January 12, 2016

2015 U.S. Legal and Regulatory Developments

The following is our annual summary of significant U.S. legal and regulatory developments during 2015 of interest to Canadian companies and their advisors.

1. SEC to Re-Propose Resource Extraction Payment Disclosure Rules

On December 11, 2015, the SEC voted 3-1 to re-propose resource extraction rules requiring issuers to disclose payments made to the U.S. federal government or foreign governments for the commercial development of oil, natural gas or minerals. The original Rule 13q-1 implemented the requirements of Section 13(q) added to the Securities Exchange Act of 1934, as amended (the "Exchange Act"), by Section 1504 of the Dodd-Frank Wall Street Reform and Consumer Protection Act (the "Dodd-Frank Act") but was vacated by the U.S. District Court for the District of Columbia after a challenge by the American Petroleum Institute, the U.S. Chamber of Commerce and two other industry groups in 2013.

Under the new Rule 13q-1, an SEC reporting issuer (domestic or foreign) that is required to file annual reports on Form 10-K, 20-F or 40-F under the Exchange Act and that is engaged in the commercial development of oil, natural gas or minerals would be required to disclose in a Form SD filed annually any payment made to the U.S. federal government or a foreign government that is not de minimis and is one of the types of payments specified in the rules (taxes, royalties, fees, production entitlements, bonuses and other material benefits), including any payment by a subsidiary or entity controlled by the issuer. Control would be determined by reference to financial consolidation principles that the issuer applies to its audited financial statements in Exchange Act annual reports. As well, "de minimis" is defined as any payment, whether a single payment or a series of related payments, which does not equal or exceed U.S. $100,000 during the same fiscal year. The proposed rules do not provide for an exemption where disclosure is prohibited by other countries, which the Court found to be arbitrary and capricious in the original rules. However, the proposing rules release did note that the SEC could provide relief on a case by case basis. Voting on the adoption of the final rule is expected to take place in June 2016.

For a more detailed summary of background and re-proposed Rule 13q-1, see the Paul, Weiss memorandum at: http://www.paulweiss.com/media/3290960/17dec15securitiesalert.pdf.

For the text of the re-proposed rule, see: http://www.sec.gov/rules/proposed/2015/34-76620.pdf.

2. FAST Act Improves JOBS Act and Other Rules

On December 4, 2015, the Fixing America's Surface Transportation Act (the "FAST Act") was signed into law. The FAST Act includes several provisions that improve upon the accommodations made for emerging growth companies ("EGCs") under the 2012 Jumpstart Our Business Startups Act (the "JOBS Act"). It also codifies the so-called "Section 4(1½)" legal framework for private resales of restricted securities and provides for simplification of certain disclosure requirements.

Below is a list of particularly significant developments:

- Reduces the number of days before a roadshow that an IPO registration statement for an EGC must be publicly filed from 21 to 15;
- Allows an issuer that was an EGC when it submitted or filed its registration statement but afterwards ceases to be an EGC to continue to be treated as an EGC until the IPO is completed;
- Allows EGCs not to submit financial information for historical periods that would otherwise be required by Regulation S-X in a registration statement under confidential review, as long as the information will not be required to be included in the Form S-1 or F-1 when the offering is consummated;
- Codifies the "Section 4(1½) exemption" as a new Section 4(a)(7) under the Securities Act of 1933 (the "Securities Act"), exempting from registration resale transactions where there is no direct placement by an issuer, no general solicitation, participation only by accredited investors and provision of certain basic financial and other information. Securities offered pursuant to Section 4(a)(7) must be part of a class that has been outstanding for more than 90 days;
- Requires the Securities and Exchange Commission (the "SEC") to make changes to Form 10-K to allow "Summary pages" to cross-reference to more complete disclosure and Regulation S-K to ease the burden on smaller companies and eliminate duplicative or unnecessary items for all companies within 180 days;
- Requires the SEC to perform a study on the modernization of Regulation S-K within 360 days; and
- Requires the SEC to revise Form S-1 within 45 days to permit forward incorporation by reference.

