Achieve with O'Melveny

Public Company Advisory Group Quarterly – Winter 2024/2025

January 2025

We are pleased to bring you our Winter 2024/2025 edition of Public Company Advisory Group Quarterly, a concise summary of the latest developments of interest to public companies. In this edition, we will focus on key items for public companies to consider for this year's annual reporting and proxy season, as well as other topics of interest to public companies.

SEC DISCLOSURE UPDATES

New Disclosure Requirements for the 2024 Annual Reporting Season

The following is a summary of disclosures that will be required for the first time for calendar-year end filers (i.e., filers with their fiscal year ending December 31, 2024):

Disclosure and Filing of Insider Trading Policies and Procedures (Item 408(b) / Item 601(b)(19) of Regulation S-K)

As discussed in our Summer 2024 Newsletter, public companies are now required to provide narrative disclosure relating to their insider trading policies and procedures in their Annual Report on Form 10-K and/or proxy statement and file as exhibits such policies and procedures to their Annual Report on Form 10-K.

- **Narrative Insider Trading Policies and Procedures Disclosure (Item 10 of Part III of Form 10-K / Item 7(b) of Schedule 14A):** Companies are required to disclose whether or not they have adopted policies and procedures "governing the purchase, sale, and/or other dispositions" of company securities that are "reasonably designed to promote compliance" by directors, officers and employees, as well as by the company, with applicable insider trading laws, rules, and regulations, and if not, to explain why they have not done so.

Practice Tip

While **"other dispositions" of company securities** (which would include gifts) and **company transactions in its own securities** (e.g., repurchases) are not covered in all insider trading policies, they are required to be discussed in the narrative disclosure. Companies should ensure that the language in their narrative disclosure captures all of the elements required by Item 408(b) of Regulation S-K.

Practice Tip

The Item 408(b) narrative insider trading disclosure is required in both a company's Form 10-K and the proxy statement for its annual meeting of stockholders. Companies that file their proxy statement within 120 days of fiscal year end may incorporate this disclosure required by Item 10 of Part III of Form 10-K (in addition to the other disclosures required by Part III of Form 10-K) by reference to their proxy statement, and do not also have to include the disclosure in their Form 10-K.

Practice Tip

Companies are required to tag the narrative insider trading disclosure in Inline XBRL in accordance with Rule 405 of Regulation S-T and the EDGAR Filer Manual.

Exhibit Disclosure (Item 15 of Form 10-K): Companies are required to file a copy of their insider trading policies and procedures (if any) as Exhibit 19 to the Form 10-K.

Practice Tip

The SEC has not offered guidance on what documents constitute a company's "insider trading policies and procedures." However, companies have been taking a narrow view of this definition and typically do not file internal materials such as trainings and FAQs under Exhibit 19.

Practice Tip

Item 408(b) does not impose prescriptive requirements on the content of a company's insider trading policies, nor does it require that a company's policies specifically address gifts or company repurchases. While it is increasingly common for insider trading policies to govern gifts of company securities by company insiders, it has been less common to date for companies to address company repurchases in their insider trading policy or in any formal separate policy.

Disclosure Concerning Timing of Option Awards (Item 402(x) of Regulation S-K)

Public companies are now required to provide narrative and tabular disclosures under Item 11 of Part III of Form 10-K and Item 8 of Schedule 14A regarding the timing of option awards in relation to the company's disclosure of material nonpublic information (MNPI).

The **narrative disclosure** describes company policies and practices governing the timing of awards of options in relation to the disclosure of MNPI by the company, including:

- How the board determines when to grant option awards (for example, whether such awards are granted on a predetermined schedule)
- Whether (and if so, how) the board or compensation committee takes MNPI into account when determining the timing and terms of an option award
- Whether the company has timed the disclosure of MNPI for the purpose of affecting the value of executive compensation

The **tabular disclosure** provides, on an award-by-award basis, details of option awards made to the company's named executive officers (NEOs) during the last completed fiscal year that were awarded beginning four business days before and ending one business day after the filing or furnishing of a (i) Form 10-K or 10-Q or (ii) Form 8-K that contains MNPI (the Covered Period), including:

Grant date of award	# of securities underlying the award	Exercise price of award ($/share)	Grant date fair value of award	% change in closing market price of securities underlying the award between the trading days ending immediately prior to and beginning immediately following the disclosure of MNPI

Practice Tip

The Item 402(x) disclosure is required in both a company's Form 10-K and the proxy statement for its annual meeting of stockholders. Companies that file their proxy statement within 120 days of fiscal year end may incorporate the Item 402(x) disclosure required by Item 11 of Part III of Form 10-K (in addition to the other disclosures required by Part III of Form 10-K) by reference to their proxy statement, and do not also have to include the disclosure in their Form 10-K.

Practice Tip

Companies are not required to make any disclosures pursuant to Item 402(x) if they do not grant option awards; however, a negative statement to that effect may still be helpful to avoid confusion. Similarly, the tabular disclosure required by Item 402(x) is only required if the company awarded options to NEOs during any Covered Period during the fiscal year, but negative disclosure may still be useful for companies who have nothing to disclose.

