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Preparing for the 2023 Annual Report and Proxy Statement Season

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A number of recent updates to SEC disclosure obligations are effective for the 2023 Form 10-K and proxy statement season. Below is a list of important updates that public companies should consider for this reporting cycle. Note that this list includes key SEC and stock exchange required updates, a potential amendment to Delaware certificates of incorporation due to the Delaware General Corporation Law and does not cover other updates that should be taken into consideration, such as voting guidelines of proxy advisory firms and institutional investors, which are beyond the scope of this alert.

Pay Versus Performance

The SEC now requires certain detailed "pay-versus-performance" disclosures pursuant to Item 402(v) of Regulation S-K. These disclosures are designed to provide information reflecting the relationship between executive compensation "actually paid" by the company and the company's performance. Public companies, including smaller reporting companies, must include the new disclosure in proxy and information statements. The new disclosure is not required in Annual Reports on Form 10-K or registration statements. Disclosure is required for fiscal years ending on or after December 16, 2022, which means that for calendar year-end companies, disclosure will be required in the first proxy statement or information statement filed in 2023.

Ultimately, all reporting companies, except for smaller reporting companies, will be required to provide pay-versus-performance disclosure for each of the company's five most recently completed fiscal years. A phase-in period will allow the company to provide the information for three years in the first proxy or information statement in which it provides the disclosure, adding another year of disclosure in each of the two subsequent annual proxy or information statement filings. Smaller reporting companies are subject to scaled disclosure requirements. Most notably among these scaled disclosure requirements, for the first year, smaller reporting companies are required to provide only two years of pay-versus-performance disclosure and, following the first year of disclosure, are required to provide three years of pay-versus-performance disclosure.

Public companies should begin preparing for pay-versus-performance disclosures now and should involve their compensation committees early in the process, as calculating executive compensation "actually paid" may be time consuming and expensive.

For more information on pay-versus-performance, please see this article prepared by Haynes and Boone Partner Rosebud Nau and Associate Alexandria Pencsak.

Universal Proxy Rule

Starting September 1, 2022, contested director elections of domestic issuers began requiring the use of "universal proxy cards," meaning proxy cards naming all director nominees presented for election, including those of the company and the dissident stockholders. This change gives stockholders the ability to vote by proxy for their preferred combination of candidates nominated by the company and the dissident stockholders in a contested election.

The universal proxy card rules apply to all non-exempt solicitations for contested elections other than those involving registered investment companies and business development companies.

New Rule 14a-19 requires that the new universal proxy card must include the names of both company and dissident nominees, along with any other stockholder nominees included as a result of proxy access bylaws to the extent applicable. The rule requires dissidents to (i) provide companies with notice of their intent to solicit proxies and the names of their nominees at least 60 days prior to the anniversary of the previous year's annual meeting (subject to a longer period pursuant to advanced notice bylaws), (ii) file their definitive proxy statement by the later of 25 calendar days before the stockholder meeting and five calendar days after the company files its definitive proxy statement and, (iii) solicit stockholders of the company representing at least 67 percent of the voting power of the shares entitled to vote at the meeting. The rule requires companies to notify dissidents of the names of the company's nominees at least 50 calendar days before the anniversary of the previous year's annual meeting. The rule requires each side in a proxy contest to mail (or provide through "notice and access") the proxy card and their proxy statement, and to refer stockholders to the other party's proxy statement for information about the other party's nominees and to the SEC's website for access to the other side's proxy statement free of charge.

The SEC has also amended proxy rules to mandate that in all director elections, proxy cards clearly state the applicable stockholder voting options and that proxy statements disclose the effect of a stockholder's election to withhold their vote. These rule amendments operate to formalize a long-standing practice already followed by most companies. Under Rule 14a-4(b), as amended, registrants are now required to include an "against" voting option in lieu of a "withhold authority to vote" option on the form of proxy for elections of directors under a majority vote standard if state law gives legal effect to such a vote and also permits shareholders to abstain in such an election. A company must also disclose in its annual proxy statement the deadline for stockholders to give timely notice to the company of dissident nominations for inclusion on a universal proxy card in connection with the following annual meeting.