For more a more detailed summary of the new FAST Act developments, see the Paul, Weiss memorandum at: http://www.paulweiss.com/media/3279495/9dec15sec.pdf.

For the text of the FAST Act, see: https://www.gpo.gov/fdsys/pkg/BILLS-114hr22enr/pdf/BILLS-114hr22enr.pdf.

3. Delaware Supreme Court Affirms *Rural/Metro* Decision

On November 30, 2015, the Delaware Supreme Court (the "DSC") issued a long-awaited decision in *RBC Capital Markets* v. *Joanna Jervis*, which affirmed the holdings by the Delaware Court of Chancery (the "DCC") in *In re Rural/Metro Corp. S'holder Litig*. concerning the duty of care of directors in the sale of a company.

The DSC held that where directors breach their fiduciary duties under *Revlon* by engaging in conduct outside of the range of reasonableness, such breach is a sufficient basis for third-party aiding and abetting liability, even if the underlying breach would not result in monetary liability for directors. The DSC further held that a board may still consent to a conflict but it must then be "especially diligent" in overseeing the conflicted advisor in the sale process and that the advisor must not act in its self-interest or to the detriment of its client, regardless of the consent. The DSC also affirmed that where a third party knows the board is breaching its duty of care and participates in the breach by misleading the board and creating an "informational vacuum," the third party can be liable for aiding and abetting.

Overall, the holdings reaffirm that directors must be active in ensuring they are informed during a sale process and inquire into potential conflicts that may impact the sale process. As well, the holdings make clear that aiding and abetting liability claims remain a possible risk against which financial advisors should protect, including by fully disclosing to the board all material conflicts.

For a more detailed summary of the decision, see the Paul, Weiss memorandum at: http://www.paulweiss.com/media/3270522/2dec15m_aalert.pdf.

4. 2016 ISS and Glass Lewis Voting Policy Updates

In November, 2015, the two largest U.S. proxy advisory firms, Institutional Shareholder Services (ISS) and Glass Lewis, issued their respective voting policies for the upcoming proxy season. Of particular interest are the developments regarding policies related to director overboarding, defensive structures and shareholder proposals.

Both ISS and Glass Lewis have stated that starting with the 2017 proxy season, they will recommend against directors who sit on more than five public company boards (instead of six under their current policies). ISS and Glass Lewis have also stated that directors who are public-company CEOs and sit on more than two public-company boards in addition to their own board will continue to receive negative recommendations at the boards of the public companies other than their own, in the case of ISS, and will be noted as a concern starting this proxy season, in the case of Glass Lewis.

ISS has also adopted a separate methodology for evaluating amendments to a company's bylaws or charter designed to implement defensive structures that are put in place prior to or in connection with a company's IPO. It will now consider the provision's impact on shareholders' ability to change the governance structure in the future, whether there is a classified board and whether there is a public commitment to put the provision to a shareholder vote within three years of the IPO. ISS also now explicitly states it will continue to consider any such unilateral adoption of bylaws or charter amendments that are materially adverse to shareholder rights in making vote recommendations for director nominees until the amendments are reversed or submitted to a binding shareholder vote.

In addition, Glass Lewis has outlined its approach to analyzing conflicting shareholder proposals that are excludable under Rule 14a-8(i)(9) of the Exchange Act against the backdrop of notable controversy last proxy season arising from the interpretation of that rule by the SEC's Division of Corporation Finance in the case of Whole Foods and its updated guidance under Staff Legal Bulletin No. 14H, which says a shareholder proposal directly conflicts with a management proposal only if a reasonable shareholder could not logically vote in favor of both proposals. Glass Lewis' outlined approach to analyzing conflicting shareholder proposals includes giving consideration to the nature of the underlying issue, the benefit to shareholders from implementing the proposal, the materiality of the differences between shareholder and management proposals, the appropriateness of the provisions in the context of a company's shareholder base, corporate structure and other relevant circumstances and a company's overall governance profile.

For a more detailed summary of these updates, see the Paul, Weiss memorandum at: http://www.paulweiss.com/media/3263695/23nov15secalert.pdf.

