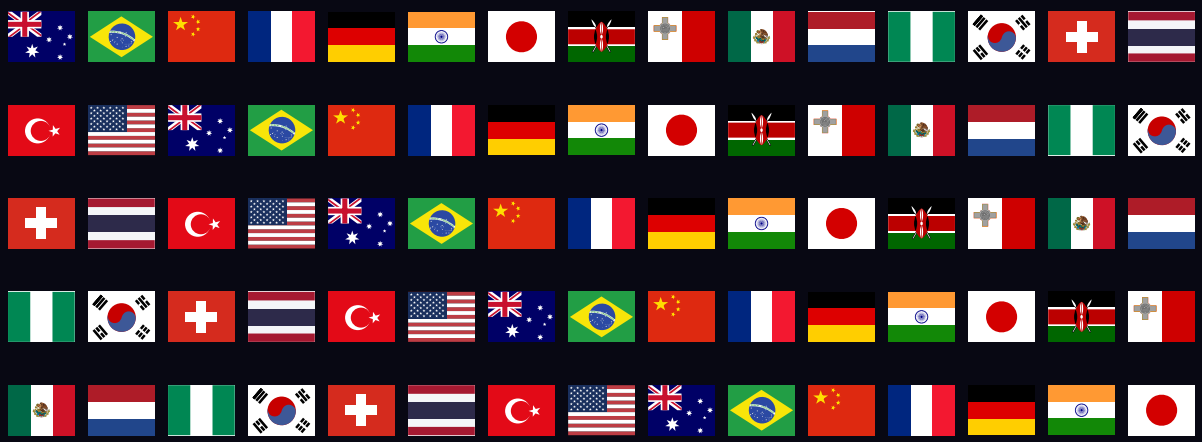
CORPORATE GOVERNANCE

USA



LEXOLOGY
Getting The Deal Through

Consulting editor
Sidley Austin LLP

Corporate Governance

Consulting editors

Holly J Gregory

Sidley Austin LLP

Quick reference guide enabling side-by-side comparison of local insights into corporate governance issues worldwide, including sources of rules and practice; responsible agencies and notable opinion formers; shareholder powers, decisions, meetings, voting, duties and liabilities; employee role in governance; corporate control issues; board structure and composition, duties, leadership, committees, meetings and evaluation; director and senior management remuneration; director protections; disclosure and transparency; hot topics, such as shareholder engagement, and sustainability, pay ratio and gender gap reporting; and other recent trends.

Generated 24 May 2023

Table of contents

Contributors

USA

Holly J Gregory
holly.gregory@sidley.com
Sidley Austin LLP

SIDLEY

Claire H Holland
cholland@sidley.com
Sidley Austin LLP

SOURCES OF CORPORATE GOVERNANCE RULES AND PRACTICES

Primary sources of law, regulation and practice

What are the primary sources of law, regulation and practice relating to corporate governance? Is it mandatory for listed companies to comply with listing rules or do they apply on a 'comply or explain' basis?

In the United States, there are two primary sources of law and regulation relating to corporate governance.

State corporate laws

State corporate law – both statutory and judicial – governs the formation of privately held and publicly traded corporations and the fiduciary duties of directors. Delaware is the most common state of incorporation. Because Delaware law and interpretation are influential in other states, the Delaware General Corporation Law (DGCL) is used in this chapter as the reference point for all state law discussion. Shareholder suits are the primary enforcement mechanism of state corporate law.

Several states have enacted or are considering legislation that would encourage greater board diversity or require disclosure about board diversity.

