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CORPORATE GOVERNANCE

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1. GENERAL PRINCIPLES

1.1 What are the general principles of corporate governance in your jurisdiction? What are the main objectives of the corporate governance principles? Is your legal system based on common law, civil law, Islamic law or something else?

The US legal system consists of a combination of state and federal common law, statutory law and rules and regulations of various government agencies, including in the area of securities law and rules applicable to publicly listed companies promulgated by the US Securities and Exchange Commission (SEC) and self-regulatory organisations, such as the stock exchanges, which are supervised by the SEC. In addition to these sources and judge-made law (principally of the Delaware Court of Chancery, as most US corporations are incorporated in the state of Delaware), the US corporate governance regime derives from a variety of non-legal sources, including best practice recommendations and guidelines and proposals advanced by shareholders, proxy advisory firms and various interest groups. Moreover, the ability of corporations and their shareholders to privately order the vast majority of their governance arrangements and the structure of the US market – in which most public companies now have widely dispersed and diversified shareholder bases, controlling shareholders are rare and institutional investor intermediaries of varying types hold more than 70% of publicly traded securities (as compared with less than 10% in the 1950s) – strongly influence corporate governance.

In the USA, a unitary board of directors, elected by shareholders and subject to fiduciary duties, is charged with overseeing the corporation's business and affairs. Directors are fiduciaries of the corporation and its shareholders and are expected to focus on promoting and developing the long-term and sustainable success of the company. See paragraph 4.1 for a discussion of fiduciary duties, including the duties of care, loyalty, good faith and candour. Unlike some jurisdictions where shareholders directly determine key business matters, such as dividend policy and material acquisitions, the US model is director-centric, giving boards broad authority to exercise their business judgement on most matters. Courts will typically not second-guess business decisions of the board where the 'business judgment rule' applies, which involves a rebuttable presumption that directors are discharging their duties in good faith, on an informed basis and in a manner the directors reasonably believe to be in the best interests of the corporation and its shareholders. "[H]elp[ing] the corporation build long-term, sustainable

growth in value for shareholders and, by extension, other stakeholders" has been described by the NYSE Commission on Corporate Governance as the "fundamental objective" of the board.

Principles of transparency are implemented through a disclosure-based securities law regime designed to provide timely information to shareholders about public companies and material developments.

1.2 Have there been any recent developments in the law, codes and rules of corporate governance?

Within a relatively stable framework of state law and federal regulation, incremental developments in corporate governance-related laws and practices have occurred in recent years, with more fundamental shifts having occurred in prior periods, such as those wrought by the Sarbanes-Oxley Act of 2002 (Sarbanes-Oxley) or the focus of boards shifting from business strategy towards a more compliance-oriented posture aimed at oversight and monitoring. Principal areas of governance pressure and change include risk management, executive compensation (*see paragraphs 4.5, 9.1 and 9.2*), board structure, director elections, takeover defences and the extent to which matters of corporate strategy and even ordinary business decisions should be determined by shareholders instead of the board (*see paragraphs 3.4 and 8.1*). Changes include:

- Most US public companies now have annually elected boards. In 2002, 61% of S&P 500 companies had classified boards in which a third of the board is elected each year; that percentage is now down to only 7%. At 86% of S&P 500 companies, directors are now elected by a majority of votes cast (instead of a plurality voting standard) with incumbent directors who are not re-elected by majority vote having to tender their resignations. These changes have increased the power of shareholders and proxy advisory firms. For example, the most influential proxy advisory firm, Institutional Shareholder Services (ISS), will recommend a "withhold" or "against" vote against directors if the board is insufficiently responsive to shareholder proposals that receive the support of a majority of the votes cast in a previous year.
- 53% of S&P 500 companies are led by a combined chairman and CEO, down from 75% in 2002. 90% of S&P 500 company boards have a lead or presiding director (which position may be filled by the independent chairman).
- Nearly 60% of major corporations today have boards whose only non-independent member is the CEO (as contrasted to 31% in 2002), even though the rules of the stock exchanges only require public company boards to have a majority of independent directors and there has been renewed interest in whether the presence on the board of a meaningful minority of directors with prior history or familiarity with the company and its industry may actually enhance board effectiveness. The voting guidelines of many institutional investors and governance advisory organisations often specify that a substantial majority or a specific

percentage of the board must be independent as defined by criteria stricter than the stock exchange definitions.

- The Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (Dodd-Frank) eliminated broker discretionary voting for the election of directors and executive compensation. In 2012, the NYSE eliminated broker discretionary voting on many governance items. As a result, brokers can no longer vote on such matters on behalf of clients who fail to provide voting instructions. These changes are considered to have made it harder for companies to achieve majority votes on company-sponsored proposals, including director elections.
- In 2011, the SEC permitted shareholders to include, in the company's proxy statement through the Rule 14a-8 shareholder proposal process, proposed byelaw amendments that would permit shareholders to nominate director candidates through the company's own proxy statement. Prior Dodd-Frank-related rule-making in which the SEC required companies to provide such "proxy access'" for shareholder-nominated directors was struck down by the courts. While these mandatory, market-wide rules never went into effect, the 2014 and 2015 proxy seasons saw increased use – and passage – of precatory shareholder proposals advocating that companies adopt proxy access frameworks, and a number of companies adopted proxy access byelaws. While specific terms vary, they generally permit shareholders who have held at least 3% to 5% of a company's stock for at least three years to nominate up to 20% to 25% of the board using the company's own proxy materials. It remains to be seen whether and what form of proxy access will ultimately take hold market-wide at US public companies.

