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Informed analysis for the financial services industry

In the News

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In This Issue ...

It's hard to read a business publication these days without seeing headlines on Russia sanctions, crypto and the SEC's new climate-related disclosure rules. It is no different this week.

We weren't at all surprised to see the continued escalation of Russia sanctions, and as James Treanor and Duncan Grieve note in a “Take Five” commentary, even harsher measures are still at the disposal of the United States and the European Union.

On crypto, James Frazier, who leads our ERISA team and also serves as co-chair of our Financial Services Group, addresses the Department of Labor release last month cautioning ERISA plan fiduciaries to use “extreme care” when considering including a cryptocurrency or other related option as part of a self-directed 401(k) plan’s menu of investment choices. We also look at the UK government's plan to become a “global hub” for the cryptoasset industry.

This week's “In Depth” article provides a very helpful guide for public companies with regard to the U.S. Securities and Exchange Commission's proposed amendments to Regulation S-K and Regulation S-X that would mandate significant additional climate-related disclosures for public companies. Peeling back some of the complexity, members of our Global Litigation, Corporate and Capital Markets teams – Jason Halper, Erica Hogan, Michael Ruder and Lauren Russo – offer next steps for public companies in advance of the new rules.

We welcome your comments and questions. Just write to us here.

Daniel Meade & **Michael Sholem**
Co-Editors, *Cabinet News and Views*

New Round of Russia Sanctions

By **James A. Treanor**
Special Counsel | White Collar Defense and Investigations

By **Duncan Grieve**
Special Counsel | White Collar Defense and Investigations

Following reports of alleged atrocities committed by Russian forces in parts of Ukraine, the United States and the European Union have announced significant new economic sanctions aimed at further cutting off Russia from international markets.

In the United States, the White House announced that President Biden would sign an Executive Order prohibiting new investments in Russia by U.S. persons. According to the Department of the Treasury's press release, the Order will also authorize the Secretary of the Treasury to impose sanctions on the provision of specific categories of services to Russia.

Newly announced U.S. sanctions also include full blocking measures applied to Russia's largest bank, PJSC Sberbank of Russia ("Sberbank"), and 42 of its subsidiaries. Previously, Sberbank and some subsidiaries were subject to more limited sanctions, including prohibitions on dealings in certain debt and equity, as well as correspondent account and payable-through account ("CAPTA") prohibitions. As a result of the new measures, U.S. persons must block and report to the Office of Foreign Assets Control ("OFAC") all property and interests in property of Sberbank, and its designated subsidiaries, as well as any other entity in which Sberbank (or a designated subsidiary) owns, directly or indirectly, a 50 percent or greater interest. In addition, OFAC imposed blocking restrictions on another major Russian bank, JSC Alfa-Bank, and certain of its subsidiaries, as well as numerous Russian business and political leaders and their family members – including Russian President Putin's daughters.

In coordination with these U.S. actions, the European Union announced its own slate of new Russia-related sanctions. In particular, President of the European Commission Ursula von der Leyen announced a fifth round of sanctions against Russia. Specific details of these additional sanctions are yet to be defined, but will include the following "6 pillars":

1. An import ban on coal from Russia, reportedly amounting to approximately 4 billion euros per year;
2. A "full transaction ban" on VTB and three other Russian banks (as yet unnamed), which together represent 23 percent of the Russian banking sector;
3. A ban on Russian vessels and Russian-operated vessels from accessing EU ports, with certain exemptions for essential products, humanitarian aid and energy. Furthermore, the EC have proposed a ban on both Russian and Belarusian road transport operators (*i.e.*, trucks and other heavy goods vehicles);

4. An export ban covering a range of sectors, notably including quantum computers, advanced semiconductors, machinery and transportation equipment;
5. An import ban covering wood, cement, seafood and liquor; and
6. A "number of very targeted measures," including a ban on Russian companies from participating in public procurement in EU member states, and an exclusion from all financial support to Russian public-sector entities.

Furthermore, EU High Representative Josep Borrell previewed that the EC will add "dozens" of Russian business and political leaders to the EU sanctions list.

The new measures announced by the United States and the European Union have been or will be joined by fresh sanctions from the United Kingdom and other countries. They represent a significant escalation in economic pressure on Russia, and especially on its financial sector. However, with no end to the conflict in sight – and with Europe, in particular, so far holding in reserve its most potentially crushing sanctions on Russia's energy exports – this latest round of sanctions is unlikely to be the last.

(The authors wish to thank trainee solicitor Benjamin Jacobs for his contributions to this commentary.)

