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The International Comparative Legal Guide to:

Corporate Governance 2018

11th Edition

A practical cross-border insight into corporate governance

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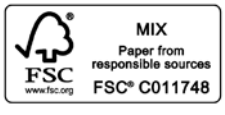

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Country Question and Answer Chapters:

EDITORIAL

Welcome to the eleventh edition of *The International Comparative Legal Guide to: Corporate Governance*.

This guide provides corporate counsel and international practitioners with a comprehensive worldwide legal analysis of the laws and regulations of corporate governance.

It is divided into two main sections:

One general chapter. This chapter provides an overview of Corporate Governance, Investor Stewardship and Engagement, particularly from a US perspective.

The guide is divided into country question and answer chapters. These provide a broad overview of common issues in corporate governance laws and regulations in 38 jurisdictions.

All chapters are written by leading corporate governance lawyers and industry specialists, and we are extremely grateful for their excellent contributions.

Special thanks are reserved for the contributing editor Sabastian V. Niles of Wachtell, Lipton, Rosen & Katz for his invaluable assistance.

Global Legal Group hopes that you find this guide practical and interesting.

The *International Comparative Legal Guide* series is also available online at www.iclg.com.

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Corporate Governance, Investor Stewardship and Engagement

Wachtell, Lipton, Rosen & Katz

Sabastian V. Niles

Corporate governance is increasingly conceived as a collaboration among corporations, shareholders and other stakeholders working together to achieve long-term value and resist short-termism. The below is an outline of synthesised principles intended to promote the common goal of facilitating sustainable long-term value creation through the governance roles of the board of directors and senior management, the role of investors in impacting corporate strategy and governance decisions within a framework of stewardship, and engagement between companies and investors to forge relationships built on transparency, trust and credibility. Companies and investors would tailor the application of these principles to their specific facts and circumstances.

Guiding Principles

Governance:

1. *Strategy, Management and Oversight*. The board of directors and senior management should jointly oversee long-term strategy and communication of that strategy, ensuring that the company pursues sustainable long-term value creation. The board of directors is responsible for monitoring company performance and for senior management succession.
2. *Quality and Composition of Board of Directors*. Directors should have integrity, competence and collegiality, devote the significant time and attention necessary to fulfil their duties, and represent the interests of all shareholders and other stakeholders. The board of directors as a whole should feature backgrounds, experiences and expertise that are relevant to the company's needs.
3. *Compensation*. Executive and director compensation should be designed to align with the long-term strategy of the company and incentivise the generation of long-term value, while dis-incentivising the pursuit of short-term results at the expense of long-term results.
4. *Corporate Citizenship*. Consideration should be given to shareholders and the company's broader group of stakeholders, including employees, customers, suppliers, creditors, and the community in which the company does business, in a manner that contributes in a direct and meaningful way to long-term value creation.

Stewardship:

1. *Beneficial Owners*. Institutional investors are accountable to the ultimate beneficial owners whose money they invest. As shareholders gain additional empowerment, they should use that power for the goal of long-term value creation for all shareholders.
2. *Voting*. Investors should actively vote on an informed basis consistent with the interests of their clients in the long-term success of the companies in which they invest.
3. *Investor Citizenship*. Investors should consider value-relevant sustainability, citizenship and ESG/CSR factors when developing investment strategies.

Engagement:

1. *By the Company*. The board of directors and senior management should engage with major investors on issues and concerns that affect the company's long-term value and be responsive to those issues and concerns.
2. *By Investors*. Investors should be proactive in engaging in dialogue with a company as part of a long-term relationship and should communicate their preferences and expectations.
3. *Shareholder Proposals and Votes*. Boards of directors should consider shareholder proposals and key shareholder concerns but investors should seek to engage privately before submitting a shareholder proposal.
4. *Interaction and Access*. Companies and investors should each provide the access necessary to cultivate engagement and long-term relationships.

Governance

Strategy, Management and Oversight. **The board of directors and senior management should jointly oversee long-term strategy and communication of that strategy, ensuring that the company pursues sustainable long-term value creation. The board of directors is responsible for monitoring company performance and for senior management succession.**

- The board of directors should oversee the company's management and business strategies to achieve long-term value creation, including having meaningful input over the company's capital allocation process and strategy. The board of directors should ensure that it understands the strategic assumptions, uncertainties, judgments and alternatives that underpin the company's long-term strategy.
- The board of directors sets the "tone at the top" to cultivate an ethical culture and demonstrate the company's commitment to integrity and legal compliance. Companies should have in place mechanisms for employees to seek guidance and alert management and the board of directors about potential or actual misconduct without fear of retribution.
- The board of directors should periodically review the company's bylaws, governance guidelines and committee charters and tailor them to promote effective board functioning. The board

of directors should be aware of the governance expectations of its major shareholders and take those expectations into account in periodic reviews of the company's governance principles. Boards of directors of companies that currently have dual or multiple class share structures should review these structures on a regular basis and establish mechanisms to end or phase out controlling structures at the appropriate time.

- The board of directors has two key roles with respect to management: oversight of management; and partnership with management. The board of directors should work to foster open, ongoing dialogue between members of the board and management. This dialogue requires directors to have access to senior management outside of board meetings. Management has an obligation to provide information to directors, and directors should seek clarification and amplification where necessary.
- The board of directors and senior management should jointly determine the company's reasonable risk appetite, oversee implementation of standards for managing risk and foster a culture of risk-aware decision-making. The board of directors should consider significant risks, including cybersecurity and reputational risks, to the company, but should not be reflexively risk averse; the board should seek proper calibration of risk to benefit the long-term interests of the company and its shareholders.
- Even with effective risk management, crises will emerge and test the board of directors, with potential situations ranging from unexpected departures of the CEO to risk management failures and major disasters. Each crisis is different, but in most instances when a crisis arises, directors are best advised to manage through it as a collegial body working in unison with the CEO and management team. Once a crisis starts to unfold, the board of directors needs to be proactive and provide careful guidance and leadership in steering the company through the crisis. If there is credible evidence of a violation of law or corporate policy, the allegation should be investigated and appropriate responsive actions should be taken. The board of directors, however, should be mindful not to overreact, including by reflexively displacing management or ceding control to outside lawyers, accountants and other outside consultants.
- The board of directors and senior management should maintain a close relationship with the CEO and monitor the performance of the CEO and key members of management.
- The board of directors and senior management should maintain a succession plan for the CEO and other key members of management. The board of directors should address succession planning on a regular rather than reactive basis. Direct exposure to employees is critical to the evaluation of the company's "bench strength".
- Companies should frame required quarterly reporting in the broader context of their articulated strategy and use quarterly financial results to show progress toward long-term plans. Companies should not feel obligated to provide earnings guidance.
- The board of directors should carefully consider extraordinary transactions and receive the information and time necessary to make an informed and reasoned decision. The board of directors should take centre stage in a transaction that creates a real or perceived conflict of interest between shareholders and management, including activist situations.