1.3 Outline recent court cases and incidents involving corporate governance issues. Were there any significant corporate scandals or large unlawful corporate cases?

Risk oversight is highly scrutinised. For example, proxy advisory firms like ISS have added material failures of risk oversight to the list of factors considered in recommending "against" or "withhold" votes in director elections – but note that this addition is not intended to "penalize boards for taking prudent business risks or for exhibiting reasonable risk appetite".

Illustrative examples of what ISS considers a failure of risk oversight include bribery, large or serial fines or sanctions from regulatory bodies, significant adverse legal judgments or settlements, and significant hedging or pledging of company stock. Cybersecurity, in particular, has become an area of intense focus. For example, in December 2013, hackers stole the payment card data of 40 million customers from Target, which led ISS to recommend that Target shareholders vote against all seven of the directors who served on Target's audit or corporate responsibility committees at the time of the data breach on the theory that a failure of board-level risk oversight had occurred. (All directors were ultimately re-elected, albeit with significant "against" votes.) Prior high-profile incidents involving perceived failures of effective oversight include the "London whale" trading losses at JPMorgan

Chase – which resulted in "withhold the vote" campaigns against certain independent directors involved in the board's oversight function and an ultimately unsuccessful shareholder proposal to separate the board chairman and CEO positions – and Hewlett-Packard's nearly $9 billion write-down of its Autonomy acquisition amid accusations of inadequate due diligence, which resulted in the chairman of the board relinquishing his chairmanship and two other directors stepping down after receiving bare majorities of votes in uncontested elections following the write-down. Recent court cases have underscored expectations that directors will be active and engaged, particularly where potential red flags revealing corporate malfeasance may be present, and that resigning from a board may not necessarily immunise directors from liability.

1.4 Which law enforcement agency is in charge of enforcing corporate governance? May a criminal sanction be levied upon infringement of the corporate governance rules?

Corporate governance, generally speaking, is traditionally not a matter of criminal or civil enforcement by law enforcement agencies. Fiduciary duties imposed by state statutory and common law are primarily enforced via private lawsuits brought by shareholders.

The SEC and the US Department of Justice (DOJ) enforce federal securities laws, including Sarbanes-Oxley, which provides for civil, criminal and administrative penalties. Many of the securities laws may also be enforced by private lawsuits.

Companies that violate substantive civil or criminal law may be subjected to remedies (or agree to settlements) that touch on corporate governance matters, such as enhancing ethics and compliance programmes or appointing an external, independent compliance monitor. Under the Federal Sentencing Guidelines and the DOJ's Principles of Federal Prosecution, sentencing may take into account the effectiveness of a company's compliance programme and active director oversight.

2. SOURCES OF LAW

2.1 Which laws, codes or statutes govern company structures and organisations? Are there statutes like the Companies Act or other forms of law? Is there much relevant case law?

There is no overarching federal corporate code in the USA, and company structure and organisation are primarily a matter of state statutory law. Each of the 50 states has its own corporate code, with Delaware's General Corporation Law being by far the most prominent, since the majority of US public companies are incorporated in Delaware. A variety of company structures are permissible under state law, including corporate, limited liability company, partnership and sole proprietorship forms, and companies can be quickly formed with minimal procedural hurdles to act in furtherance of any lawful purpose. Most state laws take an enabling approach, in which corporations and their shareholders have the ability to engage in private ordering of their governance and organisational arrangements through their

charters and byelaws. The Delaware courts, particularly the Delaware Court of Chancery, a specialised business court, have developed an immense body of case law interpreting the Delaware General Corporation Law (and equivalent laws applicable to non-corporate entities), including with respect to various corporate governance topics. These cases, while not legally binding outside Delaware, have wide influence.

For listed companies, stock exchange listing rules and regulations, such as the NYSE Listing Manual and the NASDAQ Marketplace Rules, may also implicate company structures and organisations and are adopted with the approval of the SEC. Listing rules address several important aspects of corporate governance, including director independence, the nature and composition of various board committees, meetings of non-management and independent directors in executive sessions, shareholder voting rights, regulation of dual-class stock structures and the content and public disclosure of corporate governance guidelines and codes of business conduct.

2.2 Which laws, codes or statutes regulate capital markets in your jurisdiction?

US capital markets are primarily governed by: (i) the federal securities laws, particularly the Securities Act of 1933, the Securities Exchange Act of 1934, and the rules and regulations of the SEC promulgated under those Acts, which include, among others, proxy rules, tender offer rules and ownership reporting rules for directors, officers and significant shareholders, (ii) stock exchange listing rules, predominantly those of the NYSE and the NASDAQ and (iii) the rules and regulations of the Financial Industry Regulatory Authority (FINRA), a market-wide self-regulatory organisation that regulates securities firms doing business in the USA, including member brokerage firms and exchange markets. The stock exchanges and FINRA play a significant role in promoting fair and transparent capital markets and are subject to oversight by the SEC. Both Sarbanes-Oxley and Dodd-Frank included provisions relating to capital markets, many of which operated to amend and expand provisions of the 1933 and 1934 Acts. Certain state securities laws, including "blue sky" laws, also regulate the offering and sale of securities.