Practice Tip

Companies are required to tag the disclosure required by Item 402(x) in Inline XBRL in accordance with Rule 405 of Regulation S-T and the EDGAR Filer Manual.

New Inline XBRL Tagging Requirements for Cybersecurity and Pay versus Performance Disclosures

- Cybersecurity (Item 106 of Regulation S-K): Inline XBRL tagging for the cybersecurity disclosures required by Item 106 of Regulation S-K are required in a company's first Form 10-K for fiscal years ending on or after December 15, 2024 (which, for calendar-year end filers, is the FY 2024 Form 10-K).
- Pay versus Performance (New Requirement for Smaller Reporting Companies) (Item 402(v) of Regulation S-K): Smaller reporting companies are required to comply with inline XBRL tagging requirements for pay versus performance disclosure in the third filing in which they provide the disclosure.[1] Now that the disclosure requirement is in its third year, smaller reporting companies that have been complying with the rule since its effective date are required to provide the required inline XBRL data for their pay versus performance disclosure.

Disclosure and Governance Reminders for the 2024 Annual Reporting Season

The following summarizes other recent developments in disclosure and corporate governance practices.

SEC Comment Letters Received on Cybersecurity Disclosures (Item 106(b)-(c) of Regulation S-K)

As discussed in our Reference Guide, Item 106(b) and (c) of Regulation S-K require companies to disclose in Item 1C of Part I of Form 10-K details regarding their cybersecurity risk management and strategy, as well as board and management oversight of cybersecurity governance.

This is the second year that calendar-year end companies are required to provide these disclosures in their Form 10-K. Consistent with its approach to reviewing disclosures related to newly adopted rules "to assess compliance with the rules, provide guidance, and improve disclosures,"[2] the SEC issued targeted comment letters over the past year related to cybersecurity disclosures, highlighting common areas of non-compliance.

- *Identification and Description of Management and Committee Members Responsible for Assessing and Managing Cyber Risks*. The most common comment issued related to the requirement that companies disclose (i) the management positions or committees responsible for assessing and managing cybersecurity risks, and (ii) the relevant expertise of such persons or committee members. Common missteps included:

Describing executive committee or management roles that assist or support the chief information security officer (CISO) in assessing and managing cybersecurity risks, but only describing relevant experience of CISO

Noting that CISO coordinates with "key members of management" without identifying those members of management

Noting that senior leadership is responsible for management of cybersecurity risk, without discussing relevant expertise

In addition, companies should provide a description of each individual's relevant expertise (including time served in relevant roles) rather than aggregating the individual's experiences for purposes of the disclosure.

Practice Tip

Companies should ensure their disclosure on management's role in oversight of cybersecurity risks (required by Item 106(c)(2)(i) of Regulation S-K) includes specific information about each individual responsible for managing and assessing the company's cybersecurity risks. This includes identifying individuals by name and describing each individual's relevant expertise and experience (including dates).

- Third Party Service Providers. The SEC scrutinized disclosures regarding companies' use of third parties in connection with their cybersecurity risk management processes. The SEC flagged disclosures where there was no mention of third-party service providers, as well as where there was internal inconsistency regarding a company's use of third-party service providers (e.g., a statement that the company has not engaged third-party service providers alongside statements that the company's audit committee periodically receives reports from IT support specialists).
- Missing disclosures. Some companies omitted the Item 1C disclosure entirely. Companies should be aware that not only is the Item 1C cybersecurity disclosure required in Form 10-K, but they are now also required to provide the disclosures in Inline XBRL.

SEC Comment Letters Received on Pay versus Performance Disclosure (Item 402(v) of Regulation S-K)

The SEC issued more than thirty comment letters related to pay versus performance (PvP) disclosures in the second year in which such disclosures were required. The comment letters focused on reminding registrants of the rule's requirements and highlighted common errors in its application. Top areas of comment are highlighted below.

Calculation of compensation actually paid to NEOs. Companies are required to disclose in the PvP table the "compensation actually paid" to its principal executive officer (PEO) and the average "compensation actually paid" to its non-PEO NEOs, where "compensation actually paid" is calculated by adding and deducting certain amounts related to defined benefit and actuarial pension plan and stock and option awards from the executive's "total compensation" (as reported in the Summary Compensation Table).

- *Footnote individual calculation steps.* The SEC reminded companies that the required footnotes disclosing how the company arrived at compensation actually paid must include separate numerical amounts for each item deducted and added (without aggregating steps).
- *Footnote calculations for prior fiscal years if amounts in the table have been revised from prior disclosures.* Pursuant to Regulation S-K Compliance & Disclosure Interpretation Question 128D.03, after the first PvP disclosure companies are required to provide footnote disclosure of calculations to arrive at compensation actually paid for years other than the most recent fiscal year included in the PvP table only if it is material to an investor's understanding of the information in the PvP disclosure. The SEC clarified in comment letters that companies will need to include in the PvP table footnote calculations for any prior years where the amounts reported in the table for those years have changed since the last disclosure.
- *Calculating the change in fair value of equity awards granted in prior years that vested during the fiscal year.* The SEC issued comments to companies that incorrectly added the year-over-year change in fair value of the relevant awards rather than applying the formula set forth in the rule, which requires the change to be measured from the end of the prior fiscal year to the vesting date.