For more information on the new universal proxy rule, please see this Haynes and Boone alert.

Nasdaq Board Diversity Objective

Under new Nasdaq Rule 5605(f), each Nasdaq-listed company will have to meet, or explain why it does not meet, certain diversity criteria with respect to its board composition. Companies must have, or explain why they do not have, at least two diverse directors including (1) at least one director who self-identifies as female, and (2) at least one additional director who self-identifies as an underrepresented minority or LGBTQ+. There are certain exceptions for foreign issuers, smaller reporting companies (who may satisfy the requirement with two female directors), companies with five or less directors (who must only have one diverse director) and certain exempt issuers such as SPACs and limited partnerships.

Nasdaq-listed companies must annually disclose self-identified board diversity data in a substantially similar format as Nasdaq's Form Board Diversity Matrix. The matrix must include data for the current and prior year.

Recently, Nasdaq filed a rule change with the SEC that was declared effective immediately. Under these new rules, a few important updates emerged:

- For the diversity matrix requirement that is already effective, the annual deadline for compliance is December 31st.

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- Each Nasdaq company must have, or explain why it does not have, at least one diverse director by December 31, 2023.
- Each company listed on the Nasdaq Global Select Market or Nasdaq Global Market must have, or explain why it does not have, at least two diverse directors by December 31, 2025.
- Each company listed on the Nasdaq Capital Market must have, or explain why it does not have, at least two diverse directors by December 31, 2026.
- If a company is not going to meet the board diversity objectives outlined above, it must disclose the Nasdaq requirements and explain the reasons why it did not satisfy them annually on or before December 31st either (a) in a proxy statement or an information statement (or, if the company does not file a proxy statement or information statement, in its Form 10-K or 20-F); or (b) on the company's website. If the company provides the disclosure on its website, it is required to submit the disclosure concurrently with its proxy statement or information statement (or 10-K or 20-F) and submit the URL through the Nasdaq Listing Center within one business day after posting. Under the amended rules, companies are allowed to also notify Nasdaq about this alternative corporate website disclosure by sending an e-mail to drivingdiversity@nasdaq.com.

For more information on the new board diversity objectives, please see this Haynes and Boone alert.

Exculpation of Officers from Personal Liability

Amendments to the Delaware General Corporation Law Section 102(b)(7) now permit the extension of exculpation for breaches of the duty of care to senior officers in addition to directors. However, even under amended rules, senior officers may not be exculpated from personal liability for breaches of the duty of loyalty, actions not in good faith, intentional misconduct or knowing violations of law or any transaction where an officer derives an improper personal benefit. Further, protection is not retroactive.

Claims against officers will not be barred in any action by or in the right of the company. Companies retain the right to bring an action against officers. Derivative suits for the breach of the duty of care are also still permitted (unlike for directors).

In order to benefit from the amendment to Section 102(b)(7), companies must amend their certificate of incorporation to adopt the provision and extend exculpation to officers. Board action and stockholder approval will be required, and public companies will likely need to file a proxy statement. Private companies can simply include the provision in their certificate of incorporation prior to conducting an initial public offering.

Taking advantage of Section 102(b)(7) is not without potential consequences. Although preliminary indications suggest that ISS and Glass Lewis may not be opposed in all cases, there are certain indications that ISS and Glass Lewis may not support such amendments moving forward. In issuing voting recommendations to date, neither ISS nor Glass Lewis has expressed any material concerns or made any adverse voting recommendations specifically addressing officer exculpation proposals (or made adverse voting recommendations in the re-election of directors who have approved such exculpation proposals). Despite its lack of adverse voting recommendations on officer exculpation proposals thus far, Glass Lewis' recently adopted 2023 Policy Guidelines, which are effective for annual meetings in 2023, state that Glass Lewis "will closely evaluate proposals to adopt officer exculpation provisions on a case-by-case basis [and] generally recommend voting against [officer exculpation] proposals eliminating monetary liability for breaches of the duty of care for certain corporate officers, unless

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compelling rationale for the adoption is provided by the board, and the provisions are reasonable." ISS also recently published its Benchmark Policy Changes for 2023, noting, among other things, that ISS will "vote case-by-case on proposals on director and officer … exculpation." Exculpation may be viewed with stockholder disfavor. A proposal to adopt officer exculpation could attract negative media scrutiny and adverse attention to high profile corporations. Public company boards of directors should meet to discuss the potential costs and benefits of officer exculpation.