2.3 Are there any public interest laws which apply to or influence corporate governance?

Generally, no. For example, with respect to board composition, there are no requirements for labour or government representation (or other mandated representation for particular constituencies) on the board of directors, nor are there gender or racial diversity requirements. However, with respect to diversity, public companies are required to disclose whether, and if so how, diversity is considered in identifying director nominees and how diversity policies are implemented and assessed.

2.4 Have there been any recent developments in any of the above laws? What are the recent changes to the above laws or rules and the reasons for them?

Recent changes include:

- In 2013, Delaware adopted legislation enabling the formation of for-profit "public benefit" corporations that seek to promote one or more specific public benefits identified in the corporation's certificate of incorporation. Directors of public benefit corporations have fiduciary duties to conduct the corporation's affairs for the benefit not only of shareholders, but also in the broader public interest.
- In April 2012, Congress enacted the Jumpstart Our Business Startups (JOBS) Act to ease reporting requirements for emerging growth companies and facilitate private capital formation. Related rule-making is underway.
- Various rule-makings related to Dodd-Frank are still pending, including with respect to new "pay equity" and "pay for performance" disclosures, compensation clawback policies and hedging of stock.
- Rule-making is also pending before the SEC for (i) the elimination of regulatory loopholes that enable activist hedge funds to rapidly accumulate significant and even controlling stakes in public companies without timely notice to the market and (ii) modernisation of the reporting periods in which institutional investors must report their shareholdings in public companies.

3. SHAREHOLDERS AND THE SHAREHOLDERS' MEETING

3.1 How are shareholders' interests represented in the company? How are the shareholders assured exercise of their rights? What is the highest governing body within the company structure if it is not the shareholders' meeting?

As discussed in paragraph 4.1, a unitary board of directors, all of whose members must be elected by the shareholders and each of whom is charged with acting in the best interests of the company and its shareholders, is the highest governing body of the public corporation. Shareholders' interests are represented through the shares they hold in the company. Most public companies in the USA have a single class of voting common stock entitled to one vote per share, although dual-class stock structures are permitted (such as those seen at several major technology and media companies). In the proto-typical case, shareholder interests are protected by virtue of the equal treatment generally afforded to shareholders by law, fiduciary duties owed by directors and officers to the company and its shareholders, and by one-vote-per-share operating in the context of widely dispersed share ownership. Courts will carefully scrutinise any improper curtailment of shareholder rights and apply heightened scrutiny to board actions that negatively impact a shareholder's right to vote. See paragraph 3.3 for a discussion of shareholder rights.

3.2 How is the shareholders' meeting conducted? Who may chair the meeting? May attendance (not voting) at the meeting be restricted only to the shareholders? Are the shareholders allowed to be accompanied by legal or other counsel?

Shareholders' meetings are typically held annually, as provided by state law and the organisational documents of the company. Annual and special meetings may be convened by the board and, to the extent provided for in the company's charter or byelaws, shareholders satisfying certain ownership requirements (which vary across companies) may have the right to call special meetings of the shareholders. The board sets the agenda of the meeting, and many companies have adopted advance notice byelaws that require shareholders to provide advance notice and satisfy other procedural requirements in order to propose business at a meeting.

Shareholders' meetings are usually held in person, although companies are increasingly experimenting with virtual shareholders' meetings conducted entirely online. Each meeting has a "record date" fixed by the board, and only persons holding shares as of such date are entitled to vote. Advance notice of the meeting must be given to shareholders by specified deadlines, and such notice must set forth the matters to be considered at the meeting. When items are subject to a shareholder vote, the company must provide shareholders with comprehensive proxy statements containing the recommendation of the board, information about the proposals to be considered, disclosure of interests of directors and officers that may differ from the general interests of shareholders and other mandatory items.

Meetings are conducted in accordance with the company's charter and byelaws, and the chairman of the board (who is often the CEO of the company) usually chairs the meeting. Depending on the topic at issue, the specific vote requirement for shareholder action may be a majority of the outstanding shares, a majority of the shares present and entitled to vote, a majority of voted shares, or a plurality of voted shares. In certain cases involving related party transactions, the standard is voluntarily tightened to count only votes of unaffiliated or disinterested shareholders. Actions taken at a meeting will not be effective in the absence of a sufficient quorum of shares being represented at the meeting. The specific quorum requirement is generally specified in the company's byelaws.

Companies may, but are not required to, restrict attendance at shareholders' meetings to shareholders entitled to vote. Although uncommon in practice (except in the context of proxy fights), shareholders generally may be accompanied by legal or other counsel.

3.3 How are minority shareholders' rights protected?

As an initial matter, most large public companies in the USA have a widely dispersed shareholder base and hence no majority or controlling shareholder exists with the power, even in theory, to 'exploit' minority shareholders.

In addition, most public companies have a single class of voting common stock with each share entitled to one vote. Under Delaware law, generally speaking, all shareholders must be treated equally (such as with respect

to dividends). In the rare case of a public company with a controlling shareholder, transactions between the company and the controlling shareholder are subject to heightened legal scrutiny and in practice are generally subject to the review and approval of independent directors who are unaffiliated with the controlling shareholder.