California's Board Diversity Law Tossed by Judge; Other Board Diversity Efforts Continue

By **Ellen V. Holloman**
Partner | Global Litigation

By **Zack Schrieber**
Associate | Global Litigation

On April 1, 2022, Judge Terry Green of the Los Angeles Superior Court struck down California's AB 979,[1] which required publicly held companies based in California to have at least one board director from an "underrepresented community"[2] by the end of 2021 and to set parameters for additional board diversity by the end of 2022. A company's failure to diversify its board could have led to fines totaling hundreds of thousands of dollars.

California had not brought an enforcement action, but AB 979 was challenged under a California law that permits taxpayers to challenge state laws where taxpayer funds have been expended.

Judge Green signaled that he would overturn AB 979 at a March 14, 2022, hearing, where he characterized the law's definition of "underrepresented community" as a "bit arbitrary," as certain other minority groups were not included in its definition, and stated that AB 979's established formula was effectively "a quota by any other name."[3]

In his formal opinion, Judge Green found that the law violates the Equal Protection Clause of the California Constitution. The opinion notes that while it is "true that remediating discrimination may be a compelling interest," AB 979 does not "identify a specific arena" where that discrimination occurred. In Judge Green's view, to survive constitutional scrutiny, AB 979 needed to identify and apply only to specific industries or geographic regions with a history of discrimination – not simply corporate boards throughout the entire state.

While AB 979 was struck down, other ongoing efforts at incentivizing board diversity remain in place. New York and Illinois require companies to disclose certain board diversity statistics. A Nasdaq disclosure rule, which also requires board diversity or an explanation for the failure to diversify, is set to begin implementation later in 2022. And just days after this decision, Goldman Sachs announced that it helped place its 50th diverse director on the board of a client.[4]

[1] Cal. Corp. Code § 301.4 (West) (2022).

[2] Under AB 979, "underrepresented community" includes certain racial and ethnic minorities and those who self-identify as LGBT.

[3] Craig Clough, *Law360*, "Calif. Board Diversity Law Seems 'Arbitrary,' Judge Says," Mar. 14, 2022.

[4] Emma Hinchliffe, *Fortune*, "Goldman Sachs took a stand on board diversity. The bank just placed its 50th diverse director," Apr. 5, 2022.

FRB Issues Enforcement Actions against Bank and BHC Employees for Alleged CARES Act Fraud

By **Daniel Meade**
Partner | Financial Regulation

The Federal Reserve Board ("FRB") announced on April 5 that it had entered into six separate consent orders with individuals who were previously employed at a state member bank or bank holding company ("BHC") within the FRB's jurisdiction. The consent orders prohibit each of the individuals from employment in the banking industry. The FRB stated that each of the prohibited individuals fraudulently obtained loans or grants under the Coronavirus Aid, Relief, and Economic Security Act ("CARES Act").

According to the FRB, each of the prohibited individuals applied for and obtained an economic injury disaster loan ("EIDL") or grant through the Small Business Administration "based on materially false and fraudulent representations and used the proceeds of the loan or grant for personal and other unauthorized expenses in violation of the EIDL and applicable laws and regulations."

As is usually the case with consent orders, the facts available are sparse, but the orders do not appear to allege that the individuals used their positions at their respective bank or bank holding company in their procurement of the EIDLs or grants. But because they were bank or BHC employees, they were subject to this action by the FRB. The FRB's actions look to comprise just a fraction of the efforts by many parts of the federal government to protect the integrity of CARES Act programs and deter wrongdoing. In May of 2021, Attorney General Garland established the COVID-19 Fraud Enforcement Task Force to "marshal the resources of the Department of Justice in partnership with agencies across government to enhance efforts to combat and prevent pandemic-related fraud."

The UK's Plan to Become a Global Crypto Hub

By **Michael Sholem**
Partner | Financial Regulation

On April 4, 2022, the UK government announced plans to become a "global hub" for the cryptoasset industry with proposals for the regulation of stablecoins, development of an NFT (non-fungible token) issued by the Royal Mint, together with other measures, including the introduction of a "financial market infrastructure sandbox" to help firms experiment and innovate. The proposals were laid out in a speech by John Glen, Economic Secretary to the Treasury, at the Innovate Finance Global Summit. In January 2021 the UK government issued a consultation on cryptoassets and stablecoins, and it has now published its response outlining the feedback received from 89 parties and setting out detail on proposed changes to the regulatory perimeter.

