board diversity information and threatening votes against companies whose Boards lack various types of demographic diversity. Proxy advisors are also turning up the pressure. For example, this year, leading proxy advisor Institutional Shareholder Services (ISS) is warning companies with no apparent racial and ethnic diversity that lack of diversity will lead to votes against certain directors in future years (e.g., Nomination and Governance Committee members).

States are active in this area, too. California now requires public companies with a California headquarters to have at least one director from an "underrepresented community" by the end of 2021 and, depending on Board size, at least two or three such directors by the end of 2022. Notwithstanding the question of whether such requirements are applicable to companies incorporated in another state, other states are following California's lead with similar legislation for gender, racial/ethnic, and other types of diversity.

At the end of 2020, Nasdaq filed a proposal to adopt new listing rules related to Board diversity and increased disclosures. The proposal would require Nasdaq-listed companies to disclose director diversity and feature a comply-or-explain set of quotas for female directors and directors who are otherwise diverse by means of race, ethnicity, or LGBTQ+ status. Experts expect the SEC will approve the requirements later this year.

As if the foregoing was not enough, there are litigation risks as well. Since last summer, multiple public companies have been sued in shareholder derivative lawsuits alleging misleading proxy statements and breaches of fiduciary duty arising out of an alleged lack of diversity among Board members. The complaints essentially allege it is misleading for companies to state they are committed to diversity or that they consider diverse Board candidates when, in fact, the Board lacks diversity. In other words, statements of corporate values may not just be insufficient to satisfy stakeholders; they may be used against companies whose walk does not match their talk.

Looking ahead, it would be wise to use the current attention on Board diversity to evaluate other workforce diversity issues as well. Stakeholders are increasingly interested in diversity statistics, particularly relative to company's senior leadership.

Public commitments to diversity are no longer enough to avoid scrutiny; stakeholders and the plaintiffs' bar increasingly holding public companies accountable.

PRACTICAL ADVICE

- Review and carefully craft future proxy statement disclosure and other public disclosures regarding Board composition and diversity policies and practices.
- Avoid "aspirational disclosure" regarding diversity matters; describe what you are doing.
- Assess your Board's existing composition and nominating policies and practices.
- Consider adopting a "Rooney Rule" to guarantee the pool from which director candidates are chosen will include one or more members of underrepresented communities, which is more tangible proof of interest in the issue than generic disclosure about the importance of diversity.

Mission Critical: Satisfying the Board's Duty to Monitor Requires Active Oversight

Uptick in *Caremark* Claims Highlights Duty to Monitor

(In re Caremark Intern. Inc. Derivative Litigation, 698 A.2d 959 (Del. 1996))

Over the past couple of years, plaintiffs have increasingly pursued derivative claims alleging that the directors' failure to make a good faith effort to adequately monitor operations constituted a breach of directors' oversight duties under the fiduciary duty of loyalty.

To establish these "*Caremark* claims" in reference to the above cited 1996 case under Delaware law, a plaintiff must show that either (i) directors completely failed to implement any reporting or information systems and control, or (ii) having implemented such systems or controls, directors consciously failed to monitor or oversee its operations, including by turning a blind eye to "red flags" they knew or should have known indicated risks or problems requiring their attention.

While this is a high bar and liability for directors under *Caremark* is rare, recent Delaware cases serve as a useful reminder of the importance of the Board's duty to monitor. In both *Marchand v. Barnhill* (Del. June 19, 2019) and *In re Clovis Oncology Derivative Litigation* (Del. Ch. Oct. 1, 2019), the court sustained derivative *Caremark* claims at the motion to dismiss stage based on allegations in the complaints asserting specific facts—meaning the case continued and discovery, with all related costs, was permitted, providing a tremendous advantage to the plaintiffs.

Other cases following these decisions also have included *Caremark* claims and we expect that plaintiffs will continue to assert them, including in so-called "event-driven" litigation where claims are brought following disclosure of a negative corporate event. For example, in litigation arising out of lack of Board diversity, climate change initiatives, cybersecurity/data breaches and the COVID-19 pandemic, plaintiffs have asserted that Boards failed to establish information systems or adequately monitor companies' efforts and responses in these areas.

Ultimately, protecting directors from liability requires the development and implementation of information and reporting systems that cover relevant areas, active monitoring by the Board of those systems and maintenance of consistent documentation of these monitoring efforts.

Despite the high threshold for sustaining "Caremark" claims, Boards should establish and actively monitor information and reporting systems for regulatory and compliance matters.