Shareholders also have various rights. For example, shareholders are generally entitled to communicate with other shareholders and attend, participate and vote in person or by proxy at meetings; action taken at a meeting will not be effective if too few shares are represented and quorum requirements are not met. In addition, shareholders generally have the right to elect directors, nominate their own director candidates in compliance with company byelaws, remove directors (albeit in certain cases, such as with a classified board, only at certain intervals or for cause), adopt certain forms of corporate byelaws and approve (but not initiate) charter amendments, receive dividends on a pro rata basis to the extent declared by the board, approve charter amendments and fundamental transactions (such as mergers, sales of all or substantially all of a company's assets, dissolutions or changes in the form of entity), require that shareholders' meetings be held annually, for certain transactions (such as cash-out mergers), exercise appraisal rights and receive the fair value of their shares if they do not vote in favour of the transaction, call special shareholders' meetings to the extent provided under the company's organisational documents, inspect the books and records of the company and obtain its shareholder list for proper purposes, and submit proposals for shareholder vote (including through use of the company's own proxy statement without charge if certain requirements are met). Shareholders of listed companies have additional voting rights established by stock exchange rules, including with respect to certain issuances of common stock. Where there is no controlling shareholder, as is usually the case, the outcome of voting decisions depends on the aggregate of widely held votes.

Finally, shareholders can sue directors for violating fiduciary duties or federal securities laws and petition courts to review results of shareholder votes, including the validity of the election, appointment, removal or resignation of directors and the rights of such persons to continue to hold office. Shareholders can also engage the board directly, either by working constructively with the board to propose and effect strategic or governance changes or conducting an adversarial proxy contest to replace part or all of the board.

3.4 Is shareholder activism encouraged or discouraged? If not encouraged, how is it regulated?

Corporate governance laws and practices have evolved over time to enhance significantly the power of activist shareholders and, consequently, the existing legal and regulatory regime greatly facilitates shareholder activism. Indeed, the last two decades have witnessed a slow but steady shift in the balance of power from boards of directors and corporate management to institutional shareholders and other institutional activists. Changes in SEC rules and stock exchange listing requirements, supplemented by federal and

state legislation, have provided activists with a variety of tools for organising public and private campaigns to advance their governance and economic agendas. Hedge funds and other activist shareholders frequently press boards and management, who are often under pressure to achieve quarterly financial targets, to take actions that will boost immediate stock prices – such as stock buybacks, special dividends, spin-offs, a sale of the company and other corporate reorganisations – even at the expense of long-term performance. Discussions between companies and activists concerning potential changes often involve the implicit (and sometimes explicit) threat of an election contest, proxy fight and aggressive public campaign to remove the current board and management if the activist's demands are not met. In addition, under current law, activists can accumulate substantial stakes in companies without prior notice, and use derivative/synthetic arrangements to acquire voting positions that are not commensurate with their economic stake in the company. In order to counteract the undesirable effects of shareholder activism, the disproportionate power of activist hedge funds and the outsized influence of one-size-fits-all recommendations by proxy advisory firms, long-term investors – and the companies in which they invest – are encouraged to constructively resolve governance and other issues through direct, pragmatic and case-by-case engagement on the merits. See paragraphs 1.2, 3.5 and 8.1 for related discussions of activism.

3.5 How are professional shareholders (those minority shareholders who seek some extra benefit from companies by unduly and habitually influencing management by using their shareholding) treated by the law? Are they excluded from attending the shareholders' meeting? Are they criminally or otherwise publicly sanctioned?

The phenomenon of professional shareholders – in the sense of shareholders that threaten to disrupt annual meetings in hopes of being paid off, as sometimes occurs in certain other countries – largely does not exist in the USA, although certain practices, such as "strike suit"' litigation against a company by plaintiffs firms in order to extract a settlement or receive legal fees, do exist. In the 1980s, some corporate raiders practised "greenmail" in which they would purchase large blocks of shares in public companies and then threaten a takeover unless the corporation bought back those same shares at a higher price than the raider had paid for them. While lucrative for a short period, such practices are rare today, although companies do from time-to-time buy back shares in a lump from an individual shareholder, such as a former activist.

See paragraph 3.2 for a discussion of the shareholders' meeting and paragraphs 3.4 and 13.1 for discussions of shareholder activism.

3.6 Are shareholders' benefits given to some of the shareholders by the company without resolution by the shareholders' meeting prohibited or regulated by the law or other rules?

Selective benefits given to a subset of shareholders are generally prohibited or regulated by law, which by and large requires that all shareholders of

the same class be equally treated. Holders of preferred shares may have preferences or priorities of superior rank to those of common shareholders. While related party transactions are generally rare due to the dispersed nature of ownership at most large public companies, a company may enter into transactions or arrangements with its directors, officers and significant shareholders on terms not available to all shareholders, subject to the board's exercise of its fiduciary duties and compliance with applicable stock exchange requirements (such as public disclosure, review by disinterested directors and shareholder approval in the case of certain stock issuances to directors or officers).

4. DIRECTORS AND BOARD OF DIRECTORS

4.1 What are the functions and responsibilities of the directors and the board of directors? Do you have a one or two-tier board system? What are the outside directors called?

US companies are managed under the direction of a single-tiered, unitary board of directors, elected by the shareholders and subject to fiduciary duties, and with full control over the company's business and affairs. The board's basic responsibility is to exercise its business judgement and act in a manner reasonably believed to be in the best interests of the company and its shareholders (*see paragraphs 1.1 and 4.2*).