Federal securities laws

On the federal level, the primary sources are the Securities Act of 1933 (the Securities Act) and the Securities Exchange Act of 1934 (the Exchange Act), each as amended. The Securities Act regulates all offerings and sales of securities, whether by public or private companies. The Exchange Act addresses many issues, including the organisation of the financial marketplace generally, the activities of brokers, dealers and other financial market participants and, as to corporate governance, specific requirements relating to the periodic disclosure of information by publicly held, or 'reporting', companies. A company becomes a reporting company under the Exchange Act when its securities are listed on a national securities exchange or when it has total assets exceeding US$10 million and a class of securities held of record by more than 2,000 persons or a maximum of 500 persons who are not sophisticated ('accredited') (with some exclusions). Both the Securities Act and the Exchange Act have addressed questions of corporate governance primarily by mandating disclosure, rather than through normative regulation.

The Public Company Accounting Reform and Investor Protection Act of 2002 (the Sarbanes–Oxley Act) was enacted in July 2002 in response to the corporate failures of 2001 and 2002. The Sarbanes–Oxley Act, which applies to all reporting companies (whether organised in the United States or elsewhere) with US-registered equity or debt securities, amends various provisions of the Exchange Act (and certain other federal statutes) to provide direct federal regulation of many matters that traditionally had been left to state corporate law or addressed by federal law through disclosure requirements. Under the Sarbanes–Oxley Act, many aspects of corporate governance that were previously addressed, if at all, through stock market listing requirements, best practice standards or policy statements from the Securities and Exchange Commission (SEC) are now subjects of direct binding law. Since 2002, the SEC has promulgated a number of rules that implement provisions of the Sarbanes–Oxley Act.

The Dodd–Frank Wall Street Reform and Consumer Protection Act of 2010 (the Dodd–Frank Act) was enacted in July 2010 in response to the financial crisis in 2008 and 2009. The Dodd–Frank Act is intended to significantly restructure the regulatory framework for the US financial system and also extends federal regulation of corporate governance for all public companies. The SEC has promulgated several rules that implement provisions of the Dodd–Frank Act. Ongoing rule-making by the SEC and national securities exchanges are required for full implementation.

The Jumpstart Our Business Startups Act of 2012 (the JOBS Act) was enacted in April 2012 to, inter alia, facilitate private capital formation and ease reporting requirements that may apply to 'emerging growth companies' after the initial public offering. The JOBS Act requires the SEC to undertake various initiatives, including rule-making and studies touching on capital formation, disclosure and registration requirements.

Listing rules provide an additional source of corporate governance requirements. To list a security on any of the three major listing bodies – the New York Stock Exchange (NYSE), NYSE American (formerly known as the American Stock Exchange and NYSE MKT) or the Nasdaq Stock Market (Nasdaq) – a company must agree to abide by specific corporate governance listing rules. In 2003, the SEC approved significant amendments to both the NYSE and Nasdaq corporate governance listing rules as described below. The Dodd–Frank Act requires amendments to corporate governance listing rules to be made by the NYSE and Nasdaq.

In addition, a number of corporate governance guidelines and codes of best practice recommend how public company boards should organise their structures and processes. The American Law Institute's Principles of Corporate Governance: Analysis and Recommendations present a thorough discussion of governance practices from a legal perspective. Other influential recommendations from the business community include:

- the National Association of Corporate Directors (NACD):
  - Key Agreed Principles (developed in collaboration with Business Roundtable and the Council of Institutional Investors (CII));
  - Report of the NACD Blue Ribbon Commission on Director Professionalism;
  - Report of the NACD Blue Ribbon Commission on Building the Strategic-Asset Board;
- the Business Roundtable: Principles of Corporate Governance;
- the Conference Board, Commission on Public Trust and Private Enterprise: Findings and Recommendations; and
- the Commonsense Principles of Corporate Governance issued by a coalition of high-profile representatives of leading public companies and institutional investors in 2016 and updated in the form of Commonsense Principles 2.0 in 2018.