***Quality and Composition of Board of Directors*. Directors should have integrity, competence and collegiality, devote the significant time and attention necessary to fulfil their duties and represent the interests of all shareholders and other stakeholders. The board of directors as a whole should feature backgrounds, experiences and expertise that are relevant to the company's needs.**

- Every director should have integrity, strong character, sound judgment, an objective mind, collegiality, competence and the ability to represent the interests of all shareholders and other stakeholders.
- The composition of a board should reflect a complementary diversity of thought, background, skills, experiences, and tenures. The board of directors should develop a system for identifying diverse candidates, including women and minority candidates.
- A substantial majority of the board of directors should be independent. The board of directors should consider all relevant facts and circumstances when evaluating independence. Long-standing board service should not, by itself, disqualify a director from being considered independent.
- The board of directors should decide, based on the circumstances, whether to have separate or combined chairman and CEO roles. The board of directors should explain its decision to shareholders, and, if the roles are combined, should appoint a strong lead independent director. The lead independent director should serve as a liaison between the chairman of the board and the independent directors, preside over executive sessions, call meetings of the independent directors, guide the board's self-assessment or evaluation process, and guide consideration of CEO compensation and succession.
- The size of the board of directors will depend on the nature, size and complexity of the company and its state of development. In general, the board of directors should be large enough for a variety of perspectives and as small as practicable to promote open dialogue.
- Companies should consider limitations on the number of other boards of directors on which a director sits to ensure a director's ability to dedicate sufficient time to the increasingly complex and time-consuming matters that the board of directors and committees are expected to oversee.
- The composition of a board of directors should reflect a range of tenures. The board of directors should consider whether policies such as mandatory retirement ages or term limits are appropriate, but board refreshment should be tempered with the understanding that age and experience bring wisdom, judgment and knowledge. Substantive director evaluation and re-nomination decisions will serve better than arbitrary policies.
- Directors must spend the time needed and meet as frequently as necessary to discharge their responsibilities and should endeavour to attend all board and committee meetings, as well as the annual meeting of shareholders. The full board of directors should have input into the board agenda.
- Time for an executive session without the CEO or other members of management should be on the agenda for each regular board meeting.
- The board of directors should have a well-developed committee structure with clearly understood responsibilities. Decisions about committee membership should be made by the full board based on recommendations from the nominating and governance committee, and committees should meet all applicable independence and other requirements. Committees should keep the full board of directors and management apprised of significant actions.
- Companies should conduct a robust orientation for new directors and all directors should be continually educated on the company and its industry. Companies may find it useful to have an annual two- to three-day board retreat with senior executives to conduct a full review of strategy and long-range plans.
- The board of directors should evaluate the performance of individual directors, the full board of directors, and board committees on a continuing basis. Evaluations should be substantive exercises that inform board roles, succession planning, and refreshment objectives. Evaluations should be

led by the non-executive chair, lead independent directors, or appropriate committee chair, and externally facilitated evaluations may be appropriate from time to time.

***Compensation*. Executive and director compensation should be designed to align with the long-term strategy of the company and incentivise the generation of long-term value, while dis-incentivising the pursuit of short-term results at the expense of long-term results.**

- The board of directors should develop management compensation structures that are aligned with the long-term strategy and risk compliance policies of the company. A change in the company's long-term strategy or risk compliance policies should merit a re-evaluation of management compensation structures.
- Executive compensation should have a current component and a long-term component. A substantial portion should be in the form of stock or other equity, with a vesting schedule designed to ensure economic alignment with shareholders. In general, executives should be required to hold a meaningful amount of company stock during their tenure and beyond.
- The board of directors or its compensation committee should understand the costs of compensation packages and the maximum amount payable in different scenarios. In setting executive compensation, the compensation committee should take into account the position of the company relative to other companies, but use such comparison with caution, in view of the risk of an upward ratchet in compensation with no corresponding improvement in performance.
- Companies should be sensitive to the pay and employment conditions elsewhere in the company and take into account the pay ratios within the company. The board of directors should also consider the views of shareholders, including as expressed in "say-on-pay" votes, but should not abdicate its role in deciding what is best for the company.
- Companies should monitor, restrict or prohibit executives' ability to hedge the company's stock and oversee the adoption of policies to mitigate risks, such as compensation recoupment or clawbacks.
- Directors should receive compensation that fairly reflects the time commitment of public company board service, with appropriate benchmarking against peer companies. Independent directors should be equally compensated, although lead independent directors and committee chairs may receive additional compensation and committee fees may vary.
- Director compensation should be a mix of cash and equity, with appropriate stockholding requirements to promote continued alignment between directors and shareholders.
- If directors receive additional compensation not related to service as a director, such compensation should be disclosed and explained to shareholders.

***Corporate Citizenship*. Consideration should be given to shareholders and the company's broader group of stakeholders, including employees, customers, suppliers, creditors, and the community in which the company does business, in a manner that contributes to long-term value creation.**

- Companies should strive to be good citizens of the communities in which they do business and consider relevant sustainability issues in operating their businesses.
- The board of directors and senior management should integrate relevant ESG and CSR matters into strategic and operational planning.
- Companies have an important perspective to contribute to public policy dialogue. If a company engages in political activities, the board of directors should oversee such activities and consider whether to adopt a policy of disclosure of the activities.

Stewardship

***Beneficial Owners*. Investors are accountable to the beneficial owners whose money they invest. As shareholders gain additional empowerment, they should use that power for the goal of long-term value creation for all shareholders.**

- Investors should provide steadfast support for the pursuit of reasonable strategies for long-term growth and speak out against conflicting short-term demands.
- Investors should establish a firm-wide culture of long-term thinking and patient capital, including through the design of employee compensation to discourage the sacrifice of long-term value for short-term gains.
- Investors should adopt and disclose guidelines and practices that help them oversee the corporate governance practices of investee companies. Disclosure should include investors' long-term investment policies, evaluation metrics, governance procedures, views on quarterly reports and earnings guidance, and guidelines for relations with short-term activists.
- Investors should evaluate the performance of boards of directors, including director knowledge of governance and interest in understanding key shareholder concerns, as well as the board of directors' focus on a thoughtful long-term strategic plan.