For the ISS policy updates, see: http://www.issgovernance.com/policy-gateway/2016-policy-information/.

For the Glass Lewis policy updates, see: http://www.glasslewis.com/guidelines/.

5. Delaware Court Rulings Provide Guidance on Standard of Review in Merger-Related Actions

On October 2, 2015, the DSC held in *Corwin* v. *KKR Financial Holdings LLC* that where there is a merger without a controlling stockholder, or in another situation where entire fairness review does not apply, a transaction that is approved by a fully-informed, uncoerced vote of disinterested stockholders, even where statutorily required, will invoke the business judgment rule, rather than the *Revlon* or *Unocal* standards of review.

In late October, the DCC issued opinions clarifying the decision. In *In re Zale Corporation Stockholders Litigation,* the DCC held that once the vote has shifted the standard of review to the business judgment rule, a complaint must contain well-pleaded allegations of facts that the directors were "grossly negligent" in order to successfully make a claim for breach of the fiduciary duty of care, a higher threshold than under the "range of reasonableness" in *Revlon*. In *In re Tibco Software Inc.*, the DCC found that a target board's failure to make basic inquiries after discovering an error in the count of outstanding shares that resulted in a reduction in consideration payable to the target of $100 million raised litigable questions as to whether the board acted in a grossly negligent manner. In addition, the DCC held in *Espinoza* v. *Zuckerberg* that only a formal vote or written consent of the majority of disinterested stockholders that complies with the technical requirements for stockholder action under the Delaware General Corporation Law (the "DGCL") will be effective to shift the standard of review.

For more a more detailed summary of the *KKR* ruling, see the Paul, Weiss memorandum at: http://www.paulweiss.com/media/3185869/8oct15m_aalert.pdf.

For more a more detailed summary of the *In re Zale*, *In re Tibco* and *Espinoza* rulings, see the Paul, Weiss memorandum at: http://www.paulweiss.com/media/3220038/3nov15m_aalert.pdf.

6. Delaware Court of Chancery Provides Guidance on Disclosure-only Settlements in M&A Litigation

On September 17, 2015, the DCC issued an opinion approving a disclosure-only settlement where a large range of claims were released, but said that in the future it may not accept such releases.

In *In Re Riverbed Technology Inc. Stockholders Litigation,* Riverbed Technology Inc. was acquired by third parties and shareholder plaintiffs brought a suit alleging the transaction undervalued the company and that the proxy documents did not disclose all material information about alleged financial advisor conflicts. In the settlement, the acquirers agreed to make certain supplemental disclosures relating to the financial advisor's relationship with the acquirers, the plaintiffs released all potential and federal state claims, and both parties agreed that the acquirers would not oppose a fee requested by the plaintiffs of $500,000. While the DCC accepted the broad release in the settlement largely because the stockholder class's federal and state claims being given up were not particularly viable and the parties had negotiated the remedy in good faith, the DCC noted that the release was "troubling" and that if it were not for the reasonable reliance of the parties on that type of settlement, "the interest of the [plaintiff] Class might merit rejection of a settlement encompassing a release that goes far beyond the claims asserted and the results achieved."

For a more detailed discussion of the *In Re Riverbed* decision, see the Paul, Weiss memorandum at: http://www.paulweiss.com/media/3157699/28sept15m_aalert.pdf.

7. SEC Issues Guidance on General Solicitation and General Advertising

On August 6, 2015, the SEC issued new compliance and disclosure interpretations regarding general solicitation and general advertising and a no-action letter regarding pre-existing, substantive relationships in the context of a private offering made in reliance on Rules 502(c) and 506(b) of Regulation D under the Securities Act.

Of note, the SEC clarified that an issuer's public website reflecting factual business information, including information about the issuer, its business, financial condition, products or services but not including predictions, projections or opinions about the value of a security, does not constitute a general solicitation or general advertising.