Directors owe the corporation and its shareholders fiduciary duties such as the duty of care and the duty of loyalty. The duty of care encompasses the obligation to act on an informed basis after due consideration and appropriate deliberation. The duty of loyalty encompasses the obligation to act in the best interests of the corporation and the shareholders, as opposed to the directors' personal interests. Corollary duties – such as duties of good faith and duties of candour and disclosure to shareholders when submitting matters for shareholder action – also often apply. The board is generally entitled to take into account long-term as well as short-term interests and set the appropriate time frame for achievement of corporate objectives.

The interests of non-shareholder constituencies may also be considered for their impact on creating corporate and shareholder value, and many states formally permit boards to consider the interests of non-shareholder constituencies such as employees, business partners and local communities.

Effective boards typically perform dual roles: (i) advisor to and business partner of management and (ii) monitor and overseer of management. Boards typically delegate day-to-day management to the CEO and other senior management, all of whom serve at the pleasure of the board. Outside directors are typically referred to as non-management directors and as independent directors where they qualify as such under applicable rules (*see paragraph 4.4*). Core board responsibilities include:

- Establishing the appropriate "tone at the top".
- Choosing and monitoring the performance of the CEO and establishing succession plans.
- Monitoring corporate performance and providing advice to management as a strategic partner.

- Evaluating and approving the company's annual operating plan, long-term strategy and major corporate actions.
- Determining risk appetite, setting standards for managing risk and monitoring risk management.
- Planning for and dealing with crises.
- Determining executive compensation.
- Interviewing and nominating director candidates and monitoring the board's performance and effectiveness.
- Taking centre stage in any proposed transaction that creates a potential conflict between the best interests of shareholders and those of management.
- Setting high standards for corporate social responsibility.
- Monitoring compliance.
- Supporting long-term relationships with shareholders.
- Overseeing relations with government, community and other constituents.

4.2 What are the rules that may give rise to civil and criminal liability of the director(s)? How are those liabilities sought?

Breach of fiduciary duties

Directors owe fiduciary duties, including duties of care and loyalty, to the corporation and its shareholders (or, in certain cases involving insolvent or near-insolvent companies, to its creditors) in their capacity as directors by virtue of state corporation statutes and common law. Directors may rely on management and advisors when making decisions so long as they have no reason to believe such reliance is not reasonable. Personal liability for failure of oversight for business risks is subject to an extremely high burden of proof and is typically limited to sustained, systemic and conscious failures of the board. These statutory and common-law duties are generally enforced by private actions alleging breach brought by shareholders against directors directly or derivatively on behalf of the corporation.

Illegal dividends

Subject to state law and knowledge requirements, directors may be jointly and severally liable for the payment of unlawful dividends or unlawful stock repurchases or redemptions by the corporation for the full amount unlawfully paid.

Breach of securities laws

Violations of US federal securities laws can result in civil and criminal liabilities and administrative penalties. The SEC and the DOJ have various enforcement powers, and violations of securities laws can also be enforced by private civil suits brought by shareholders. State securities laws are enforced by state securities regulators. In addition to the anti-fraud prohibitions discussed in paragraph 6.2 concerning intentional or reckless misrepresentations or material omissions made in securities offering documents or certain other SEC filings, securities laws also prohibit insider

trading, which is the violation of the Rule 10b-5 prohibition on trading in company securities while in the possession of material non-public information. Directors may also be held criminally liable for fraudulently influencing, coercing or misleading an accounting firm during an audit with the intention of rendering the audit report misleading, or for knowingly destroying, altering or concealing records with the intent to obstruct, influence or impede any official proceeding (punishable by imprisonment of up to 20 years).

Fraud, theft and corrupt payments

A director can be criminally liable under US federal law for fraud and theft, such as the misappropriation of corporate funds through the use of mail or electronic communications as part of an intentional scheme to defraud another of money or property. The Foreign Corrupt Practices Act (FCPA) makes it a crime for the company or any of its directors, officers or employees to bribe any foreign official, political party or candidate for political office to curry business favours. The FCPA also prohibits any person from directly or indirectly falsifying the company's books, and directors and officers cannot make materially false, misleading or incomplete statements to an accountant in connection with a required audit or any filing with the SEC.

Other laws

US federal bankruptcy laws and other insolvency provisions, such as laws prohibiting fraudulent conveyances, may also give rise to director liability, as may the Fair Labor Standards Act, which guarantees employees federal minimum wages and overtime compensation, depending on the level of control exercised by the director. Other state and federal laws may also give rise to liability under certain circumstances.

4.3 Does the board of directors have a committee system, for example nomination committee, compensation committee, audit committee? If not required, is it common practice for companies? How does it function?

No particular committee system is mandated by state law, but the board of directors is generally authorised to delegate powers to committees (and determine their membership), although certain powers cannot be delegated (such as declaring dividends, amending the organisational documents or recommending or adopting fundamental transactions). At public companies, board committees typically perform a significant portion of the board's work and provide reports and recommendations to the full board. Certain committees, such as audit, nominating and governance, and compensation committees, are required for publicly traded companies and must consist of independent directors and fulfil certain minimum duties. Each of the nominating, compensation and audit committees must have a written charter that specifies its purpose and responsibilities.

Other permanent or ad hoc committees may be created as needed, such as to handle succession planning, risk management, health and safety or

public policy matters. Special committees can also be created to deal with a crisis or handle conflict transactions. Dodd-Frank requires certain financial institutions to have a separate, fully independent risk committee and that an appropriate committee review derivatives activities involving entry into covered swap transactions involving certain commercial end-user exemptions.