***Voting*. Investors should actively vote on an informed basis consistent with the interests of their clients in the long-term success of the companies in which they invest.**

- Investors should devote sufficient time and resources to the evaluation of matters for shareholder vote in the context of long-term value creation.
- Investor votes should be based on the independent application of internal policies and guidelines. Investors may rely on a variety of information sources to support their evaluation. Third-party analyses and recommendations, including proxy advisory firms, should not substitute for individualised decision-making that considers the facts and circumstances of each company.
- Investors should disclose their proxy voting and engagement guidelines and report periodically on stewardship and voting activities.
- Investors should have clear procedures that help identify and manage potential conflicts of interest in their proxy voting and engagement and disclose such procedures.

***Investor Citizenship*. Investors should consider value-relevant sustainability, citizenship and ESG/CSR factors when developing investment strategies.**

- Investors should integrate material ESG factors into investment analysis and investment decisions.
- Investors should disclose their positions on ESG and CSR matters.

Engagement

***By the Company*. The board of directors and senior management should engage with major investors on issues and concerns that affect the company's long-term value and be responsive to those issues and concerns.**

- The board of directors and senior management should establish communication channels with investors and be open to dialogue on a "clear day". Boards should be responsive to shareholders and be proactive in order to understand their perspectives.

- Companies should clearly articulate for investors the company vision and strategy, including key drivers of performance, risk and evolution of business model.
- Companies should make adequate disclosures on a variety of topics, including: how compensation practices encourage and reward long-term growth; the director recruitment and refreshment process; succession planning; consideration of relevant sustainability, citizenship, and ESG/CSR matters; climate risks; political risks; corporate governance and board practices; anti-takeover measures; material mergers and acquisitions; and major capital commitments. Companies should explain the bases for their recommendations on the matters that are submitted to a shareholder vote.
- Companies should disclose their approach to human capital management: employee development, diversity and a commitment to equal employment opportunity; health and safety; labour relations; and supply chain labour standards; amongst other things.

***By Investors*. Investors should be proactive in engaging in dialogue with a company as part of a long-term relationship and should communicate their preferences and expectations.**

- Investors should actively listen to companies, participate in meetings or other bilateral communications and communicate their preferences, expectations and policies with respect to engaging with and evaluating companies. Investors should address and attempt to resolve differences with companies in a constructive and pragmatic manner that is intended to build trust and a common understanding and should give due consideration to the company's rationale.
- Investors should assume some accountability for the long-term interest of the company and its shareholders as a whole, provide companies with candid and direct feedback and give companies prompt notice of any concerns.
- Investors should invite companies to privately engage and work collaboratively with boards of directors and management teams to correct subpar strategies and operations. If an investor discloses a negative opinion about the company, it should state whether the investor first provided an opportunity for the company to engage privately.
- Investors should disclose their preferred procedures and contacts for engagement and establish clear guidelines regarding, and disclose, what further actions they may take in the event they are dissatisfied with the outcome of their engagement efforts.

***Shareholder Proposals and Votes*. Boards of directors should consider shareholder proposals and key shareholder concerns but investors should seek to engage privately before submitting a shareholder proposal.**

- Boards of directors should respond to shareholder proposals that receive significant support by implementing the proposed change if the board of directors believes it will improve governance, or providing an explanation as to why the change is not in the best long-term interest of the company if the board of directors believes it will not be constructive.
- Investors should raise critical issues to companies as early as possible in a constructive and proactive way, and seek to engage in a dialogue before submitting a shareholder proposal. Public battles and proxy contests have real costs and should be viewed as a last resort where constructive engagement has failed.
- Long-term shareholders should recommend potential directors if they know the individuals well and believe they would be additive to the board.
- Shareholders have the right to elect representatives and receive information material to investment and voting decisions. It is reasonable for shareholders to oppose re-election of directors who have persistently failed to respond to shareholder feedback.
- Boards of directors should communicate drivers of management incentive awards and demonstrate the link to long-term strategy and sustainable economic value creation. If the company clearly explains its rationale regarding compensation plans, shareholders should consider giving the company latitude in connection with individual compensation decisions. The board of directors should nevertheless take into account "say-on-pay" votes.

***Interaction and Access*. Companies and investors should each provide the access necessary to cultivate engagement and long-term relationships.**

- Engagement through disclosure is often the most practical means of engagement, though in other cases, in-person meetings or interactive communications may be more effective.
- Independent directors should be available to engage in dialogue with shareholders in appropriate circumstances without undermining the effectiveness of management to speak for and on behalf of the company.
- Investors' ultimate decision-makers should have access to the company, its management, and in some cases, its board of directors, and likewise the company should have access to investors' ultimate decision-makers.
- Boards of directors and senior management should consider cultivating relationships with the government, the community and other stakeholders.

USA

Wachtell, Lipton, Rosen & Katz

Sabastian V. Niles

1 Setting the Scene – Sources and Overview

1.1 What are the main corporate entities to be discussed?

This discussion focuses on publicly traded corporations incorporated under the laws of a state within the United States of America (for example, Delaware, the most common state of incorporation for U.S. companies) with securities listed on a U.S. stock exchange. Non-U.S. companies afforded "foreign private issuer" ("FPI") status whose securities are traded on a U.S. stock exchange are generally subject to the laws of their home state of incorporation and modified versions of U.S. stock exchange rules, but some U.S. laws will apply equally to FPIs and U.S. companies.

1.2 What are the main legislative, regulatory and other sources regulating corporate governance practices?

U.S. companies are governed by a variety of legal regimes relating to corporate governance matters. These consist of state law and federal statutory rules and regulations of various government agencies, including rules promulgated by the U.S. Securities and Exchange Commission (the "SEC") and self-regulatory organisations such as stock exchanges that impose requirements on companies whose securities are listed and trade on such exchanges. In addition to those sources of law, the U.S. corporate governance regime derives principles from a variety of non-legal sources.

State corporate law rules are derived from the laws of the state of incorporation and the organisational documents of each company. Each state has its own corporate code, with Delaware's General Corporation Law (the "DGCL") being the most common for large, publicly traded corporations, as the majority of U.S. public companies are incorporated under the laws of the state of Delaware. State corporate laws generally include a mix of mandatory provisions as well as "default" rules that may be modified by provisions in a company's certificate of incorporation (also referred to as a charter) or bylaws, enabling self-ordering and tailored governance features to be established on a company by company basis.