PRACTICAL ADVICE

- Identify the company's "mission critical" risks and ensure that reporting systems are in place to adequately identify and communicate operational and compliance developments.
- Position your Board to demonstrate active oversight through established and consistent management reporting and regular Board meetings to review and consider such reports or consider establishing a separate risk/compliance committee to do so.
- It is essential to build a proper record by memorializing the Board's oversight efforts in meeting minutes as courts look for contemporaneous evidence of the Board's knowledge of key risks and its actions regarding its oversight responsibilities.
- Add an evaluation of the related oversight function to the Board's regular agenda.

Officers Owe Fiduciary Duties, too, and are Increasingly Litigation Targets

Plaintiffs are Targeting Corporate Officers in M&A Litigation

Gantler v. Stephens (965 A.2d 695 (Del. 2009))

In 2009, the Delaware Supreme Court ruled in *Gantler v. Stephens* (965 A.2d 695 (Del. 2009)) that officers owe fiduciary duties identical to directors.

So, like directors, officers must comply with the duty of care and the duty of loyalty, but compared to directors, officers have less protection as they do not benefit from Section 102(b)(7) of the Delaware General Corporation Law, which permits a corporation to exculpate directors from money damages for breaches of the duty of care. As a result, officers face the potential of personal liability for breaches of their fiduciary duties.

Recently, stockholder plaintiffs have named corporate officers in complaints alleging breaches of the duty of care, particularly in the context of M&A transactions, and many of these cases have survived a motion to dismiss in court.

For example, the Delaware courts have recently refused to dismiss claims alleging that officers breached their "disclosure duties" because they provided shareholders with a proxy statement relating to an M&A transaction that did not disclose certain unaudited financial projections that were provided to the Board, did not fully disclose certain conflicts of interest, or did not accurately describe the terms of a merger agreement. Plaintiff's firms have also advanced claims against officers under a "fraud on the Board" theory, alleging that a target's officers failed to disclose "material information" to the Board, thereby inducing the Board to breach its fiduciary duties to stockholders.

More recently, V.C. Laster in *In re Columbia Pipeline Group, Inc. Merger Litigation*, (C.A. No. 2018-0484-JTL (Del. Ch. Mar. 1, 2021) stated that a plaintiff can recover monetary damages for a breach of (i) the duty of care, only by establishing that the fiduciary was grossly negligent and (ii) the duty of loyalty, only by proving that the fiduciary "harbored self-interest adverse to the stockholders' interests, acted to advance the self-interest of an interested party …, or [otherwise] acted in bad faith."

All is not lost for officers however – while officers cannot be exculpated under Section 102(b)(7), depending upon the circumstances they may be indemnified under a company's bylaws or pursuant to an indemnification agreement. D&O insurance may also cover certain actions by officers.

Nevertheless, corporate officers should be mindful that their conduct and actions may well be targeted and ensure that they execute their duties in a deliberate and considered manner.

Officers of Delaware companies are potential targets of breach of fiduciary duty of care claims, even where director liability is exculpated.

PRACTICAL ADVICE

- Recent cases highlight the importance of (1) ensuring adequate procedures are in place to report material conflicts to the Board, particularly in the context of an M&A transaction and disclosed to stockholders if a stockholder vote is required, and (2) officers taking reasonable steps to ensure material information is disclosed to the Board and stockholders.
- D&O insurance policies should be reviewed annually from a substantive perspective to ensure they contain appropriate protections from the latest trends in stockholder litigation.
- D&O indemnification agreements should contain the broadest protections appropriate for the company.

Spring Cleaning: Why It's Time to Dust Off Your Forum Selection Bylaw

Have you read your forum selection bylaw recently?

Just over a decade ago, a footnote to an otherwise unrelated decision by Vice Chancellor Laster set in motion a change that is today reflected in the bylaws or charters of over 500 Delaware public companies. Vice Chancellor Laster's reference to an exclusive forum provision for the resolution of intra-party disputes opened the door to an attractive means of consolidating litigation in a single forum (particularly a forum known for its advanced body of relevant case law, such as Delaware). In the following years, hundreds of Delaware public companies adopted such exclusive forum provisions, both in certificates of incorporation and in bylaws.

Litigation during the first part of the decade confirmed that such provisions were legal and valid and would be respected by other forums in which litigation was brought. Importantly, this validity extended to exclusive forum provisions adopted unilaterally by Boards of Directors through an amendment of the bylaws.