4.4 Is it a legal requirement to have an independent director or a third party director? If so, how are they appointed? Is it required for listed companies?

No particular board composition is mandated by state law, but stock exchange listing rules applicable to publicly traded companies typically require that a majority of the board consists of independent directors, as defined by stock exchange rules, and that certain responsibilities be handled by independent board committees (*see paragraph 4.3*). Independent directors, like non-independent directors, are elected by the shareholders, and the board determines which director candidates to submit to the shareholders, typically on the recommendation of the nominating and governance committee, and which directors to appoint to the various committees. In order for a director to qualify as independent, the board of directors generally must affirmatively determine that he or she has no material relationship with the company and that other "bright-line" independence standards are met. Some companies voluntarily impose a higher minimum number of independent directors or stricter independence criteria than those required by stock exchange listing rules.

4.5 How is the compensation for directors or officers determined? Can it be contested by the shareholders or the regulatory authorities? What are the common rules or practices for the compensation of officers?

The board of directors has the legal authority to determine compensation for directors and officers. At public companies, stock exchange rules mandate that committees of the board play a central role in compensation decisions. On account of these requirements, an independent compensation committee of the board usually determines and approves the CEO's compensation. Non-CEO executive officer compensation is also usually determined by the independent compensation committee, although stock exchange rules permit the full board to make such determinations after receiving the compensation committee's recommendation. Heightened independence rules apply to the members of compensation committees and committee advisors. Using an independent compensation committee also facilitates tax deductibility of certain compensation.

Compensation philosophies and programmes are often developed with the input of third-party compensation consultants. The appropriate mix of fixed compensation (for example annual base salary) and variable compensation (that is short- and long-term performance incentives), as well as the form of compensation (for example stock options, restricted shares, restricted stock units or cash-based payments) vary among companies, as determined

by the compensation committee in its business judgement based on the particular needs of the business. Equity-based components are common, and shareholder approval is required of most equity compensation plans under stock exchange rules, including those involving grants of equity-based awards to directors and officers. In addition, Dodd-Frank's requirement of non-binding shareholder advisory votes on executive compensation, popularised as "say on pay", provides shareholders with means for expressing dissatisfaction with compensation practices, which may also be expressed directly to the company outside of the annual meeting context. While these votes are non-binding, companies that receive low approval ratings face intense pressure to modify executive compensation programmes. Courts typically respect compensation decisions so long as the directors act on an informed basis, in good faith and not in their personal self-interest. Except in the case of certain financial institutions (where special "safety and soundness" provisions apply), regulators generally cannot contest compensation decisions.

4.6 How will the board handle a corporate crisis like an internal criminal case, violence, social media exposure or dawn raid by the authorities?

The board of directors, along with senior management as appropriate, is expected to provide careful guidance and leadership in steering the company through a crisis if and when one arises. The specific circumstances will dictate the appropriate handling of the situation, including as to whether to conduct an internal investigation and the form and content of any responsive or remedial action. Advance planning and preparedness is recommended.

5. BOARD OF AUDITORS, AUDIT COMMITTEE, ACCOUNTING AUDITORS

5.1 How is the internal accounting and legal audit structured and conducted? Is an outside accounting audit required and, if so, how is it structured? Are there requirements to change the auditor every five years?

A public company's accounting and audit function involves an independent committee of the board (referred to as the audit committee), external independent auditors, internal auditors and senior management. Public companies must have adequate internal controls over financial reporting, and publicly filed annual and quarterly reports must contain related certifications from the CEO and CFO. All public companies must have their financial statements audited annually by a registered independent accounting firm in compliance with US generally accepted accounting principles and generally accepted auditing standards (US GAAP and US GAAS). The company's external auditor – in the case of large public companies, usually one of the major registered public accounting firms – must publicly file its signed annual report attesting to the quality of the audit and the company's internal control over financial reporting. The federal securities laws require prompt disclosure with respect to changes in the external auditor and any revision to or

inability to rely on prior audited financial statements. There is no entity-level auditor rotation requirement, but the partner in charge of the audit must be rotated at least once every five years.

Federal law and stock exchange rules require that an independent audit committee of the board (comprised of financially literate members, none of whom may accept consulting or advisory fees from the company, with "comply or explain" disclosure required if no member qualifies as a financial expert) be responsible for the appointment, compensation, retention and oversight of the independent auditor and for oversight of certain internal audit function-related matters. While not required, shareholders are typically asked to ratify such auditor's appointment.

5.2 Are there supervisory auditors? What is the function of the supervisory auditors' board?

Generally, not applicable. The annual financial statements of public companies must be audited by a registered independent accounting firm as discussed above. The Public Company Accounting Oversight Board, a federal-level agency created by Sarbanes-Oxley, generally oversees accounting firms and public company audits.

6. MARKET DISCLOSURE/TRANSPARENCY TO THE SHAREHOLDERS AND THE PUBLIC

6.1 What are the disclosure requirements for companies in your jurisdiction under company law, capital markets law or any other rules?

The federal securities laws require public companies to file annual, quarterly and periodic current reports triggered by the occurrence of specified events. The contents of such reports are prescribed by law, and false and misleading statements are generally prohibited. Annual reports contain audited financial statements and comprehensive information about the business, performance and relevant risk factors, quarterly reports contain unaudited interim financial statements and other business information, and current reports disclose the occurrence of certain material events, such as entry into material agreements, completion of significant acquisitions or dispositions of assets, and changes in officers or directors and amendments to the corporation's charter or byelaws. Regulation FD generally prohibits selective disclosure of material information.