The primary sources of federal rules and regulations include the Securities Act of 1933 (the "Securities Act") and the Securities Exchange Act of 1934 (the "Exchange Act") and regulations promulgated by the SEC under those and other acts. The Securities Act regulates the offer and sale of securities, primarily through a disclosure-based approach that reaches some governance topics. The Exchange Act mandates certain annual, quarterly and interim reporting of financial and other material matters in addition to proxy disclosure and other requirements concerning shareholder votes and meetings. Other relevant federal regulations imposing disclosure and compliance requirements include the Sarbanes Oxley Act of 2002 ("SOX") and the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 ("Dodd-Frank"). SOX imposed a variety of substantive requirements to enhance the integrity of financial statements and reporting. The Dodd-Frank Act requires additional disclosure in proxy statements, non-binding shareholder votes on items related to executive compensation and facilitated greater access for shareholder-proposed director nominees to the company proxy.

Certain federal statutes and rule-makings provide for streamlined or reduced disclosure requirements on smaller public companies, and various pending pieces of legislation may further modify these federal statutes, especially as to Dodd-Frank matters. Particular areas of corporate practice are governed by specialised federal statutes as well that may have governance implications (for example, regulations promulgated by the Federal Reserve and other federal and state agencies with respect to banks and other financial institutions, and by other similar regulatory bodies in respect of communications, transportation and other regulated fields).

Stock exchange listing rules are issued by the New York Stock Exchange ("NYSE") and the NASDAQ, the two predominant U.S. stock exchanges. Companies must comply with these rules, many of which relate to corporate governance matters, as a condition to being listed on the exchange. Exchange listing rules address a variety of corporate governance matters, including director independence, the composition of various board committees, requirements to submit certain matters to a vote of shareholders beyond the requirements of state law and the company's organizational documents, regulation of dual-class stock structures and other special voting rights, topics to be covered by corporate governance guidelines and their publication, and certain requirements related to disclose on the corporation's public website. These rules are enforced by the threat of public reprimand from the exchanges, temporary suspension of trading for repeat offences and permanent delisting for perennially or egregiously non-compliant companies. Other stock exchanges are in the process of emerging and may have their own governance-related listing rules that go beyond or otherwise differ from NYSE and NASDAQ frameworks.

Non-legal sources such as industry and third-party best practice guidelines, recommendations, shareholder proxy advisory firms such as Institutional Shareholder Services ("ISS") and Glass Lewis, proposals advanced by shareholders and the evolving views of the institutional investor community provide additional sources of governance "principles". The investor community's views have

become particularly influential as the shareholder base of most US publicly traded corporations consists of an overwhelming majority of institutional shareholders, including index funds, mutual funds, hedge funds and pension funds. As a result, major institutional investors are increasingly developing their own independent views on preferred governance practices.

Because of the federal system of U.S. law, different sources of law are not always harmonised and corporations are often subject to different obligations to federal and state governments, regulators at each level of government and demands of other relevant bodies, such as the applicable stock exchange. This mosaic of rules and regulations, and the mechanisms by which they are implemented and enforced, make for an environment of frequent change and evolution.

1.3 What are the current topical issues, developments, trends and challenges in corporate governance?

In the US, questions about the basic purpose of corporations, how to define and measure corporate success, the weight given to stock prices as reflecting intrinsic value, and how to balance a wider range of stakeholder interests (including employees, customers, communities, and the economy and society as a whole) beyond the investor have become issues for concern and focus within corporate boardrooms and among policymakers and investors. In addition, many of the corporate governance issues facing boards today illustrate that corporate governance is inherently complex and nuanced, and less amenable to the benchmarking and quantification that was a significant driver in the widespread adoption of corporate governance "best practices". Prevailing views about what constitutes effective governance have morphed from a relatively binary, check-the-box mentality – such as whether a board is declassified, whether shareholders can act by written consent and whether companies have adopted majority voting standards – to tackling questions such as how to craft a well-rounded board with the skills and experiences that are most relevant to a particular corporation, how to effectively oversee the company's management of risk, and how to forge relationships with shareholders that meaningfully enhance the company's credibility. Today, many key corporate governance discussions focus on:

- How boards of directors and management teams can collaborate on developing, adjusting and communicating the company's long-term strategy and anticipating threats to progress.
- Assessing board strength, composition, performance and practices, including as to director expertise, average tenure, diversity, independence, character, and integrity and the board's role in succession planning and selection and oversight of the CEO.
- Recognising that vibrant board and corporate cultures are valuable assets, sources of competitive advantage and vital to the creation and protection of long-term value.
- How companies can effectively own business-relevant sustainability concerns, integrate relevant corporate social responsibility issues into decision-making and enhance disclosures in appropriate ways, while resisting one-size-fits-all approaches delinked from long-term business imperatives.
- The appropriate level of executive compensation and incentive structures, with awareness of the potential impact of compensation structures on business priorities and risk-taking, as well as investor and proxy advisor views on compensation.
- Oversight of risk management and compliance efforts and how risk is taken into account into business decision-making.
- Ensuring that the CEO and board are prepared to deal with takeover threats and shareholder activism.
- Cultivating strong relationships with investors that will support the company's execution of its strategy.
- Disintermediating the outsized influence of proxy advisory firms, including through efforts like the U.S. Investor Stewardship Group ("ISG") and increased investments by active managers and passive investors in their own governance teams and policies, even as proxy advisory firms retain significant power and influence over voting outcomes and company practices.

1.4 What are the current perspectives in this jurisdiction regarding the risks of short-termism and the importance of promoting sustainable value creation over the long-term?

"[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. In light of increasing pressure on public companies to promote short-term interests at the expense of long-term value and a decline in long-term investment, corporate governance is being increasingly viewed as a framework for aligning boards, management teams, investors and stakeholders towards long-term value creation and guarding against the perils of short-termism. In particular, there is increasing recognition that the value chain for alignment towards the long-term across public companies, asset managers, asset owners and ultimate beneficiaries (long-term savers and retirees) – each with their own time horizons, goals and incentives – is broken.

While some argue that short-termism is not a concern, additional academic and empirical evidence is being published showing the harms to GDP, national productivity and competitiveness, innovation, investor returns, wages and employment from the short-termism in US public markets. Absent evidence that private sector solutions to resist short-termism are gaining traction, legislation to promote long-term investment and regulation to mandate long-term oriented stewardship is expected to be considered.