The investor community has also issued a number of corporate governance guidelines, codes of best practices and proxy voting policies that are increasingly influential. These include:

- the CII: Policies on Corporate Governance;
- the Teachers Insurance and Annuity Association of America-College Retirement Equities Fund (TIAA)/Nuveen: TIAA Policy Statement on Responsible Investing;
- the California Public Employees' Retirement System (CalPERS): Governance and Sustainability Principles;
- proxy voting policies of large institutional investors, such as BlackRock, Vanguard, State Street and Fidelity; and
- the Investor Stewardship Group, Corporate Governance Principles for US Listed Companies and Stewardship Principles issued in 2017 by a group of US-based institutional investors and global asset managers representing more than US$20 trillion in assets under management.

In addition, proxy advisory firms, such as Institutional Shareholder Services (ISS) and Glass Lewis, have developed proxy voting guidelines that set forth the voting recommendations that these firms will make on particular issues to be voted on by shareholders. These guidelines are based on what these firms consider to be 'best practices' and have also become influential.

Unlike many corporate governance codes in the European Union and other parts of the world that call for voluntary adoption of their substantive provisions or 'comply or explain' disclosure requirements, the corporate governance rules in the United States are generally mandatory. However, most US federal securities regulation of listed issuers is

disclosure-driven and, even where substantive matters are addressed, disclosure is most often used as the vehicle to achieve a desired objective or to add transparency to matters deemed worthy of public attention. For example, with respect to executive compensation, the rules provide for extensive disclosure requirements rather than substantive requirements.

Law stated - 12 May 2023

Responsible entities

What are the primary government agencies or other entities responsible for making such rules and enforcing them? Are there any well-known shareholder or business groups, or proxy advisory firms, whose views are often considered?

The primary means of enforcing state corporate law is through derivative suits initiated by shareholders. At the federal level, the SEC has the power to regulate, implement and enforce the Securities Act and the Exchange Act (including the Sarbanes–Oxley Act, the JOBS Act and relevant provisions of the Dodd–Frank Act). In addition, the Sarbanes–Oxley Act created the Public Company Accounting Oversight Board (PCAOB) to regulate the services accounting firms provide to companies. The SEC oversees the PCAOB, appoints its members and must approve any rules adopted by the PCAOB.

Several states have enacted or are considering legislation that would encourage greater board diversity or require disclosure about board diversity. Typically the state statute requires periodic reporting to the Secretary of State who is required to publicly report on corporate compliance with the board diversity requirements.

The CII is an influential association of public and private pension funds that often pushes for governance reforms. Pension funds have traditionally been the most activist of the institutional investors, working both in concert and individually. Influential pension funds include TIAA/Nuveen and CalPERS – respectively, among the largest private and public pension funds in the world. The New York City Pension Funds have become increasingly active in recent years with highly effective campaigns urging companies to adopt proxy access and prioritise board composition, diversity and refreshment, and disclosure of workforce diversity. In addition, Vanguard Group, BlackRock Inc and State Street Global Advisors, three of the United States' largest institutional investors, have recently become more assertive in pushing for corporate governance reforms and increased director-shareholder engagement at the companies in which they invest.

The views of proxy advisory firms ISS and Glass Lewis are also influential.

Law stated - 12 May 2023

THE RIGHTS AND EQUITABLE TREATMENT OF SHAREHOLDERS AND EMPLOYEES

Shareholder powers

What powers do shareholders have to appoint or remove directors or require the board to pursue a particular course of action? What shareholder vote is required to elect or remove directors?

Under state corporate law, shareholders generally have the right to elect directors (see the Delaware General Corporation Law (DGCL), section 216).