When items are brought before the shareholders for their approval, such as for election of directors or consideration of significant transactions such as mergers or the sale of all or substantially all corporate assets, proxy statements containing the recommendation of the board, information about the proposals to be considered, disclosure of interests of directors and officers that may differ from the general interests of shareholders and other mandatory items must be filed. Proxy statements for the annual meetings at which directors are elected contain extensive information about the board and senior management, director and executive compensation, auditor information and other matters. Anti-fraud rules generally prohibit public

disclosures from containing material misstatements or omissions of material facts. While the SEC does not opine on the merits of a securities offering or corporate actions, SEC clearance is required for certain disclosure documents before they become effective.

6.2 What is the liability or responsibility of the board in relation to the company's disclosure requirements?

As part of its oversight role, the board has ultimate responsibility for overseeing management's implementation of adequate disclosure controls and procedures. Under the federal securities laws, directors can be held liable for their material misstatements or omissions of material facts in public filings. In some cases, liability is limited to circumstances where the director acted with *scienter* (actual knowledge or reckless disregard), and various defences, including demonstrating appropriate due diligence, may be available. Violations of the corollary fiduciary duties of candour and disclosure may also result in liability.

7. M&A AND CORPORATE GOVERNANCE

7.1 Upon an M&A offer, how are the transparency and fairness rules of the company provided under the company and stock market laws and rules?

In the case of a tender offer, various disclosure requirements operate to ensure that shareholders are sufficiently informed to assess the offer. Federal securities laws require that the offer be held open for a minimum of 20 business days, and while the bidder is not required to bid for any specific maximum or minimum percentage of shares, all shareholders must be given the opportunity to participate in the offer, receive the same consideration and withdraw their shares from the offer for a specified period of time.

M&A transactions are required to be announced to the market at the time the parties have entered into a definitive agreement, and where shareholder approval is required for the transaction to be consummated, a proxy statement setting forth all material information is required to be made available to all shareholders entitled to vote on the transaction. Prior to reaching such definitive agreement, the bidder and target generally have no disclosure obligations, including with respect to preliminary discussions, and to the extent takeover rumours emerge or inquiries are made, "no comment" is the typical response.

8. PROXY FIGHTING

8.1 Is proxy fighting customarily conducted for control of the company management or anything else? How is it regulated under the company law or market regulations?

See paragraph 3.4 for a discussion of shareholder activism generally.

Proxy fights have become a common feature of the US landscape, and the frequency of election contests has recently increased, particularly among large public companies. Activist shareholders and hostile bidders may nominate their own director candidates and conduct campaigns for full or partial

board control or threaten to do so to pressure the company to enact desired changes. "Withhold" campaigns – in which shareholders are encouraged to withhold votes from or vote against incumbent directors running unopposed – also occur and can have a significant impact at companies with majority voting standards or policies. Precatory resolutions encouraging the company to enact governance or business changes may also be submitted at the shareholders' meeting; if such non-binding resolutions receive majority support by shareholders and the board determines not to adopt the changes, the board may be subject to criticism and adverse vote recommendations from proxy advisory firms at the next year's annual meeting.

Proxy fights are regulated by: (i) federal securities laws, primarily with respect to communications with shareholders, including prohibitions on making false and misleading statements and required filings such as proxy statements, (ii) corporate organisational documents, such as with respect to advance notice byelaw requirements for director nominations or other proposed business and as to the number of election cycles required to replace the full board, and (iii) state law fiduciary duties, with respect to the actions of the board.

9. OFFICERS' REMUNERATION RULES

9.1 How is remuneration of officers determined? By whom? Is there a role for the shareholders' meeting? Is there any mechanism for an independent body to review and evaluate them?

See paragraph 4.5.

9.2 Is the mechanism of officers' remuneration publicly debated?

Executive compensation – particularly the degree of alignment between executive pay and performance and the magnitude and components of pay packages – has been one of the most hotly debated issues over the past several years. Mandatory, but non-binding, "say on pay" votes are conducted annually at most publicly traded companies, and in addition to negative publicity, failed votes can result in proxy advisory firms recommending that shareholders withhold their votes from members of the compensation committee and, in egregious cases, from the entire board. Director compensation has also become an increasingly debated topic.

10. DIRECTORS' LIABILITIES, LIABILITY INSURANCE, INDEMNIFICATION

10.1 What are the directors' responsibilities and liabilities under the law? Can those liabilities be covered by insurance? Can it be indemnified by the company or other related parties?

See paragraphs 4.1 and 4.2 for a discussion of board functions, responsibilities and liabilities. Most states generally allow the corporate charter to limit directors' personal liability to the corporation or its shareholders, except in the case of liability arising out of breaches of the duty of loyalty, intentional misconduct, illegal dividends or transactions from which the director derives an improper personal benefit.

Most state laws also expressly permit corporations to purchase insurance on behalf of current or former directors (as well as officers), including for non-indemnifiable matters, and nearly all companies purchase such insurance and negotiate appropriate coverage limits.