2 Shareholders

2.1 What rights and powers do shareholders have in the strategic direction, operation or management of the corporate entity/entities in which they are invested?

In the U.S., a unitary board of directors, elected by shareholders and subject to fiduciary duties, is charged with overseeing the corporation's business and affairs. Accordingly, unlike in some jurisdictions where shareholders directly determine key business matters, such as corporate strategy, dividend and share repurchase policy, capital raising and material acquisitions, the U.S. model is director-centric, giving broad authority to the board of directors to exercise their business judgement on most matters and delegate day-to-day decision making to management. The U.S. model is director-centric, giving boards broad authority to exercise their business judgment on most matters and. Therefore, under U.S. state law, it is generally not necessary to seek shareholder approval of management decisions other than for fundamental changes. Under most state laws, shareholder approval is generally required to approve only relatively fundamental matters such as: (1) an amendment to the corporation's charter; (2) a merger; or (3) the sale of all or substantially all of the corporation's assets. Accordingly, in

most cases, including most asset sales and spinoffs, absent a special provision in the company's governing documents, shareholders do not have a right to vote on or ratify management's decisions. Under NYSE and NASDAQ exchange rules, shareholder approval may be triggered by share issuances involving: (1) 20% or more of the common stock or voting power of an issuer; (2) a change of control (often in the context of funding a large acquisition); and (3) issuances to certain related parties (subject in each case to certain limited exceptions). While shareholder approval is not required for most business matters, shareholders will typically engage with the management teams of U.S. companies and, in certain cases, with directors to provide input and perspectives to be considered by the board and management. If shareholders are not satisfied with the company's strategic direction, governance, operation or management, they may seek to change the composition of the board of directors (including through nominating their own candidates), register dissatisfaction through their votes, submit shareholder proposals (generally precatory) to be voted on by shareholders, inspect corporate books and records for proper purposes, pursue litigation and/or apply public and private pressure. See also question 2.3 regarding shareholder meetings.

In addition, Delaware law, as a general matter, requires shareholders to be treated equally (e.g., with respect to dividends) within share classes. As a result of this basic tenet of Delaware law, all shareholders, whether a minority or controlling shareholder, have a number of equal rights with respect to their shares, on a per share basis where applicable.

2.2 What responsibilities, if any, do shareholders have as regards to the corporate governance of the corporate entity/entities in which they are invested?

Generally none. However, concerns regarding the excesses of short-termism and shareholder power are giving rise to debates regarding whether shareholders should have governance-related responsibilities (even if not liability), such as through voluntary stewardship obligations and taking a long-term view with respect to governance matters. In addition, shareholders may vote on governance-related shareholder proposals and influence corporate governance that way too. See also question 2.4 regarding duties of controlling shareholders, which most U.S. companies do not have.

2.3 What kinds of shareholder meetings are commonly held and what rights do shareholders have as regards to such meetings?

Shareholders' meetings are typically held annually, as provided by state law and the organisational documents of the company. The DGCL, for example, requires annual meetings to be held for director elections and, if a company has not held such a meeting within 13 months of the prior year's meeting, shareholders may petition the Delaware courts to order such a meeting. Annual and special meetings may be convened by the board and, to the extent provided for in the company's charter or bylaws, shareholders satisfying certain ownership requirements (which vary across companies) may have the right to call special meetings of the shareholders or act by written consent in lieu of a meeting. Subject to the inclusion of any shareholder proposals or nominations that are submitted in accordance with state and federal law, the board sets the agenda of the meeting. Actions to be considered at a meeting may be binding or non-binding (precatory), and a typical annual shareholder meeting will include, at a minimum, election of directors, ratification of the company's selection of an outside auditor (voluntary) and the non-binding "say on pay" vote. Many companies have adopted advance notice bylaws that require shareholders to provide advance notice and satisfy other procedural requirements in order to propose business at a meeting.

Shareholders have the right to attend meetings in order to vote but more commonly vote by "proxy". Shareholders also have the right, subject to applicable law and satisfying disclosure and filing requirements when applicable, to communicate with other shareholders privately or publicly regarding matters to be considered at a meeting and may through their votes support, oppose or abstain from matters. 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.

Shareholder meetings are conducted in accordance with the company's charter and bylaws, including as to who 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 subject to a shareholder vote, the standard is voluntarily tightened to count only votes of unaffiliated or disinterested shareholders, but this is typically not legally required, and related party transactions are typically matters of board review and approval rather than the subject of a shareholder vote. 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 bylaws.

2.4 Do shareholders owe any duties to the corporate entity/entities or to other shareholders in the corporate entity/entities and can shareholders be liable for acts or omissions of the corporate entity/entities?

By nature of the corporate form, shareholders are not liable for the acts or omissions of the corporation and generally do not owe any duties to other shareholders or to the corporation. This lack of fiduciary duties on the part of shareholders to other shareholders has recently become a point of controversy, however, now that shareholders wield extraordinary influence over the decisions of – and regularly exert substantial pressure on – the boards of directors and management teams, including in situations where the interests and priorities of a given investor may not align with the interests of other shareholders. Concepts of stewardship – perhaps in time backed by potential liability or other enforcement mechanism – are in the early stages of emergence to address the concern that shareholders may be exercising power without responsibility.

While specific requirements often seen in Europe and other jurisdictions related to the protection of minority shareholders, such as mandatory tender offer obligations, are generally not hardwired into the U.S. rules and regulations, certain attention must be paid to minority shareholders when there is a controlling shareholder. Companies with a controlling shareholder (and such controlling shareholder) are generally subject to heightened legal scrutiny

and disclosure requirements with respect to transactions between such companies and their controlling shareholders. Corporate shareholders generally acquire fiduciary duties only if they control the corporation, which is rarely the case at most U.S. publicly traded companies in which shareholdings are widely dispersed and is itself a high bar, generally requiring ownership of more than a majority of the common stock or otherwise demonstrating "domination' of the corporation through actual exercise of direction over corporate conduct and, in the limited subset of cases where such shareholder-level fiduciary duty may apply, are generally limited to precluding a controlling shareholder from leveraging its position as such to extract benefits from the corporation at the expense of the minority shareholders or from transferring control to a known "looter".

2.5 Can shareholders seek enforcement action against the corporate entity/entities and/or members of the management body?