Stablecoins are a form of cryptoasset pegged to a reserve asset like a fiat currency, commodity or even another cryptocurrency. The UK government proposes to legislate to bring stablecoins, where used as a means of payment, within the regulatory perimeter under the supervision of the Financial Conduct Authority ("FCA"). This would require stablecoin issuers to hold equal reserves of pounds sterling for the tokens issued. Glen stated that the "approach will ensure convertibility into fiat currency, at par and on demand," adding that the Bank of England would regulate "systemic" stablecoins.

The UK government also announced its intention to review taxation rules for cryptoassets, including a review of DeFi loans (where holders of the cryptoasset lend them out for a return). Glen stated that the government intended to explore the possibility of issuing government debt using distributed ledger technology ("DLT") and that they were also developing opportunities to use DLT to "ease the import of goods."

In May, the FCA will hold a two-day "CryptoSprint" with industry participants, seeking views from industry on key issues relating to the development of a future cryptoasset regime. The UK government also intends to establish an engagement group convening regulatory authorities and industry to advise the government on the sector.

There remains, however, significant scepticism from some policymakers, including Governor of the Bank of England Andrew Bailey, who, on the same day as the UK government's announcement, stated in a speech at the Stop Scams Conference that cryptocurrencies were the new "front line" in criminal scams and that the technology had created an "opportunity for the downright criminal."

Despite these high-profile announcements, at present there remains a distinct lack of detail in the proposals. For the moment, the UK government appears to be signalling a warmer approach to the role of cryptoassets in the economy than that envisaged by UK regulators.

DOL Warns Sponsors against Permitting Cryptocurrency-Related Investments on 401(k) Plan Investment Menus

By **James Frazier**
Partner | Executive Compensation, Benefits & ERISA

The U.S. Department of Labor ("DOL") last month issued Compliance Assistance Release No. 2022-1 - *401(k) Plan Investments in "Cryptocurrencies"* (the "Release") in which it strongly cautions ERISA plan fiduciaries to use "extreme care" before considering the inclusion of a cryptocurrency or other related option as a choice on a self-directed 401(k) plan's menu of investment choices. In the Release, the Department noted that it had become aware that certain firms were marketing cryptocurrency-type investments as potential options for 401(k) plans.

The DOL reiterated that under ERISA, plan fiduciaries must act solely in the financial interests of plan participants and comply with ERISA's demanding standard of care, and that a breach of these standards could result in personal liability for plan losses. Regarding participant-directed 401(k) plans, the DOL further noted that fiduciaries responsible for the investment options have an ongoing duty to ensure the prudence of such options.

The DOL indicated that, at this current stage in the history of digital assets, it has serious reservations regarding the prudence of exposing 401(k) plan participants to cryptocurrencies or products whose value is tied to cryptocurrencies. According to the DOL, these investment options can pose significant risks (including those associated with fraud, theft and loss) and challenges for participant-directed retirement plans for the following reasons:

- Cryptocurrencies are speculative and volatile investments;
- There are meaningful challenges regarding the ability of plan participants to make informed investment decisions;
- There are custody-related concerns (including vulnerability to hacking and theft), given that cryptocurrency is not held, like more traditional assets, in trust or custodial accounts, and related concerns pertaining to recordkeeping regarding such assets;
- There are concerns around the reliability and accuracy of cryptocurrency valuations; and
- The regulatory environment pertaining to cryptocurrencies is actively evolving, and some market participants may be acting outside of or not otherwise complying with the current regulatory frameworks.

Importantly, the DOL not only sets forth the foregoing concerns, but goes on to provide that, based on these and related considerations, it expects to engage in an investigative program focusing on participant-directed plans that offer on their investment menus cryptocurrency and related products, and "to take appropriate

action to protect the interests of plan participants and beneficiaries with respect to these investments.”

In Depth: What Can Public Companies Do Now to Prepare for the SEC's New Proposed Rules on Climate-Related Disclosures?


By **Jason M. Halper**
Partner | Global Litigation


By **Erica Hogan**
Partner | Corporate


By **Michael J. Ruder**
Special Counsel | Capital Markets


By **Lauren Russo**
Law Clerk | Corporate

On March 21, 2022, the U.S. Securities and Exchange Commission (the "SEC") proposed far-reaching amendments to Regulation S-K and Regulation S-X that would mandate significant additional climate-related disclosures for public companies. A summary of the new disclosure requirements is available in our Clients & Friends Memo dated March 23, 2022. In brief, the proposed rules would require a public company to make significant additional disclosures regarding, among other things, its board and management's oversight of climate-related risks; its processes for identifying, assessing and managing climate-related risks; and its climate-related targets and goals. In addition, a company would be required to disclose how climate-related risks have had or are likely to have an impact on its business and consolidated financial statements, as well as on its strategy, business model and outlook. A company also would be required to disclose its greenhouse gas emissions and provide an attestation report to provide reasonable assurance, after a phase-in period, covering certain disclosed emissions.