For many years, it was common practice for directors to be elected by a plurality of shareholders that can either vote in favour of, or withhold their votes from, the director candidates nominated by the board; 'withheld' votes are not counted. Accordingly, absent a contested election, the candidates nominated by the board are automatically elected whether or not a majority of shareholders vote for them. From the mid-2000s onward, shareholders have pressed companies for the ability to veto the election of a particular director nominee or nominees in the context of an

uncontested election. This can be achieved through the adoption of charter or by-law provisions requiring that director nominees receive the approval of a 'majority of the votes cast' to be elected, or, in lieu of a charter or by-law provision, the adoption of corporate policies that effectively require a director who has not received a majority of the votes cast to resign. In 2006, the Delaware legislature adopted amendments to the DGCL that facilitate both of these options. Specifically, the amended DGCL, section 141(b) expressly permits a director to irrevocably tender a resignation that becomes effective if he or she fails to receive a majority vote in an uncontested election. The amended DGCL, section 216 provides that a by-law amendment adopted by shareholders specifying the vote required to elect directors may not be repealed or amended by the board alone (generally, by-law provisions may be amended by the board).

The proportion of companies in the Standard & Poor's (S&P) 500 that have adopted some form of majority voting in uncontested director elections has increased dramatically from 16 per cent in 2006 to nearly 90 per cent in 2022. The source of the S&P 500 company data referenced in this chapter is the 2022 Spencer Stuart Board Index.

Shareholders can also nominate their own director candidates either before or at the annual general meeting (AGM), although most public companies adopt 'advance notice' bylaws that require nominations to be received by the company several months before the AGM. To solicit the proxies needed to elect their candidates, however, at a company that has not adopted 'proxy access' a shareholder must mail to all other shareholders, at the shareholder's own expense, an independent proxy solicitation statement that complies with the requirements of section 14 of the Securities Exchange Act of 1934 (the Exchange Act). Given these constraints, independent proxy solicitations are rare and usually undertaken only in connection with an attempt to add designated directors to the board and/or seize corporate control. In November 2021, the SEC adopted changes to the federal proxy rules to require the use of 'universal' proxy cards, which allow shareholders to vote for a mix of management and dissident nominees in a contested director election. The rules are now effective for shareholder meetings held after 31 August 2022.

In addition, shareholders generally have the right to remove directors with or without cause or, where the board is classified, only for cause (unless the certificate of incorporation provides otherwise); the vote required to remove directors is a majority of the shares then entitled to vote at an election of directors (subject to certain modifications, for example, where the company has adopted cumulative voting in director elections) (see DGCL, section 141(k)). However, as many publicly held companies do not permit shareholders to call special meetings or act by written consent, this power can be difficult to exercise in practice.

Shareholders' liability for corporate actions is generally limited to the amount of their equity investment. In keeping with their limited liability, shareholders play a limited role in the control and management of the corporation. A number of corporate decisions require shareholder approval. In addition, shareholders can typically enjoin ultra vires acts (see DGCL, section 124) and vote on certain issues of fundamental importance at the AGM, including the election of directors (see DGCL, section 216).

Law stated - 12 May 2023

Shareholder decisions

What decisions must be reserved to the shareholders? What matters are required to be subject to a non-binding shareholder vote?

Under state corporate law, shareholders typically have a right to participate in the following types of decisions:

- election of directors, held at least annually (see DGCL, sections 141(d), 211(b) and 216);
- filling of board vacancies and newly created directorships, if so provided in the certificate of incorporation or by-laws (see DGCL, section 223);
- removal of directors (see DGCL, section 141(k));
- approval or disapproval of amendments to the corporation's certificate of incorporation (which requires prior

board approval) or by-laws, although the board is also typically authorised (in the certificate of incorporation) to amend the by-laws without shareholder approval (see DGCL, sections 109, 241 and 242); and
- approval or disapproval of fundamental changes to the corporation not made in the regular course of business, including mergers, consolidations, compulsory share exchanges, or the sale, lease or exchange of all or substantially all of the corporation's property and assets (see, for instance, DGCL, sections 251(c) and 271).

Other issues that may be brought to shareholder vote include:

- approval of certain business combinations with interested shareholders that would otherwise be prohibited (see DGCL, section 203(a)(3));
- approval of conversion to a different type of entity (see DGCL, section 266);
- approval of transfer, domestication or continuance in a foreign jurisdiction (see DGCL, section 390);
- approval of dissolution and revocation of dissolution (see DGCL, sections 275 and 311); and
- ratification of defective corporate acts that would have required shareholder approval (see DGCL, section 204(c)).