Calculation of company's net income. Companies are required to disclose in the PvP table their net income as reported in their audited GAAP financial statements. The SEC issued comments to companies that incorrectly disclosed (i) net (loss) earnings attributable to the registrant's shareholders, (ii) net income (loss) attributable to the registrant, and (iii) a figure that deducted earnings attributable to non-controlling interests.

Company-Selected Measure. Companies are required to disclose in the PvP table an amount attributable to the most important additional financial performance measure used by the company to link compensation actually paid to its NEOs to company performance (the Company-Selected Measure).

- *Use of non-GAAP measures.* The SEC reminded companies to include the calculations for how non-GAAP Company-Selected Measures are calculated from the company's audited financial statements. The reconciliation may not incorporate by reference a separate filing, but it can reference another section of the same document. Additionally, the Company-Selected Measure should be calculated consistently for each fiscal year presented in the PvP table—in at least one instance, the SEC noted that adjustments made to the non-GAAP Company-Selected Measure varied by year.
- *Only include one Company Selected Measure.* The SEC issued comments to companies that included more than one additional measure in the PvP table without identifying the Company Selected Measure. If a company chooses to include additional financial measures in the PvP table, it needs to clearly identify which one (and only one) is the Company Selected Measure.

Peer group total shareholder return (TSR). Companies are required to disclose in the PvP table the TSR of its peer group. The SEC reminded companies that the peer group used in the PvP table must match exactly the peer group used by the company in the compensation discussion and analysis (CD&A) section of its proxy statement or Item 5 of Form 10-K. Additionally, if a company changes its peer group from the immediately preceding fiscal year, (i) it should provide footnote disclosure of the reason(s) for the change and compare the cumulative total return of the current and preceding peer group; and (ii) provide the peer group TSR information for each year in the table using the most recent peer group.

Measurement point for TSR calculations. The SEC issued comments reminding companies that the TSR calculation is based on an initial fixed investment of $100 on the last trading day before the company's earliest fiscal year presented in the table (instead of the end of the fiscal year).

Relationship disclosure. Companies are required to provide a "clear description" of the relationships between (i) the compensation actually paid to its PEO and non-PEO NEOs and (ii) the company's (a) cumulative TSR, (b) net income, and (c) Company Selected Measure.

- *Relationship disclosure must be separate from the PvP table.* Even though the relationship disclosure compares amounts contained in the PvP table, the disclosure itself must be separate from the table (i.e., not a footnote to the table).
- *Narrative disclosure should include a description of all relationships required by Item 402(v)(5).* The SEC issued comments to companies that omitted a description of the comparisons between compensation actually paid and net income.
- *Description of relationship is not a recitation of amounts.* The SEC issued a comment letter to one company noting that simply reciting the amounts in the PvP table did not "clearly describe" the relationship between the amounts.
- *Not sufficient to state that no relationship exists.* The SEC noted that even if a particular measure is not used in setting compensation, Item 402(v)(5) still requires the company to describe the relationship between that measure and compensation actually paid.

Reminder on Requirements for Clawback Policy and Clawback Recovery Disclosures (Item 402(w) and Item 601(b)(97) of Regulation S-K)

As discussed in our Client Alert, since December 1, 2023, public companies have been required to comply with the SEC's final rules regarding recovery of erroneously awarded compensation (the Clawback Rules).

Exhibit Disclosure (Item 15 of Form 10-K): The Clawback Rules require public companies to adopt and file as Exhibit 97 to Form 10-K a policy regarding recovery of erroneously awarded compensation (a Clawback Policy) meeting the minimum coverage standards required by applicable stock exchange listing standards adopted pursuant to the Clawback Rules.[4] At a minimum, a company's Clawback Policy must be mandatorily triggered in the event of an accounting restatement due to material noncompliance with any financial reporting requirement. As discussed in our Fall 2024 Newsletter, these requirements are a floor and not a ceiling, and companies may in their discretion implement broader clawback policies than the minimum required by the rules. Companies should review whether updates were made to their filed Clawback Policy since it was last filed and, if so, include the updated version as an exhibit to the Form 10-K.

Restatement Disclosure (Item 11 of Part III of Form 10-K / Item 7(b) of Schedule 14A): The Clawback Rules require disclosure if (i) the company was required to prepare a covered accounting restatement at any time during the last completed fiscal year or (ii) there was an outstanding balance of erroneously awarded compensation as of the end of the last completed fiscal year to be recovered in connection with any prior restatement. Companies that file their proxy statement within 120 days of fiscal year end may incorporate the Item 402(w) disclosure required by Item 11 of Part III of Form 10-K (in addition to the other disclosures required by Part III of Form 10-K) by reference to their proxy statement and do not also have to include the disclosure in their Form 10-K.