In addition, the SEC guidance elaborates on the meaning of a "pre-existing, substantive relationship" with a prospective investor required to demonstrate the absence of a general solicitation. Its guidance makes it clear that a pre-existing substantive relationship can be established indirectly and not only through registered broker-dealers or registered investment advisors (e.g., a pension consultant).

For a more detailed summary of the SEC's guidance, see the Paul, Weiss memorandum at: http://www.paulweiss.com/media/3091881/12aug15alert.pdf.

For the above-mentioned C&DIs, see:

- http://www.sec.gov/divisions/corpfin/guidance/securitiesactrules-interps.htm#256.23.
- http://www.sec.gov/divisions/corpfin/guidance/safinterp.htm#130.15.

8. Delaware Bans Fee Shifting Bylaws and Authorizes Exclusive Forum Bylaws

On August 1, 2015, amendments to the DGCL came into effect prohibiting stock corporations from adopting fee-shifting bylaws and charter provisions and authorizing Delaware corporations to adopt Delaware-only forum selection provisions.

The amendments add Sections 102(f) and 109(b) to the DGCL to prohibit "any provision that would impose liability on a stockholder for the attorneys' fees or expenses of the corporation or any other party in connection with an internal corporate claim" in a stock corporation's charter and bylaws.

The amendments also add Section 115 to the DGCL allowing, with certain limitations, corporations to require that any internal corporate claims be brought in Delaware court, but disallowing making any other jurisdiction the exclusive forum for internal corporate claims. The authorization of a Delaware-only forum selection acts to codify the DCC's 2013 holding in *Boilermakers Local 154 Retirement Fund* v. *Chevron Corp*, and the prohibition on selection of a non-Delaware jurisdiction as the exclusive forum effectively overruled the DCC's 2014 decision *City of Providence* v. *First Citizens BancShares Inc*.

For the text of the amendments, see:
http://legis.delaware.gov/LIS/lis148.nsf/vwLegislation/SB+75/$file/legis.html?open

9. SEC Proposes Executive Compensation Clawback Rules

On July 1, 2015, as mandated by Section 954 of the Dodd-Frank Act, the SEC voted 3-to-2 to propose the new Rule 10D-1 under the Exchange Act requiring all listed companies, including EGCs, smaller reporting companies, controlled companies and foreign private issuers, to (i) adopt and comply with written compensation clawback policies for executive officers and (ii) disclose these clawback policies in accordance with SEC rules.

Rule 10D-1 would require that national securities exchanges and associations establish listing standards requiring all listed companies to adopt and comply with compensation recovery. Recovery would be required from current and former executive officers who received incentive based compensation during the three fiscal years preceding the date on which the company is required to prepare an accounting restatement to correct a material error. Companies would be required to recover the amount (on a pre-tax basis) of incentive-based compensation that exceeds the amount the executive officer would have received during the applicable period had the incentive-based compensation been determined based on the restated financial statements. Companies would have the limited discretion not to recover if the direct expense of enforcing recovery would exceed the amount to be recovered, or for foreign private issuers, if in certain circumstances, recovery would violate home country law. In addition, each listed company would be required to file its recovery policy as an exhibit to its annual report under the Exchange Act.

The proposed rules would implement the last remaining executive compensation provision of the Dodd-Frank Act for which rules have not yet been proposed, and are expected to become effective before the second half of 2016. Once effective, each company would be required to adopt its recovery policy not later than 60 days following the date on which the listing exchange's rule becomes effective and would require recovery of all excess incentive-based compensation received by current and former executive officers on or after the effective date of Rule 10D-1 for any period ending on or after the effective date of the new rule.

For a more detailed summary of the proposed rules, see the Paul, Weiss memorandum at: http://www.paulweiss.com/media/3063571/9july15_alert.pdf.

For a copy of the proposed rules, see: http://www.sec.gov/rules/proposed/2015/33-9861.pdf.

10. SEC Adopts Rules to Update Regulation A Promoting Small Capital Formation

On March 25, 2015, the SEC voted unanimously to adopt amendments to its public offering rules to exempt an additional category of small capital raising efforts as mandated by Title IV of the JOBS Act.