Indemnification, including expense reimbursement, is also expressly permitted and, in certain cases, is mandatory (such as where a director is wholly successful on the merits in defending against a suit involving his or her conduct as a director). Indemnification is generally not available to the extent the director acted in bad faith or against the interests of the corporation, and certain federal laws prohibit indemnification for specified violations. The SEC has taken the position that indemnification of officers, directors or control persons for Securities Act liability arising out of knowing violations of the law is unenforceable as against public policy. In the case of a derivative suit, indemnification may be limited to defence costs and not extend to monetary damages or amounts paid in settlement.

11. SHAREHOLDERS' DERIVATIVE SUITS

11.1 Is a shareholder's derivative suit provided for by law in your jurisdiction? How is it enforced by the shareholders?

Shareholders may, and often do, bring derivative suits on behalf of the corporation against the corporation's directors and officers pursuant to state corporation law. Such derivative suits are often used to allege breaches of fiduciary duties. Certain procedural requirements must be met in order to proceed with such suits, including, subject to certain exceptions, compliance with "demand" procedures whereby the corporation is given the opportunity to initiate the suit itself.

11.2 Have there been any recent relevant court cases on the subject?

US corporations and their directors and officers have increasingly faced duplicative shareholder derivative suits filed in multiple forums. A recent innovation responding to this problem is board adoption of exclusive forum selection byelaws, which require shareholders bringing derivative claims or other claims involving breaches of fiduciary duties (or otherwise addressing violations of state law or the internal affairs of the corporation) to file such lawsuits in a single forum, such as the issuer's state of incorporation. In June 2013, following uncertainty as to the validity of such byelaws, the Court of Chancery for the State of Delaware – where most US public companies are incorporated – declared the adoption of such byelaws to be a legitimate subject for board action, with shareholders retaining the right to challenge enforcement of such byelaws on a case-by-case, fact-specific basis.

12. SOCIAL INTEREST IN CORPORATE BEHAVIOUR

12.1 How is a company in your country expected to deal with the following issues: corporate social responsibility; gender, racial and social diversification; environmental issues; ecology and corruption?

Corporate social responsibility, including treatment of environmental, social and ethical issues, is an appropriate matter of business judgment for the

board, and the modern public company is expected to set, and meet, high standards of social responsibility. Related risks are expected to be addressed through robust risk oversight and management processes. Companies often voluntarily disclose performance and policies in this area. Specific disclosure requirements may apply in some of these areas, such as climate change, board diversity policies and environmental topics. Substantive law may also apply, such as for anti-bribery, anti-corruption and anti-discrimination rules or environmental mandates. Shareholder proposals often involve sustainability, environmental and social issues, including greenhouse gas emissions and renewable-energy concerns; international labour standards and human rights; and diversity, equality and non-discrimination issues, particularly with respect to sexual orientation.

13. REGULATORY FRAMEWORKS FOR PROFESSIONAL INVESTORS

13.1 How are professional investors (like pension funds or investment funds) required or encouraged to exercise their power for the good corporate governance of the company? Are they required to comply with rules like the Stewardship Code?

There is no direct equivalent of the UK Stewardship Code for professional investors in the USA. Shareholders may generally pressure management and exercise their rights freely and self-interestedly, even to the extent of imposing significant costs on the company or proposing actions that may not be in the best interests of the company and its shareholders collectively. Unlike the board of directors, non-controlling shareholders owe no fiduciary or other duties to their fellow shareholders or to the company. However, there is an emerging consensus that the US private sector is subject to significant short-termist pressures that operate to undermine long-term sustainability, investment and value creation and that it is incumbent upon investors to prioritise sustainable value creation over short-term measures.

There are also various organisations, both for-profit and nonprofit, that promote corporate governance policy agendas. The most prominent example is ISS and the other proxy advisory firms. While proxy advisory firms are not a source of law, their guidelines figure significantly in the corporate governance landscape and investor voting decisions, and, more than ever, with respect to mandated, albeit advisory, "say on pay" votes. These adviser firms exert pressure on companies to conform to governance standards they promulgate by issuing rankings and director election voting recommendations to each publicly traded company's shareholders based on the corporation's compliance with the advisory firm's published standards. Perhaps because of the problem of rational apathy – that is, because an individual shareholder bears all of the costs of becoming an informed voter but shares the benefits with all other shareholders, shareholders have little incentive to inform themselves – ISS wields outsized influence on corporate elections, especially among institutional investors such as pension funds. One recent study found that a recommendation from ISS to withhold a favourable vote in an uncontested director election correlates with a 20.9% decline in favourable

voting. In addition, a recent study sponsored by Stanford University found that companies were altering their compensation programmes to comply with proxy advisory firms' ever-evolving policies. ISS is estimated to control approximately 61% of the proxy advisory market, with Glass, Lewis & Co estimated to control approximately 36%. The US Congress, US Department of Labor and the SEC have raised questions regarding fiduciary responsibility in the context of the outsourcing of proxy voting decisions to proxy advisory firms, and in 2014 the SEC issued guidance addressing certain aspects of interactions between investment advisers and proxy advisory firms such as ISS, including requiring proxy advisory firms to disclose conflicts of interest and emphasising that when investment advisors vote on behalf of their clients, they must adopt reasonably designed protocols to ensure the proxies are voted in their clients' best interests. Significantly, certain major institutional investors, such as BlackRock Inc (which invests over $4.3 trillion in client assets) have indicated that they intend to reach proxy voting decisions on the basis of their own internal guidelines, independent of proxy advisory firms, and have sought to engage directly and pragmatically with companies.