Restatement Checkbox (Cover Page of Form 10-K): The Clawback Rules require companies to indicate by checkbox on the cover page of the Form 10-K whether (i) the company had to correct errors from previous financial statements and (ii) a corrected error prompted a clawback analysis.

Disclosures Required for Each Restatement

- The date the issuer was required to prepare a covered restatement.
- The total amount of erroneously awarded compensation attributable to the restatement (including details on how the amount was calculated), or if the amount has not yet been determined, an explanation as to why the determination has not been made.[5]
- The total amount of erroneously awarded compensation that has yet to be clawed back at the end of the last completed fiscal year (including names of individuals for whom erroneously awarded compensation has remained outstanding for 180 or more days and the clawback amount owed by such individual).
- If, in the limited circumstances provided in Rule 10D-1(b)(1)(iv) under the Securities Exchange Act of 1934, as amended (the Exchange Act), the compensation committee (or, if applicable, a majority of independent directors) determines clawback recovery would be impracticable following the restatement, the amount of recovery foregone and a brief description of the reasons the company did not pursue a clawback (for each NEO and for all other executive officers as a group).
- If the company concluded that its Clawback Policy does not require a clawback following a restatement, a brief explanation about why the policy resulted in that conclusion.

Risk Factors

Annual Review of Risk Factor Topics. Companies should conduct an annual review of their risk factors in Item 1A of Form 10-K to ensure that they reflect current and emerging risks. Although relevant topics will vary based on a company's specific circumstances (industry, markets, geography, etc.), companies may want to consider the following topics:

Risks related to the use of AI by the company or third parties	Risks related to the change in presidential administration (e.g., tariffs)	Risks of continuing and emerging geopolitical conflicts (e.g., Ukraine, Israel, Syria)
Cybersecurity risks	Risks related to inflation and changes to interest rates	Other risks specific to the company's industry and geography

Consideration of Risks That Have Materialized. The SEC and investors have recently pursued legal action against companies for framing risk factors as hypothetical or generic when the companies knew the warned-of risks had already materialized.[6] Thus, companies should review and update existing risk factors to reflect events or circumstances that have already occurred. In June 2024 the Supreme Court granted certiorari in *Facebook, Inc. v. Amalgamated Bank* to address a three-way circuit split concerning whether public companies must disclose in the "Risk Factors" section of the Form 10-K instances where a risk has materialized in the past,[7] but dismissed the writ of certiorari as improvidently granted shortly after hearing oral arguments. Absent a high court ruling, we expect that this will be a continued area of litigation and enforcement activity. Companies should accordingly carefully review their risk factors to determine whether any of the disclosed risks have materialized and, if so, consider whether such event should be disclosed within the risk factor.

Form 10-K Exhibits

New Exhibit Requirements. As discussed above, companies now need to include their insider trading policies and procedures and Clawback Policy as Exhibit 19 and Exhibit 97 to the Form 10-K, respectively.

Exhibit Index. Companies should review their exhibit index to ensure that it captures all required exhibits, including (i) exhibits filed as an exhibit to a Form 10-Q or Form 8-K during the fiscal year, (ii) material contracts described in but not filed as exhibits to a Form 8-K, and (iii) immaterial amendments to previously filed material contracts. Companies may also remove from the exhibit list any exhibits that are no longer required to be filed, including expired or terminated material contracts for which there are no continuing obligations.

Exhibit 4 Description of Securities. Companies should review their Description of Securities required under Item 601(b)(4)(vi) of Regulation S-K to ensure that it remains accurate with respect to each class of the company's securities that is registered under Section 12 of the Exchange Act. Corporate events that could trigger an update to this exhibit include (but are not limited to) issuances of additional securities or classes of securities or material changes to previously issued shares (such as by stock split, reverse stock split or otherwise).

Exhibit 21 List of Subsidiaries. Companies should review the list of subsidiaries required under Item 601(b)(21) of Regulation S-K. As a reminder, companies may omit the names of particular subsidiaries if the unnamed subsidiaries, considered in the aggregate as a single subsidiary, would not constitute a "significant subsidiary" (as defined in Rule 1-02(w) of Regulation S-X) as of the end of the fiscal year covered by the Form 10-K.

Exhibit 22 List of Subsidiary Guarantors. Companies should review and update the list of subsidiary guarantors required under Item 601(b)(22) of Regulation S-K to ensure that the exhibit accurately reflects any guaranteed debt that was offered and sold on a registered basis under the Securities Act of 1933, as amended, that remains outstanding.

Exhibit 23 Auditor Consents. Companies should review and update the consent of their independent registered public accounting firm required under Item 601(b)(23) of Regulation S-K (Consents of Experts and Counsel) to ensure that the consent correctly references all current registration statements into which the company's financial statements are being incorporated (e.g., Forms S-3 and S-8).