Tier 1 and Tier 2 Offerings. The final rules update and expand the Regulation A exemption by creating two tiers of Regulation A offerings, available only to companies organized in or with their principal place of business in the United States or Canada:

- Tier 1, which includes securities offerings of up to $20 million in a 12-month period, including up to $6 million for the account of selling securityholders that are affiliated with the issuer; and
- Tier 2, which includes offerings of up to $50 million in a 12-month period, including up to $15 million for the account of selling securityholders that are affiliated with the issuer.

For offerings of up to $20 million, an issuer can elect to use either Tier 1 or Tier 2.

Offering Process. Issuers are required to prepare an offering statement including the narrative and financial information required by Form 1-A. Form 1-A requires basic information about the issuer, material risks, use of proceeds, an overview of the issuer's business, a management's discussion and analysis ("MD&A") type discussion, disclosures about executive officers and directors and compensation, beneficial ownership information, related party transactions, a description of the offered securities, and two years of financial statements (or for such shorter time that the issuer has been in existence). Preliminary offering statements must be filed with the SEC on EDGAR at least 48 hours in advance of a sale unless the issuer is already subject to, and current in, ongoing reporting requirements under Regulation A (described below). The offering statement is "qualified" by SEC order so that the SEC has the opportunity to review and comment. Final offering statements must be filed on EDGAR within two business days after the sale.

Tier 2 Offerings. Unlike Tier 1 offerings, Tier 2 offerings are preempted from state securities laws registration and qualification requirements but are subject to additional requirements, including a cap on the amount of securities a non-accredited investor may purchase, a requirement that financial statements must be audited and ongoing reporting requirements on Forms 1-K (annual report), Form 1-SA (semi-annual report) and Form 1-U (for certain current event reporting). Form 1-K requires disclosures relating to the issuer's business and operations, related party transactions, beneficial ownership, executive officers and directors, executive compensation, MD&A and audited financials.

For more a more detailed summary of the updates to Regulation A, see the Paul, Weiss memorandum at: http://www.paulweiss.com/media/2850660/8april15alert.pdf.

11. SEC Grants No-Action Relief Permitting Five Business Day Debt Tender Offers

On January 23, 2015, the Staff of the Division of Corporation Finance (the "Staff") of the SEC issued a no-action letter granting the relief requested in a letter submitted by a number of nationally recognized law firms (including Paul, Weiss) and supported by various market participants regarding the conduct of certain debt tender offers. In its letter, the Staff confirmed that it would not recommend any enforcement action to the SEC if an issuer were to conduct a tender offer for non-convertible debt securities (including high-yield debt securities) and hold the tender offer open for at least five business days from and including the date the tender offer is first publicized, so long as such tender offer satisfies certain criteria (such offer, a "Five Business Day Debt Tender Offer"). The tender offer would be required to be held open for an additional ten business days following any change in the consideration offered or the announcement of any other material change in the offer. The new relief was effective immediately and superseded the Staff's prior no-action relief in this area, which permitted certain tender offers for investment grade securities to occur in as little as seven calendar days.

For a detailed summary of the no-action relief permitting Five Business Day Debt Tender Offers, see the Paul, Weiss memorandum at: http://www.paulweiss.com/media/2779114/25jan15alert.pdf.

*   *   *

For a discussion of certain other developments during 2015 not highlighted above, please see our memoranda available at: http://www.paulweiss.com/practices/region/canada.aspx.

*   *   *

This memorandum is not intended to provide legal advice, and no legal or business decision should be based on its content. Questions concerning issues addressed in this memorandum should be directed to:

Matthew W. Abbott 212-373-3402 mabbott@paulweiss.com	Christopher J. Cummings 416-504-0522 ccummings@paulweiss.com	Andrew J. Foley 212-373-3078 afoley@paulweiss.com
Adam M. Givertz 416-504-0525 agivertz@paulweiss.com	Edwin S. Maynard 212-373-3024 emaynard@paulweiss.com	Stephen C. Centa 416-504-0527 scenta@paulweiss.com

Associate Rebecca Vasluianu contributed to this client alert.