Although the SEC's proposal made clear that asset-backed securities issuers are not covered by the proposed rules, the SEC indicated that it is continuing to consider whether and how to apply this type of regulation to asset-backed securities issuers.

If adopted as proposed, the amendments would impose significant reporting requirements on registrants, which in turn would increase compliance costs and require additional managerial time and attention. Although the proposed rules contain various phase-in periods dependent upon filer status, there are steps, discussed below, that public companies can act on today to prepare for the new rules.

1) Review Existing Public Disclosures

Although not yet required to do so by a specific climate-related rule (existing securities law disclosure requirements dependent on general determinations of materiality always have applied), many companies already make a variety of climate-related disclosures to meet investor and legal demands. Some metrics that are currently being reported on a voluntary basis might need to be revised going forward in order to satisfy the technical requirements of the SEC's proposed rule. For example, even if not mandated under a traditional materiality analysis,

companies may already be releasing information about their greenhouse gas emissions and other metrics in their voluntary ESG or corporate sustainability reports. To prepare for the new proposed SEC rule, companies should evaluate their existing disclosures, and the internal processes, procedures and quantitative methodologies underlying such disclosures (*i.e.*, a climate audit), to determine how to bring them into alignment with the SEC's proposed requirements. Particular attention should be paid to identifying which areas will require the most time to develop new internal processes and procedures to comply with the proposed SEC rule.

2) Review and/or Implement Policies and Procedures Related to the Board's Oversight of Climate-Related Risks

The proposed rule will require a company to disclose information about the board and management's oversight and governance of climate-related risks, which include physical risks (*i.e.*, risks to company assets as a result of acute climate events or chronic climate change) and transition risks (*i.e.*, risks and opportunities associated with the transition to a low-carbon economy). Accordingly, a company should evaluate the board and management's roles, and the processes in place, for assessing, managing and overseeing climate-related risks. Companies could also consider whether any changes to the board, the committees and their charters, or management roles are appropriate to ensure those with proper expertise on climate-related matters are in leadership positions.

3) Engage Climate Change Experts – Both Internal and External

Given the breadth of the proposed rule, companies should consider whether their personnel that will be addressing climate-related risks and opportunities possess the relevant knowledge, skills and resources. Companies may consider implementing training or professional development programs for those new to such undertakings to ensure the companies are considering the full range of risks – both physical and transition risks – as required by the proposed rule. A company could also consider engaging outside consultants or counsel to help evaluate the company's climate-related risks and advise the company on complying with the SEC's proposed new requirements.

4) Measure Scope 3/Supply Chain Emissions

The proposed rule requires companies to disclose their Scope 3 emissions only if material or if a company has set a particular target or goal with respect to Scope 3 emissions. Companies could thus begin to measure their Scope 3 emissions now to determine materiality and if they will eventually need to make Scope 3 emissions-related disclosures. Unfortunately, there is no consensus around how exactly to measure these emissions (a process known as "carbon accounting"), in part because companies must rely on their supply chains to provide this information. Nevertheless, companies could still initiate these conversations with their supply chains. For companies in the financial sector, the Partnership for Carbon Accounting Financials' Global GHG Accounting and Reporting Standard for the Financial Industry provides useful guidance on carbon accounting for different asset classes. Given the uncertainty around measuring Scope 3 emissions, the proposed rule contains a safe harbor provision that provides that Scope 3 emissions disclosures will not be deemed fraudulent unless it is shown that the

statement was made without a reasonable basis or was disclosed in other than good faith.

5) Discuss with Auditors

To develop a better understanding of the new rule and its implications, companies should be engaging in a dialogue with their independent auditors. Under the proposed rules, large accelerated filers and accelerated filers will need to provide an attestation report from an independent GHG emissions attestation provider to cover Scope 1 and 2 greenhouse gas emissions metrics, subject to a phase-in period. While the report need not be provided by an outside auditor, many companies likely may opt to have an accounting firm issue the attestation. The proposed rules will likely create high demand for service providers in this space, so registrants may wish to begin discussions with potential service providers.

6) Write a Comment Letter to the SEC

The SEC has requested public comments on the proposed amendments by either May 20, 2022 or 30 days after the date of publication in the Federal Register, whichever is later. The SEC will review and take these comments into consideration before issuing a final rule. Accordingly, a company should consider filing a comment letter with the SEC to express any particular points of concern or support regarding the new rule, as well as to suggest any necessary changes that should be made before the rule is finalized.