D&O Questionnaire

To the extent not already addressed, companies should consider the following updates to their Directors and Officers Questionnaires (D&O Questionnaires) in response to recent litigation, rulemaking, and enforcement actions.

- Director Independence – Close Personal Relationships. As discussed in our Fall 2024 Newsletter, in September 2024 the SEC announced settled charges against a public company's former CEO for misrepresenting his status as an independent director by failing to disclose a close personal friendship that had developed between himself and a company executive. In light of this enforcement action, companies should review questions in their D&O Questionnaire relating to director independence to ensure that the questionnaire sufficiently probes whether an independent director has any material relationships with the company or management that could impair a director's independence under the relevant listing rules.
- Board Diversity. As discussed in our Client Alert, on December 11, 2024, the full Fifth Circuit Court of Appeals vacated the approval by the SEC of two Nasdaq rules relating to corporate board diversity disclosures. As a result of this decision, Nasdaq-listed companies are no longer required to collect and report on their board diversity statistics, including the requirement to summarize board diversity composition in a standardized table format. Companies may still choose to include a board diversity question in their D&O Questionnaire; however, they now have leeway in how they collect and whether they choose to report on the information collected.
- Board AI and Cyber Expertise. If a company utilizes its D&O Questionnaire to collect information about the skills and qualifications of members of its board of directors, a company should consider enhancements to the list of skills to determine whether any member of the company's board of directors possesses specific expertise (including through work experience, education, certification, or other means) relating to AI, cybersecurity, or other topics of board focus.
- Universal Proxy. In light of the universal proxy rules, companies should ensure that they obtain a director's consent to be named in any proxy materials, not just the company's.

Artificial Intelligence Disclosures in SEC Filings

Companies should consider on an ongoing basis how generative artificial intelligence (AI) is impacting their business and/or industry. To the extent a company's or a third party's use of AI becomes material to the company's business or financial condition, it should consider adding appropriate disclosures under Item 1 (Business), Item 1A (Risk Factors), Item 7 (Management's Discussion & Analysis) or another appropriate section of the Form 10-K.

The outgoing SEC Chair Gary Gensler and Erik Gerding, the former Director of the SEC's Division of Corporation Finance, have both publicly spoken on the importance of tailored AI disclosures (these were discussed in our Summer 2024 Newsletter and Fall 2024 Newsletter). Based on these statements, companies should consider the following with respect to AI disclosures:

Is AI disclosure required under the securities laws?
AI disclosure may be required under the securities laws if AI usage by the company or by third parties is material to the company's business or to investors. The company should consider the materiality of AI to its business, especially if it is discussing AI in earnings call or in extensive discussions with its board of directors.

How should the company describe its use of AI?
Companies should clearly define what they mean by "artificial intelligence" or "generative AI" and specify how the technology can improve (or harm) its results of operations, financial condition, and future prospects. Companies should have a reasonable basis for any claims they make about the use of AI.

Both Chair Gensler and former Director Gerding warned companies against focusing on AI “buzz” not directly relating to their business.

Although the SEC is expected to undergo significant turnover in connection with the change in presidential administration on January 20, 2025 (as we discuss in the next section)[8] and future agency leadership and SEC priorities are still unknown at this time, it is expected that AI will remain an important area of focus for this reporting season and going forward.

ADMINISTRATION CHANGES AT THE SEC

When the U.S. presidential election results in a political party flip, as was the case in 2024 when Republican Donald Trump won over Democratic incumbent Vice President Kamala Harris, the SEC has historically experienced changes to its leadership, rulemaking, enforcement priorities and focus areas. The following summarizes our current expectations as to what to expect from the SEC in this year of transition and for the upcoming administration.

- **Chair and Leadership.** The SEC announced on November 21, 2024, that Chair Gensler will step down from the SEC on January 20, 2025, as is customary for SEC chairs to do when the incoming U.S. president is from the opposite political party. President-elect Trump has tapped Paul Atkins to chair the SEC. We expect Atkins, with his significant prior SEC experience as Commissioner from 2002 through 2008 and also having served as counsel to SEC Chairs Richard C. Breedan and Arthur Levitt, to bring an “institutionalist” perspective as well as a somewhat contrasting free-market and pro-business perspective as he continues the historical trend when a new administration takes over of redirecting the SEC’s priorities and focus areas. Further leadership changes, including the departure of Erik Gerding, former Director of the Division of Corporation Finance, on December 31, 2024, evince potentially significant changes to come.
- **Rulemaking.** The SEC under Chair Gensler prioritized significant rulemaking, requiring new and enhanced disclosures by public companies on various governance topics, including its landmark climate rules, as well as cybersecurity and insider trading rules. We anticipate that the most significant differences for an Atkins-led SEC from outgoing Chair Gensler’s regulatory agenda may relate to fewer (or less restrictive) SEC rule-based mandates regarding climate, ESG or cybersecurity matters, as well as the possibility of cryptocurrency-friendly rulemaking activities.
- **Enforcement.** While Chair Gensler’s SEC enforcement priorities included cryptocurrency and off-channel communications, we expect that an Atkins-led SEC will be more focused on pursuing cases involving traditional fraud, Foreign Corrupt Practices Act cases, and misconduct by financial professionals (though that does not mean that Atkins will limit the agency to more traditional cases—during his six-year tenure as a Commissioner under Republican administrations, the SEC brought scores of significant cases, often in “new” areas such as stock options backdating and mutual fund market timing). It is also possible that an Atkins-led SEC may take a less aggressive stance toward most corporate penalties and industry sweeps. Based on Atkins’ prior public statements regarding cryptocurrency, many expect fewer SEC enforcement matters that related to non-fraud-based cryptocurrency securities law violations (e.g., Section 5 of the Exchange Act and broker-dealer registration).