Risk Factor Updates

Each year, public companies should revisit their risk factor disclosures for important updates. In their annual reports, companies should consider adding or updating risk factors related to inflation and interest rates, foreign exchange rate volatility and economic uncertainty, the Inflation Reduction Act, the potential impact of an economic recession, the impact of the rising cost of capital on the company's business plans and financial position, supply chain risks, the war in Ukraine, the ongoing COVID-19 pandemic, climate change, cybersecurity risks, the increased cost and shortage of labor and any other risks which may have emerged for the company during the prior year.

Say-on-Frequency Votes

Exchange Act Rule 14a-21(b), the so-called "Say-on-Frequency" rule, requires that companies provide a separate stockholder advisory vote in proxy statements for annual meetings to determine whether the vote on the compensation of executives required by Section 14A(a)(1) of the Exchange Act will occur every 1, 2, or 3 years. Say-on-Frequency votes must be held once every six years and must be taken even if the company does not intend to change the frequency with which it seeks to conduct its Say-on-Pay votes. The upcoming year is when many public companies will be seeking a Say-on-Frequency vote again, as many public companies were first required to do so in 2011, when the Dodd-Frank Act was enacted.

In addition to seeking the Say-on-Frequency vote, Item 5.07 of Form 8-K requires that a company must disclose its decision as to how frequently the company will conduct Say-on-Pay votes following each Say-on-Frequency vote. In order to comply with this requirement, a company must disclose the determination in the original Form 8-K filing that discloses the preliminary and final results of the Say-on-Frequency vote, or file an amendment to the original Form 8-K. The Form 8-K amendment is due no later than 150 calendar days after the date of the end of the annual meeting in which the Say-on-Frequency vote occurred, but in no event later than 60 calendar days prior to the deadline for submission of stockholder proposals as disclosed in the proxy materials for the meeting at which the Say-on-Frequency vote occurred. Specifically with respect to Say-on-Frequency votes, an issuer must disclose the number of votes cast for each of the choices (every one, two or three years), as well as the number of abstentions in Item 5.07 of Form 8-K.

Clayton Act D&O Questionnaires

Given the increased level of enforcement of Section 8 of the Clayton Antitrust Act of 1914, we recommend that public companies include questions addressing potential Clayton Act issues in their 2023 D&O Questionnaires. If interested in sample D&O Questionnaire language that may be added to address these concerns, please contact a member of the Haynes and Boone Capital Markets and Securities Practice Group.

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Cryptocurrency Updates

Recent bankruptcies and financial distress among crypto asset market participants have caused widespread disruption in those markets. Companies may have disclosure obligations under the federal securities laws related to the direct or indirect impact that these events and collateral events have had or may have on their business. On December 8, 2022, the SEC posted a sample letter to companies regarding recent developments in cryptocurrency asset markets. Public companies should review the sample letter, available here, in detail. This may form another basis on which the SEC enforcement teams could focus when assessing disclosure failures.

Clawback Rules Under Dodd-Frank

On October 26, 2022, the SEC adopted final rules implementing the incentive-based compensation recovery provisions of the Dodd-Frank Act. The final rules direct the stock exchanges to establish listing standards requiring listed companies to develop and implement policies for the recovery of erroneously awarded incentive-based compensation received by current or former executive officers and to satisfy related disclosure obligations. These new rules are expected to be effective in 2023.

The SEC has decided to interpret Dodd-Frank expansively to include both “Big R” and “little r” restatements as triggers for a compensation recovery analysis. “Big R” restatements correct errors that resulted in a material misstatement in previously issued financial statements. “Little r” restatements correct errors that would only result in a material misstatement if the errors were left uncorrected in the current report or if the error correction was recognized in the current period.