Yes. State law fiduciary duties of directors and officers are predominantly enforced by private actions led by plaintiffs' lawyers. These private actions generally fall into one of two categories: direct suits, typically in the form of class-action suits on behalf of a particular group of the corporation's shareholders (typically all shareholders who bought or sold during a particular period or all unaffiliated shareholders); and 'derivative' suits purportedly on behalf of the corporation itself. Putative class-action suits must satisfy the criteria under the Federal Rules of Civil Procedure or analogous provisions of state law before being permitted to proceed as a class action, including the numerousity of the class members, the commonality of legal and factual issues between members of the class, the typicality of the claims or defences of the representative parties to the class, and the fairness and adequacy of the representative parties' protection of the class interests. Derivative suits, creatures of state corporate law, provide a mechanism by which shareholder plaintiffs can, in theory, represent the corporation in suing the corporation's own board of directors or management, sometimes after complying with a 'demand' procedure in which the plaintiff must request that the corporation file suit and be rebuffed. In certain circumstances, especially when it can be shown that the board of directors is for some reason conflicted with respect to the alleged breach of duty, this 'demand' requirement is excused and the shareholder will be permitted to pursue a claim in the corporation's name without further enquiry.

Shareholders may also seek to have the SEC or other regulatory and enforcement bodies initiate investigatory and enforcement actions against companies and their personnel for violations of applicable law.

2.6 Are there any limitations on, or disclosures required, in relation to the interests in securities held by shareholders in the corporate entity/entities?

Certain state laws and provisions of a company's organisational documents may impose restrictions (or special approval requirements) on covered transactions between a company and significant shareholders. For example, Section 203 of the DGCL restricts the ability of a shareholder who owns 15% or more of a company's outstanding stock from engaging in certain business combination transactions with the company unless certain requirements are met or an exception applies.

Under the Hart-Scott-Rodino Antitrust Improvements Act of 1976, as amended (HSR Act) and relevant regulations hereunder, a shareholder's acquisition of voting securities in excess of specified thresholds usually requires prior notice to the Federeal Trade Commission and U.S. Department of Justice and clearance from regulatory authorities. In addition, investments and acquisitions by non-U.S. persons may also be regulated and restricted by applicable laws, such as where national security concerns are relevant through the auspicies of the Committee on Foreign Investment in the United States ("CFIUS") and implementing statutes and regulations, as well as in regulated industries where special considerations apply, such as aircraft, financial services, and communications media.

In addition, in terms of limitations on acquiring stakes in public companies, a critically important tool for enabling boards of directors to discharge their fiduciary duties in the face of the threat of hostile takeovers and significant accumulations under current law remains the shareholder rights plan, or "poison pill". The shareholder rights plan entails a dividend of special "rights" to each of the corporation's shareholders. In the event that a shareholder amasses equity ownership in excess of a predetermined threshold – often 10 to 15 per cent – without the approval of the board of directors, the rights held by every other shareholder 'trigger' and convert into the right to purchase stock of the corporation at a price substantially below the current market value. Alternatively, most rights plans provide that the board of directors may instead choose to exchange one share of common stock for each right held by shareholders other than the hostile bidder or activist shareholder. Either way, the result of this conversion or exchange is that the ownership position of the triggering shareholder is substantially diluted. The rights plan is the only structural takeover defence that allows a board to resist a hostile takeover attempt, and it has also been deployed in numerous activism situations. While it does not provide complete immunity from a takeover, it allows the board to control the process and provides the corporation with leverage to bargain for a higher acquisition price and the power to reject underpriced or otherwise inappropriate bids. It is also implemented exclusively by the board of directors and does not require shareholder approval, so it can be put in place in very short order. Whether or not to implement a rights plan in a given situation requires significant judgment, including taking into account investor reaction and the potential of ISS "withhold" recommendations if a rights plan has a term of greater than one year and is not subject to shareholder ratification. As a result, and because a rights plan can be adopted quickly, most corporations adopt a rights plan only after a threat appears – and prior to that time, the plan is kept 'on the shelf'. Keeping a rights plan on the shelf offers almost all of the protection of an active rights plan without any risk from an adverse ISS recommendation, but it can leave a corporation vulnerable to 'stealth acquisitions', in which an activist shareholder purchases just under 5 per cent of the company's stock, and then buys as much as possible on the open market within the next 10 days. Because Regulation 13D under the Securities Exchange Act gives shareholders 10 days after acquiring over 5 per cent of a company's stock to publicly disclose their ownership stake, this technique can result in an acquisition of a substantial portion of a company's equity before it is ever disclosed. Similarly, Regulation 13D does not cover all forms of derivatives. While all interests must be disclosed after a shareholder crosses the 5 per cent threshold, only some derivative interests are counted towards that threshold – generally, only those that are settled "in kind" (for stock of the corporation rather than for cash from the derivatives counterparty), and only those that can be exercised within the next 60 days. However, because an activist may accumulate its position in a corporation, without public disclosure, the board of directors may not have any warning of the activist's behaviour, and there is thus some risk that a company may not be able to adopt a rights plan in time to avoid a significant accumulation of stock in unfriendly and opportunistic hands.

With respect to disclosure, shareholders or groups of shareholders who own or acquire beneficial ownership of more than 5 per cent of a corporation's registered equity securities will also be required to file reports with the SEC under Regulation 13D. Investors who are not "passive" and are interested in influencing the Company, or are directors or officers, will be required to file a Schedule 13D within 10 days of the acquisition of more than 5 per cent in beneficial ownership of the Company's stock disclosing such ownership and the investment purpose (e.g., control intent), as well as amendments to report subsequent changes of more than 1 per cent. However, this 10-day filing requirement only starts ticking once the 5 per cent beneficial ownership threshold is reached. During the 10-day period between crossing the 5 per cent threshold and making the Schedule 13D filing, investors are permitted to further increase their ownership. This may involve making direct share purchases, as well as purchasing options and other derivatives. The 10-day window allows investors the ability to increase their interest in a company, in some cases quite dramatically, before the Schedule 13D alerts the market as to their ownership, even after crossing the 5 per cent threshold. Investors who have a "passive" interest in the Company and own more than 5 per cent but less than 20 per cent of the Company's stock or are otherwise exempt investors will be permitted to file the shorter Schedule 13G on a delayed schedule after year-end.