CORPORATE GOVERNANCE

ISS and Glass Lewis Announce 2025 Benchmark Policy Updates

Institutional Shareholder Services Inc. (ISS) and Glass, Lewis & Co. (Glass Lewis), the two largest proxy advisory firms, have released their 2025 updates to their respective benchmark proxy voting policies. Institutional investors, which typically make up a large portion of public company outstanding share ownership, often rely on the ISS and Glass Lewis benchmark policies to inform how they vote on matters at a company’s annual meeting.

ISS’s voting policy updates were relatively minor for 2025, with changes from Glass Lewis likely having more relevance in the upcoming proxy season. The following summarizes the notable ISS and Glass Lewis voting policy changes for 2025.

ISS 2025 Proxy Voting Guidelines – United States[9]

Short-Term Poison Pills	ISS clarified the factors that it will consider on a case-by-case basis when evaluating whether a board's adoption of a short-term poison pill is reasonable or a "governance failure warranting a recommendation to vote against directors." The factors for consideration included in the update are already considered by analysts, but they are now spelled out in the proxy voting guidelines to increase transparency.
SPACs – Proposals for Extensions	Instead of voting on a case-by-case basis, ISS will now generally support requests to extend a special purpose acquisition company (SPAC) termination date by up to one year (accounting for prior extension requests). ISS may consider additional factors, such as added incentives, business combination status, other amendment terms, and, if applicable, use of money in the trust fund to pay excise taxes on redeemed shares.
Shareholder Proposals – Environment or Social Impact Reports	ISS will still vote on a case-by-case basis for shareholder proposals regarding reports on policies and/or the potential environmental and/or social impacts of company operations. However, in light of the development of nature-related reporting frameworks, ISS will now consider as a factor in their analysis the alignment of a company's current disclosures with "relevant broadly accepted reporting frameworks."[10] Previously, ISS considered a company's current disclosures without reference to these frameworks.

Glass Lewis 2025 Benchmark Policy Guidelines[11]

AI	Glass Lewis will generally not make voting recommendations on the basis of a company's AI-related oversight or disclosures. Glass Lewis may, however, recommend voting against "appropriate" directors if there is evidence of insufficient company oversight and/or management of AI technologies that results in material harm to shareholders. In that case, Glass Lewis will review company practices and disclosures, as well as the board's and management's response to the issue, and determine whether the board's oversight, response or disclosure concerning AI-related issues is insufficient.
Treatment of Unvested Awards in a Change-in-Control	Glass Lewis believes that companies that give board committees discretion over the treatment of unvested awards should also provide "clear rationale for how such awards are treated in the event a change in control occurs."
Board Responsiveness to Shareholder Proposals	Glass Lewis expects the board of directors to engage with shareholders on proposals that received "significant" support (generally more than 30% but less than the required majority of votes cast), and to provide disclosure addressing shareholder concerns and the board's outreach initiatives.
Reincorporation	Glass Lewis generally defers to board determinations on a company's appropriate jurisdiction of incorporation. For 2025, Glass Lewis clarified that it will review proposals to reincorporate to a different state or country on a case-by-case basis. The review will include changes in corporate governance provisions, differences in corporate statutes and legal precedents, and relevant financial benefits, resulting from the change in domicile.
Say-on-Pay	Glass Lewis added language emphasizing its holistic approach to analyzing executive compensation programs, noting that, except for "particularly egregious pay decisions and practices," no one factor would ordinarily be determinative. Unfavorable factors will be analyzed in the context of rationale, overall structure, overall disclosure quality, the compensation program's ability to align executive pay with performance and shareholder experience, and the "trajectory of the pay program resulting from changes introduced by the compensation committee."
Long-Term Incentives	Glass Lewis added "post-vesting holding periods" to its list of what it believes are elements of a well-structured long-term incentive plan.

BlackRock Removes Diversity Requirements from Proxy Voting Guidelines

BlackRock Investment Stewardship (BIS) updated its proxy voting guidelines for Benchmark Policies to remove references to board diversity in its consideration of board composition. Under the new policy, which became effective in January 2025, instead of diversity, BIS is now interested in seeing "a variety of experiences, perspectives, and skillsets in the boardroom."

In addition, BIS no longer expects companies to disclose how diversity (including both professional and demographic characteristics) is considered in board composition or whether it considers a diverse slate of candidates for all available board nominations.