Listed companies will be required to adopt a clawback policy providing for recovery of incentive-based compensation erroneously received by current or former executive officers during the three completed fiscal years immediately preceding the year in which the company is required to prepare an accounting restatement due to material noncompliance with financial reporting requirements. Erroneous payments must be recovered even if there was no misconduct or failure of oversight on the part of an individual executive officer.

Listed companies must (i) file their written clawback policies as exhibits to their annual reports, (ii) indicate by checkboxes on the cover pages of their annual reports whether the financial statements included in the filings reflect a correction of an error to previously issued financial statements and whether any of those corrections are restatements requiring a recovery analysis of incentive-based compensation under their clawback policies and (iii) disclose how they have applied their clawback policies during or after the last completed year. Under the new rules, a company may be delisted if it does not timely adopt a clawback policy that complies with the applicable listing standard, disclose the clawback policy and any application of the policy in accordance with SEC rules or enforce the clawback policy’s recovery provisions.

Rescinded Rules and Guidance for Proxy Advisory Firms

After the 2020 rules and guidance for proxy advisory firms were issued, institutional investors and other proxy advisory firm clients expressed concerns regarding the ability of proxy advisory firms to provide independent advice in a timely manner.

In September 2022, the SEC approved certain final modifications to address these concerns:

- Note (e) to Rule 14a-9 was deleted due to it adding confusion rather than certainty regarding the application of Rule 14a-9 to proxy voting advice.

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- Rule 14a-2(b)(9)(ii) was deleted due to the potential benefits not outweighing the potential detriments to the cost, timeliness and independence of the proxy voting advice.
- Rules 14a-2(b)(9)(iii-vi) were also deleted as they were safe harbors and exclusions to the conditions in Rule 14a-2(b)(9)(ii), which was deleted.
- Supplemental Guidance was provided in 2020 by the SEC to accompany the Rule 14a-2(b)(9)(ii) conditions and have now been deleted due to such rule being deleted.

Some rules from 2020 remain:

- Definition of Solicit and Solicitation
  - *Rule 14a-1(l)(1)* – Furnishing a form of proxy or other communication to security holders reasonably calculated to result in the procurement, withholding or revocation of a proxy. This includes proxy voting advice making recommendations to a security holder as to its vote, consent or authorization on a specific matter for which the security holder is solicited and the provider of the advice markets its expertise as a provider of proxy voting advice, separately from other forms of investment advice, and such advice is sold for a fee.
  - *Rule 14a-1(l)(2)* provides that the definition does not apply to a person who furnishes such advice only in response to an unprompted request.
- Conflicts of Interest Disclosure
  - *Rule 14a-2(b)(9)* – Disclosure should be provided for (i) any information regarding an interest, transaction or relationship of the proxy voting advice business that is material to addressing the objectivity of the proxy voting advice in light of the circumstances of the interest, transaction or relationship and (ii) any policies or procedures used to identify, as well as any steps taken to address, any such material conflicts of interest arising from such interest, transaction or relationship.

For more information on these rescinded rules, please see this Haynes and Boone alert.

Additional Electronic Filing Requirements

Beginning on January 11, 2023, electronic filing of the following documents is required under amendments to Rule 101 of Regulation S-T :

- Annual reports to security holders (the “glossy” annual reports).
  - Required to be filed on Edgar in PDF format, although online posting will be permitted also, but not to the exclusion of EDGAR filing.
  - Cannot otherwise be reformatted, re-sized or otherwise redesigned for Edgar filing.
  - Includes electronically submitting the Form 6-K glossy report for Foreign Private Issuers.
- Form 11-K for annual reports of employee benefit plans.
- Form 6-K for Foreign Private Issuers.
- Notices of exempt solicitations and preliminary roll-up communications.
- Various international bank filings.

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- Section 33 of the Investment Company Act filings.

For more information on electronic filing requirements, please see this Haynes and Boone alert.

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