Section 13F of the Exchange Act requires institutional investment managers with over $100 million of assets under management to disclose their ownership of exchange-traded stock, shares of closed-end investment companies, shares of exchange-traded funds and certain convertible debt securities, equity options and warrants within 45 days after the end of each quarter, rather than equity positions as of the date of filing (resulting in a meaningful lag). Hedge funds who have transferred their equity positions into total return swaps or other derivatives prior to the end of a quarter may be able to avoid disclosing such positions under Schedule 13F, even if they still have economic exposure to the company. Confidential treatment of specific 13F positions may also be sought from the SEC while the investment manager is in the process of accumulating a position, and the SEC often grants such requests for Schedule 13F purposes, including in the context of activist or strategic accumulations.

As noted in question 3.4, Section 16 filings of transactions in the company's securities are required to be made of directors, officers and 10 per cent shareholders, and a company's annual proxy statement is required to specify the beneficial ownership in the company's equity securities of the company's directors, officers and 5 per cent shareholders.

2.7 Are there any disclosures required with respect to the intentions, plans or proposals of shareholders with respect to the corporate entity/entities in which they are invested?

Investors who do not have a "passive" intent and cross the 5 per cent threshold must publicly report their ownership positions and intent on a Schedule 13D. This disclosure must also address the shareholder's identity and background (including as to members of any filing group), source of financing include a discussion of the shareholder's plans or proposals with respect to the company as to a wide variety of matters (including as to extraordinary transactions, acquisitions and dispositions , or changes to the company's board or management, dividend policy, corporate structure or business) and set forth various arrangements, relationships or undersatndings regarding the company's securities and include certain items as filed exhibits. Material changes to these disclosures must also be publicly reported. In addition, under the U.S. antitrust rules, the acquisition of equity securities in excess of specified thresholds usually requires prior approval of regulatory authorities. Such approval, in turn, would require notice to be given to the targeted company of the intention to exceed this amount, effectively previewing to the target the shareholder's intention to not be a "passive investor" who would qualify for certain exemptions from such notice. While such filings may be confidential as to third parties, the target will be on notice of potential activity.

3 Management Body and Management

3.1 Who manages the corporate entity/entities and how?

U.S. 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. Directors must be natural persons under state law but need not be shareholders (though directors usually do have equity in the company). The board's basic responsibility is to exercise its business judgment and act in a manner reasonably believed to be in the best interests of the company and its shareholders. 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. Boards will also determine their own committee structures (including as to the exchange-managed committees, such as the nominating and governance committee, the compensation committee and the audit committee) and board leadership structures (for example, with respect to the identity of the chair of the board and whether the chair is a different person than the CEO). 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, and there is a legal framework for considering director's oversight duties. 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. Under U.S. law, 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.

3.2 How are members of the management body appointed and removed?

Members of the board of directors are elected by the shareholders, with the board having the right to alter the size of the board and appoint directors to fill vacancies, whether created by newly created directorships or resignations of incumbent directors. State law and the corporation's charter will establish the extent to which directors may be removed with or without cause, whether a shareholder vote is required for removal, the voting standard that must be met and any judicial authorities to remove directors. The board of directors, and not the shareholder body, appoints and removes corporate officers.

3.3 What are the main legislative, regulatory and other sources impacting on contracts and remuneration of members of the management body?

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, although tax rules in this regard are in a period of flux.

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 judgment 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.

Director compensation is also within the purview of the board of directors and the company's director compensation programme must be publicly disclosed. In recent years, there have been a handful of instances where outsized director compensation has been scrutinised and litigation has been pursued.

3.4 What are the limitations on, and what disclosure is required in relation to, interests in securities held by members of the management body in the corporate entity/entities?

Directors and officers (as well as 10 per cent shareholders) are required to file Section 16 forms reporting their beneficial ownership of the Company's registered securities. Such persons must file a Form 3 at the time the Company registers its securities (or within 10 days after becoming subject to the provision), a Form 4 within two days of changes in beneficial ownership, and a Form 5 within 45 days after the end of the Company's fiscal year to report any transactions that should have been reported earlier on a Form 4 or were eligible for deferred reporting.

Company insiders (including officers, directors and 10 per cent shareholders) can be forced to return any profits made from the purchase and sale (or sale and repurchase) of Company stock if both transactions occur within a six-month period and applicable exemptions do not apply.

To the extent a director or officer acquires or holds substantial equity positions, the limitations and disclosures that would apply generally to shareholders seeking to acquire or hold such positions as discussed in question 2.6 would also generally apply to the director or officer.

Companies may also establish (and enforce) company-specific stock ownership guidelines on directors and officers as well as restrictions on hedging or pledging of securities by such individuals.

3.5 What is the process for meetings of members of the management body?

In addition to regular meetings of the board of directors, boards may convene more frequently through special meetings of the board. Who may call a special board meeting is set forth in the company's organisational documents and governance guidelines. Notice and quorum requirements for board meetings are also set forth in the company's charter or bylaws (as is ability to waive notice requirements); the DGCL sets a majority of the total number of directors as the default quorum requirement. Board business may also be conducted through duly-constituted committees, which will also meet and act as needed and in accordance with notice and quorum requirements and committee charters. Boards may generally act by written consent in lieu of a meeting if such consent is unanimous.

3.6 What are the principal general legal duties and liabilities of members of the management body?

See questions 3.1, 3.8 and 5.1.

3.7 What are the main specific corporate governance responsibilities/functions of members of the management body and what are perceived to be the key, current challenges for the management body?

Effective boards typically perform dual roles: (i) advisor to and business partner of management; and (ii) monitor and overseer of management. 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 matters.
- Planning for and dealing with crises.
- Determining executive and director compensation.
- Interviewing and nominating director candidates and monitoring the board's performance and effectiveness.
- Reviewing the company's corporate governance practices and considering changes.
- Interviewing and nominating director candidates and monitoring the board's performance and effectiveness.
- Taking centre stage in any proposed transaction involving a conflict of interest with management.

- Setting high standards for corporate social responsibility.
- Monitoring compliance.
- Supporting long-term relationships with shareholders.
- Overseeing relations with government, community and other constituents.

See also questions 1.3 and 1.4.