Although BIS removed language encouraging large (i.e., S&P 500) companies to aspire to have at least 30% of its members be diverse, BIS noted that 98% of S&P 500 companies currently meet that diversity threshold and added language that it may recommend votes against members of the nominating/governance committee of S&P 500 companies that are outliers with respect to having a "mix of professional and personal characteristics" on their boards.

Institutional Investors Expand Pass-Through Voting Programs

Traditionally, investors in equity funds have voted their shares in accordance with the guidelines adopted by each fund's board. In recent years, however, institutional investors have been experimenting with programs that give investors more options for voting shares in accordance with investor preferences.

Since 2022, three of the largest asset management firms in the United States—BlackRock, Inc., The Vanguard Group, Inc., and State Street Global Advisors—have offered "voting choice" programs to investors in eligible funds. Participating investors in these programs can choose to vote their shares in accordance with specified voting policies offered by proxy advisors (e.g., ISS, Glass Lewis, and Egan-Jones Proxy Services (Egan-Jones)) instead of in accordance with the fund's preference.

- State Street Global Advisors' proxy voting choice program allows investors in its equity index funds (covering 80% of eligible index equity assets it manages) to choose from one of the seven voting policies offered through ISS or to vote with the portfolio company board's recommendation.[12]
- The BlackRock Voting Choice program allows investors in certain institutional pooled vehicles (representing 50% of the assets held by Blackrock's total index equity clients) to choose from voting policies offered through ISS, Glass Lewis and Egan-Jones.[13]
- The Vanguard Investor Choice program allows investors in certain Vanguard funds to choose from one of five voting policy options, including a company board-aligned policy, a "mirror" voting policy (to vote shares in approximately the same proportions as votes cast by other shareholders at the annual meeting), and both an ESG (through Glass Lewis) and "anti-ESG" (through Egan-Jones) voting policy.

Although access to voting choice is growing, uptake among eligible investors is currently low. BlackRock reported that as of June 28, 2024, its clients exercised voting choice for 23% of the assets under management eligible to participate in the program, while Vanguard reported that 2% of eligible shareholders (representing 40,000 investors) participated in their Investor Choice pilot program during the 2024 proxy season (the 2024 Investor Choice Pilot).

Still, the growth of investor choice has the potential to make a difference in how institutional shares are voted during the proxy season. According to a Vanguard report on the results of its 2024 Investor Choice Pilot (which allowed investors in five eligible index funds to choose from one of four voting policy options):[14]

- Around 45% of investors in each of four of the five eligible funds[15] opted to vote their shares in accordance with the Vanguard-Advised Funds Policy, which is also the default option for investors who did not participate in the pilot, while approximately 30% and 20% of investors opted to vote their shares in accordance with the company board-aligned policy and the ESG policy, respectively.
- Nearly 80% of investors in the fifth eligible fund, the Vanguard ESG U.S. Stock ETF, chose to vote their shares in accordance with the ESG policy.

While voting choice programs are still nascent, they are expected to increase uncertainties about how shares held by these large institutional investors will be voted at a company's annual meeting and may complicate shareholder engagement efforts.

En Banc 5th Circuit Vacates SEC's Approval of Nasdaq Board Diversity Rule

As discussed in our Client Alert and as mentioned above in this newsletter, on December 11, 2024, the full Fifth Circuit Court of Appeals vacated (by a 9-8 vote) the approval by the SEC of Nasdaq rules requiring listed companies to meet certain board diversity requirements (or disclose their reasons for failing to comply with the requirements) and to disclose a company's board diversity statistics on a standardized template.

With this ruling and expectations that it will not be appealed, Nasdaq will no longer require companies to collect diversity information from their boards of directors or report the statistics on their Form 10-K, in their proxy statement, or on their website. However, companies may still voluntarily collect and report on this information, either to comply with separate state law requirements, internal board composition goals, or to respond to requests from institutional or other investors.

California Climate Rule Updates

As discussed in our Fall 2024 Newsletter, on September 27, 2024, California Governor Gavin Newsom signed into law amendments to two California laws imposing climate-related reporting requirements on companies operating in California that meet certain financial thresholds (together, the California Climate Disclosure Laws). The amendments did not change the deadlines for reporting under the California Climate Disclosure Laws, which will be required starting in 2026.

As discussed in our Client Alert, on December 5, 2024, the California Air Resource Board (CARB), which is the agency tasked with promulgating regulations under the California Climate Disclosure Laws, issued an Enforcement Notice stating that it would exercise its enforcement discretion "such that, for the first report due in 2026, reporting entities may submit scope 1 and scope 2 emissions from 'the reporting entity's prior fiscal year' that can be determined from information the reporting entity already possesses or is already collecting" as of December 5, 2024. The Enforcement Notice goes on to state that "for the first reporting cycle, CARB will not take enforcement action for incomplete reporting against entities, as long as the companies make a good faith effort to retain all data relevant to emissions reporting for the entity's prior fiscal year."