Last year (and perhaps lost due to it being issued during the early days of the pandemic), Delaware provided another helpful clarification regarding the utility of exclusive forum provisions—in this instance, regarding the applicability of forum selection clauses related to claims under the Securities Act of 1933. Following the U.S. Supreme Court decision in *Cyan, Inc. v. Beaver County Employees' Retirement Fund* (138 S. Ct. 1061 (2018)), which held that claims arising under the 1933 Act could be brought in either (or both!) state or federal court, many Delaware companies refined exclusive forum provisions to add a new prong related to such federal securities claims. These new and improved bylaws made clear that any claims under the 1933 Act must be brought exclusively in federal court. In *Salzberg v. Sciabaucchi* (227 A.3d 102 (April 14, 2020)), the Delaware Supreme Court held that a Delaware corporation would be permitted to ease the burden of duplicative litigation at the state and federal level by requiring that all 1933 Act claims be made exclusively in federal court.

So, for the second time in a decade, the Delaware courts have assisted Delaware corporations to avoid multi-jurisdiction litigation. With upticks in shareholder litigation (*See*, for example, the discussion of *Caremark* claims on page 4), now is the time to ensure that your bylaws include the latest "bells and whistles," including the ability to defend 1933 Act claims in federal court.

Recent developments provide new ways for Boards to enhance control over the forum for shareholder litigation.

PRACTICAL ADVICE

- Review your bylaws to ensure you have the latest forum selection provisions.
- If the forum selection provision can be improved, we recommend discussing it with your Nominating and Governance Committee at the next meeting—significant protections are available and may be adopted unilaterally by your Board of Directors.
- As with any Board action, it is imperative to build a proper record by memorializing the Board's rationale for adopting new forum selection provisions.
- While preferable to adopt these provisions on a "clear day," even when adopted in connection with a transaction (which may trigger this type of litigation) the courts have respected the exclusive forum provisions.

Is Your Poison Pill a Proportionate Response to a Legitimate Threat?

The Williams Companies Stockholder Litigation

(2021 WL 754593 (Del. Ch. Feb. 26, 2021))

In February 2021, the Delaware Chancery Court permanently enjoined a stockholder rights plan (a/k/a "poison pill") adopted by The Williams Companies, Inc. in March 2020 as a response to a declining stock price in the wake of the COVID-19 pandemic. In the press release announcing adoption of the pill, Williams said its pill was intended to "reduc[e] the likelihood that any person or group gains control of Williams through open market accumulation or other tactics (especially in recent volatile markets) without paying an appropriate control premium."

The Williams pill was of a limited duration (one year), with a trigger (the percentage of shares acquired or proposed to be acquired that triggers the pill) at the unusually low threshold (outside of pills designed to protect tax attributes) of 5% and included limited passive investor exclusions as well as a broad "wolfpack" provision aimed at preventing shareholders from "acting in concert."

Applying the intermediate "enhanced scrutiny" standard of review adopted in *Unocal Corp. v. Mesa Petroleum* (493 A.2d 946 (Del. 1985)), the Chancery Court assessed (i) the reasonableness of Board action under the circumstances and (ii) whether the defensive action was reasonable in relation to the threat posed and not coercive or preclusive. In its decision, the Court assessed the threats as "purely hypothetical" and ultimately concluded that a "combination of features created a response that was disproportionate to [the] stated hypothetical threat."

The Court also noted the Board meeting at which the pill was adopted was "initially scheduled to last for one hour, adjourned after forty minutes" and observed that "the lawyer-drafted documents" such as resolutions and minutes did not reflect the directors' actual intent based on their testimony.

V.C. McCormick's inclusion of those observations underscores the importance of having a thoughtful process for reviewing the purposes of and the bases for adoption of pills under various circumstances, both generally when reviewing potential defensive actions and specifically in the case of an immediate threat.

As more companies put a poison pill "on the shelf," it is imperative that proper Board process is followed if the pill is taken off the shelf and adopted. The earlier/first meeting to put the pill on the shelf is not a substitute.

The Williams decision provides a guardrail but does not change the fact that pills remain a valuable defensive tool for companies facing an identifiable takeover or activist threat.

PRACTICAL ADVICE

- Review your "on-the-shelf" pill to see if any changes are appropriate considering this decision and use it as an opportunity to discuss with your Board. If you don't have a pill "on-the-shelf" and ready to go in the event of an identified threat, now is a good time to consider one.
- A pill can be an effective tool but relying solely on a pill is inadequate. Preparing for a threat requires considered forward thinking and deliberate stakeholder engagement.
- When adopting a pill in response to a specific threat, consider whether the threat is legitimate/real and whether the terms present a proportionate response to the threat.
- As with any high-profile corporate action, it is important that the Board's process for evaluating and considering a response to a threat is properly informed, discussed and memorialized.

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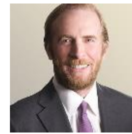
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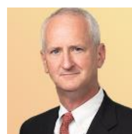
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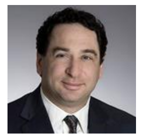
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