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Corporate Governance Update: AI Disclosure and Governance in the Spotlight

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The 2024 proxy season demonstrated that artificial intelligence (AI)-related disclosures and governance structures currently are a subject of intense shareholder interest. Companies in a wide range of industries faced shareholder proposals, some of which received significant support—and regulators are watching. Recent statements by U.S. Securities and Exchange Commission (SEC) officials indicate that regulators will be carefully monitoring the expanding universe of AI-related corporate disclosures in order to ensure that issuers' public statements conform to applicable laws and regulations and are not misleading to investors.

It is likely that both disclosure- and governance-oriented shareholder proposals regarding AI will gain traction in future proxy seasons. Yet despite the dizzying speed with which AI issues have proliferated in corporate America, the reassuring reality is that the "old" standards and practices governing disclosure and governance do apply to "new" topics, and AI is no exception to this rule. Companies and boards can be confident that the application of sound fundamental principles of governance and disclosure will serve them as well in this area as in others.

2024 Proxy Season Proposals

A number of AI-related shareholder proposals in the recent proxy season targeted company disclosures, seeking a wide range of information about the deployment and risk management of AI. The American Federation of Labor and Congress of Industrial Organizations (AFL-CIO) filed proposals requesting extensive "transparency reports" from several entertainment companies, including Apple. The AFL-CIO's proposal asked Apple to publicly report on "the company's use of [AI] in its business operations and to disclose any ethical guidelines that the company has adopted regarding the company's use of AI technology." Apple opposed the proposal on the grounds that Apple already provides transparency around and oversight of AI, that the scope of the proposed disclosure was so broad that it could harm Apple's competitive position, and that a dedicated AI report would be premature in the evolving regulatory landscape. The AFL-CIO's proposal was rejected by a vote ratio of roughly five to three.

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Investment firm Arjuna Capital filed identical proposals at several companies that went further. The shareholder proposal filed at Microsoft called for an annual report "assessing the risks to the company's operations and finances as well as risks to public welfare presented by the company's role in facilitating misinformation and disinformation disseminated or generated via artificial intelligence, and what steps, if any, the company plans to remediate those harms, and the effectiveness of such efforts." Like Apple, Microsoft cited its ongoing risk management and reporting in its response recommending a vote against the proposal, describing the proposed report as unnecessary.

In a number of cases, AI-related disclosure proposals garnered support in the range of 20% to 30% of votes cast. In a few cases, they were withdrawn when companies agreed to provide more information on their own. Glass Lewis and Institutional Shareholder Services (ISS) typically recommend voting in favor of proposals seeking enhanced disclosure, whether or not related to AI, and that was generally true this season. However, both Glass Lewis and ISS recommended voting against the Arjuna Capital proposal at Microsoft, on the basis that Microsoft's AI disclosure and risk management are already sufficient. As AI is a new and rapidly developing area, investors that do not have relevant expertise can be expected to rely heavily on the recommendations of proxy advisors. Large institutional investors followed proxy advisor recommendations on AI-related proposals this season in many, but not all, cases.

Other AI-related shareholder proposals this season addressed corporate governance. The AFL-CIO filed a proposal at Amazon calling for a new committee of independent directors focused on AI "to address human rights risks associated with the development and deployment of AI systems." Amazon opposed the proposal, stating that AI-related risks are overseen by its board committees that are already tasked with risk oversight in a variety of contexts and noting that "none of our peer companies has a board committee dedicated solely to risks arising from AI."

Equity fund Trillium, along with other investors, filed a proposal at Alphabet alleging that the company had not "successfully implemented" the set of "AI Principles" that it launched in 2018 and accordingly requested that the board amend the charter of the Audit and Compliance Committee to add "appropriate language which makes it clear that the Committee is responsible for overseeing Alphabet's artificial intelligence activities and ensuring management's comprehensive and complete implementation of its AI Principles." In its response, Alphabet countered that it has been transparent in its implementation of its AI Principles and that it integrates AI oversight into enterprise risk management at both committee and board levels. Alphabet did not specifically say that it has indeed "successfully implemented" the AI Principles; it did contend that "explicitly calling out AI in the Audit Committee Charter is unnecessary as it is already subsumed within the broader risk assessment areas set forth in its Charter."

These governance proposals share a common theme: If implemented, they would have the effect of making certain directors — *i.e.*, the members of a newly formed AI committee, the members of the audit committee, or the chairs of such committees —

publicly and individually accountable for AI oversight failures. This would enable shareholders to target these directors in activist campaigns and, potentially, in litigation. Boards concerned about this scenario may wish to consider this factor in deciding whether to specifically delegate or broadly distribute responsibility for AI oversight. There are many factors to consider, however, and the most effective governance structure for some boards may entail creating an AI or technology committee or charging an existing committee specifically with AI oversight responsibility. Each board must determine how it can best structure oversight of AI-related issues and, crucially, ensure that it fulfills its duty of oversight, recognizing that the current environment is one of both intense scrutiny and rapid change.

The Fundamentals Still Apply

In a speech last month, SEC Enforcement Director Gurbir S. Grewal observed that "elevated investor interest in rapidly developing technology or offerings often leads to elevated investor risk." He compared the accelerating investor interest in AI to the sudden uptick of interest in environmental, social and governance (ESG) investing when that was new, noting that "companies had meaningful financial incentives to exaggerate, or make misleading statements about, their supposed ESG activities or products…. Not surprisingly, we are now seeing the same thing with AI."

Citing a report indicating that 40% of S&P companies mentioned AI in their latest annual reports, SEC Chair Gary Gensler recently emphasized that AI-related disclosures are not held to different disclosure or liability standards: "As AI disclosures by SEC registrants increase, the basics of good securities lawyering still apply." In other words, "claims about prospects should have a reasonable basis, and … when disclosing material risks about AI … investors benefit from disclosures particularized to the company, not from boilerplate language." Companies feeling overwhelmed by the novelty and variety of AI-related issues should take comfort from that and from the assurance that, as Grewal put it in his April speech: "[A]s I've said before [in other contexts] and I will say … again in the context of AI-related risk disclosures: folks who operate in good faith and take reasonable steps are unlikely to hear from us."

The exponential growth of generative AI in recent years has opened a new universe of disclosures for corporations. Business operations, risk factors, human rights concerns, strategic planning, internal policies, corporate governance, forward-looking statements — AI-related developments may affect all of these and more. However, companies can be confident that the fundamentals of disclosure and governance remain unchanged. Best practices for AI disclosure and AI-related governance are, for now and the foreseeable future, no different from those for non-AI related disclosure and governance. Likewise, board oversight obligations for AI risks are no different than oversight obligations for any other significant risks that a company may face, and they must be addressed on a company-specific basis. Keeping these fundamentals in mind while making decisions related to AI disclosure and governance will enable companies and boards to see the essential issues clearly rather than be distracted by the novel guise in which they appear.