1 Item 402(v)(7)-(8) of Regulation S-K.

2 Erik Gerding, *The State of Disclosure Review,* Sec. & Exch. Comm'n: Speeches and Statements (June 24, 2024), https://www.sec.gov/newsroom/speeches-statements/gerding-statement-state-disclosure-review-062424.

3 Item 106(c)(2)(i) of Regulation S-K.

4 Exchange Act Rule 10D-1; NYSE Listed Company Manual 303A.14; Nasdaq Listing Rule 5608. The Clawback Policy should apply to all incentive-based compensation received by executive officers after October 2, 2023.

5 Once determined, disclosure must be made in the next filing that is subject to Item 402 of Regulation SK.

6 See Check Point Software Technologies Ltd., Exchange Act Release No. 101, 399 (Oct. 22, 2024), https://www.sec.gov/files/litigation/admin/2024/33-11321.pdf; Unisys Corp., Exchange Act Release No. 101,401 (Oct. 22, 2024), https://www.sec.gov/files/litigation/admin/2024/33-11323.pdf. *See also* Craig v. Target Corp, No. 2:23-cv-00599 (M.D. Fla. Dec. 4, 2024) (order denying Target's motion to dismiss).

7 Petition for Writ of Certiorari, Facebook v. Amalgamated Bank, No. 23-980 (Sup. Ct. Mar. 4, 2024) ("The Sixth Circuit holds that companies need not disclose past instances when a risk has materialized. The First, Second, Third, Fifth, Tenth, and D.C. Circuits hold that companies must disclose that a risk materialized in the past if the company knows that event will harm the business. The Ninth Circuit here adopted a third, outlier position requiring companies to disclose that a risk materialized in the past even if there is no known threat of business harm.").

8 See, e.g., SEC Chair Gensler to Depart Agency on January 20, SEC Release No. 2024-182 (Nov. 21, 2024), https://www.sec.gov/newsroom/press-releases/2024-182; SEC Announces Departure of Corporation Finance Division Director Erik Gerding, SEC Release No. 2024-200 (Dec. 13, 2024), https://www.sec.gov/newsroom/press-releases/2024-200. See also Alex Veiga, Trump nominates cryptocurrency advocate Paul Atkins as SEC chair, Associated Press, Dec. 4, 2024, https://apnews.com/article/sec-chair-atkins-gensler-investors-financial-markets-d1c544f1846071b33c75b9f2dd0c1ba4.

9 Institutional Shareholder Services, Proxy Voting Guidelines – Benchmark Policy Changes for 2025: U.S., Canada, and Americas Regional (Dec. 17, 2024), https://www.issgovernance.com/file/policy/active/updates/Americas-Policy-Updates.pdf (ISS 2025 Updates).

10 Frameworks include, for example, the Taskforce on Nature-related Financial Disclosures (TNFD) and Kunming-Montreal Global Biodiversity Framework (GBF). See ISS 2025 Updates at 9.

11 Glass Lewis, *2025 Benchmark Policy Guidelines* – United States, https://resources.glasslewis.com/hubfs/2025%20Guidelines/2025%20US%20Benchmark%20Policy%20Guidelines.pdf.

12 State Street, *State Street Global Advisors to Extend Proxy Voting Choice to ETFs and Mutual Funds* (May 22, 2023), https://investors.statestreet.com/investor-news-events/press-releases/news-details/2023/State-Street-Global-Advisors-to-Extend-Proxy-Voting-Choice-to-ETFs-and-Mutual-Funds/default.aspx.

13 BlackRock, *BlackRock Expands Voting Choice Through New Egan-Jones Voting Guidelines and Customization* (June 11, 2024), https://www.blackrock.com/corporate/newsroom/press-releases/article/corporate-one/press-releases/blackrock-expands-voting-choice.

14 Vanguard, *Vanguard Investor Choice – About Investor Choice*, https://corporate.vanguard.com/content/corporatesite/us/en/corp/how-we-advocate/investment-stewardship/investor-choice.html (accessed Dec. 19, 2024).

15 The four funds were: the Vanguard S&P 500 Growth Index Fund, Russell 1000 Index Fund, Mega Cap Index Fund, and Dividend Appreciation Index Fund.

***

This memorandum is a summary for general information and discussion only and may be considered an advertisement for certain purposes. It is not a full analysis of the matters presented, may not be relied upon as legal advice, and does not purport to represent the views of our clients or the Firm. Shelly Heyduk, an O'Melveny partner licensed to practice law in California; Robert Plesnarski, an O'Melveny partner licensed to practice law in the District of Columbia and Pennsylvania; Pia Kaur, an O'Melveny counsel licensed to practice law in California, New York, and Texas; Ashley Gust, an O'Melveny counsel licensed to practice law in New York; Aliza Cohen, an O'Melveny resource attorney licensed to practice law in California; and Chloe K. Keedy, an O'Melveny associate licensed to practice law in California, contributed to the content of this newsletter. The views expressed in this newsletter are the views of the authors except as otherwise noted.