3.8 Are indemnities, or insurance, permitted in relation to members of the management body and others?

Yes, and the available scope of indemnification and permitted insurance is broad. Under Section 145 of the Delaware General Corporation Law ("DGCL"), companies have extensive power to indemnify directors, officers and others against threatened, pending and completed legal actions. The only limitations in civil suits are first, that the indemnified person must have acted in good faith and with a reasonable belief that he or she was serving the best interests of the company, and second, that a company may not indemnify a person found liable to the company itself, unless a court rules otherwise. In addition to providing broad indemnification protections in corporate bylaws, U.S. companies commonly opt to protect their directors further by including in their corporate charters a provision eliminating or limiting personal liability for monetary damages for breach of fiduciary duty as a director. DGCL Section 102(b)(7) 3 permits such provisions so long as they do not eliminate or limit liability for any breach of the duty of loyalty, for acts or omissions not in good faith or which involve intentional misconduct or a knowing violation of law, for unlawful dividend payments or unlawful stock purchases or redemptions, or for any transaction from which the director derived an improper personal benefit. Charter provisions implemented pursuant to DGCL Section 102(b)(7) provide powerful protection for directors. Expense advancement is also an important and customary aspect of indemnification bylaws. DGCL Section 145(e) provides that companies may provide advance payment of expenses to officers and directors in defending legal actions upon receipt of an undertaking to repay the advancement if it is ultimately determined that the person is not entitled to indemnification. It further provides that companies have the discretion to determine the terms and conditions under which they wish to provide advancement to former directors and officers or other employees or agents. D&O insurance is also regularly provided to directors and officers at the company's expense and in some cases companies will enter into additional direct agreements with directors regarding indemnification.

3.9 What is the role of the management body with respect to setting and changing the strategy of the corporate entity/entities?

As discussed above, a unitary board of directors, elected by shareholders and subject to fiduciary duties, is charged with overseeing the corporation's business and affairs, including setting and directing corporate strategy. 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. In the U.S., hostile takeovers and shareholder activism can pose significant threats to U.S. corporations and execution of long-term corporate strategies, especially where such developments result in the capture of corporate control or influence over corporate policy by short-term oriented shareholders or bidders pursuing short-term profits, short-sighted breakups of a company, the excess return of capital to shareholders or incurrence of inadvisable amounts of leverage. In other situations, companies are able to navigate such situations effectively, including through making prudent adjustments to the corporate strategy in a manner that is responsive to the interests of long-term shareholders and other stakeholders and aligned with the long-term success of the company.

4 Other Stakeholders

4.1 What, if any, is the role of employees in corporate governance?

With respect to board composition, there are no requirements for employee or labour representation (or other mandated representation for particular constituencies) on the board of directors. In the M&A context, there are no required pre-notification or consultation provisions in the U.S. relating to employees. Some collective bargaining agreements ("CBA") may contain provisions that provide union employees with certain benefits, or the right to re-re-negotiate their CBA, in the event of a change in control, but these matters are contract-specific, however, are not legally required and do not provide a consent right on a bid.

4.2 What, if any, is the role of other stakeholders in corporate governance?

The interests of non-shareholder constituencies may be considered by the board 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, as well as broader constituencies such as the economy as a whole. As a practical matter, U.S. companies and large institutional investors are increasingly recognising that the long-term success of the company and its status as a durable enterprise requires giving due regard to the interests of important stakeholders, rather than focusing solely on the desires of shareholders.

4.3 What, if any, is the law, regulation and practice concerning corporate social responsibility?

While not a matter of significant legal regulation in the U.S. beyond compliance matters, 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 and substantive laws may also apply, such as for anti-bribery, anti-corruption and anti-discrimination rules or environmental mandates. Shareholder proposals increasingly 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. Where such proposals receive significant support, companies will have to determine whether and how to demonstrate responsiveness.

5 Transparency and Reporting

5.1 Who is responsible for disclosure and transparency?

The fundamental responsibility for a company's financial statements and disclosures rests with management and the independent auditor. Each NYSE-listed company must have an internal audit function to provide management and the audit committee with ongoing assessments of a company's risk management processes and systems of internal control. However, 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. Regulation FD generally prohibits selective disclosure of material information and requires public disclosure of information selectively disclosed to investors, subject to certain exceptions.

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 bylaws. 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.

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. 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. No aspect of an audit committee's role is more vital than its oversight of the audit process. An audit committee should have procedures in place to ensure that it stays abreast of evolving standards and best practices in this area. The PCAOB has promulgated strengthened independence and ethics rules and adopted auditing standards relating to the transparency and quality of audit reports, including requirements for enhanced disclosures of certain "critical audit matters", and the effectiveness of communications between an audit committee and the independent auditor.

5.2 What corporate governance-related disclosures are required?

Required governance-related disclosures include: information concerning the composition of the company's board of directors and management team; independence determinations regarding the board and director qualifications; the existence of a board diversity policy; corporate governance guidelines that address qualification standards for directors, responsibilities for directors, director access to management and independent advisers, compensation of directors, education and orientation of directors, management succession, and evaluation of board performance (as provided under NYSE rules); board committee structures and committee charters; the number of board meetings held and whether any directors attended less than 75 per cent of board and committee meetings; how shareholders may communicate with the board; whether the company has a code of ethics and any waivers of such codes; the board's leadership structure and role in risk oversight; risks arising from compensation policies that may have a material adverse effect on the company; related party transactions; and other matters.

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, governance practices, director and executive compensation, auditor information and other matters.

5.3 What is the role of audit and auditors in such disclosures?

See question 5.1.

5.4 What corporate governance-related information should be published on websites?

The websites of major public companies will typically include corporate governance-related information, including the company's organisational documents (charter and bylaws), key corporate governance guidelines and policies including as to director independence criteria, committee charters for the audit, compensation and nominating and governance board committees, business codes of conduct, proxy statements and annual reports, Section 16 filings reporting trades by directors and officers and information concerning the company's board of directors and management teams. While not generally required, companies are also increasingly posting sustainability-related information, corporate social responsibility initiatives and progress publicly on company websites and bringing such matters to the attention of investors. While stock exchange rules require or provide the option of posting certain governance information to the company's website, most company websites go beyond what is strictly required.

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In addition to serving as Consulting Editor for the New York Stock Exchange's Corporate Governance Guide, Sabastian writes frequently on corporate law matters and has been a featured speaker at corporate strategy and investor forums. His speaking engagements have addressed topics such as Shareholder Activism; The New Paradigm of Corporate Governance; Hostile Takeovers; Strategic Transactions and Governance; M&A Trends; Board-Shareholder Engagement; Confidentiality Agreements in M&A Transactions; Negotiating Strategic Alliances with U.S. Companies; Current Issues in Technology M&A; Corporate Governance: Ethics, Transparency and Accountability; and Developments in Cross-Border Deals.

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