Shareholders may also be asked by the board to approve certain matters, including:

- approval of interested director or officer transactions (see DGCL, section 144);
- the making of determinations that indemnifying a director or officer is proper (see DGCL, section 145); or
- if so provided in the certificate of incorporation, the making of determinations that the consideration for which shares of stock with or without par value may be issued, and treasury stock disposed of (see DGCL, section 153).

Since 2011, the Dodd–Frank Wall Street Reform and Consumer Protection Act of 2010 has required US public companies to conduct separate shareholder advisory votes on:

- executive compensation – to be held at least once every three calendar years (annual votes are typical);
- whether the advisory vote on executive compensation should be held every year, every two years or every three years – to be held at least once every six calendar years; and
- certain 'golden parachute' compensation arrangements in connection with a merger or acquisition transaction that is being presented to shareholders for approval.

The rules of the New York Stock Exchange (NYSE) and Nasdaq Stock Market (Nasdaq) also require that shareholder approval be obtained prior to:

- any adoption of an equity compensation plan pursuant to which officers or directors may acquire stock, subject to limited exceptions;
- issuance of common stock to directors, officers or substantial security holders if the number of shares of common stock to be issued exceeds either 1 per cent of the number of shares of common stock or 1 per cent of the voting power outstanding before the issuance, with some exceptions including if the issuance is a cash sale for a price that is at least a specified minimum price (NYSE), or could result in an increase in outstanding common shares or voting power of 5 per cent or more (Nasdaq);
- issuance of common stock that will have voting power equal to or greater than 20 per cent of the voting power prior to such issuance or that will result in the issuance of a number of shares of common stock that is equal to or greater than 20 per cent of the number of shares of common stock outstanding prior to such issuance, subject to certain exceptions including any public offering for cash or if the issuance is in connection with an acquisition

of the stock or assets of another company and the issuance alone or when combined with any other present or potential issuance of common stock in connection with such acquisition is equal to or exceeds the 20 per cent threshold; and

- issuance of securities that will result in a change of control of the company.

Law stated - 12 May 2023

Disproportionate voting rights

To what extent are disproportionate voting rights or limits on the exercise of voting rights allowed?

Under state law, a corporation may issue classes of stock with different voting rights, limited voting rights and even no voting rights, if the rights are described in the corporation's certificate of incorporation (see DGCL, section 151). If, however, a corporation issues a class of non-voting common stock, it must have an outstanding class of common shares with full voting rights.

The NYSE and Nasdaq listing rules also permit classes of stock with different voting rights; however, the listing rules prohibit listed companies from disparately reducing or restricting the voting rights of existing shareholders unilaterally.

In 2017, two major stock index providers (S&P Dow Jones and FTSE Russell) announced changes to their index eligibility requirements that would exclude most companies going public with multiple classes of stock from the primary indices in the United States. Nevertheless, some companies in the technology industry and other industries have subsequently gone public with dual-class or multi-class stock.

Although it prefers equal voting rights, BlackRock acknowledges that newly public companies may benefit from a dual-class structure but endorses a limited duration through a sunset provision or periodic approval by shareholders.

The Council of Institutional Investors (CII) and the California Public Employees' Retirement System have expressed their opposition to non-voting shares. The CII is part of the Investor Coalition for Equal Votes, which was launched in June 2022 by the UK pension fund Railpen and several US pension funds, which encourages IPO companies with dual-class stock structures to include a reasonable time-based 'sunset' provision (ie, seven or fewer years) on the super-voting shares.

ISS will generally recommend voting against or withholding votes from individual directors, committee members or the entire board (except new nominees, who should be considered on a case-by-case basis) if the company employs a common stock structure with unequal voting rights. There are certain limited exceptions to this policy, including for newly-public companies with a sunset provision of no more than seven years from the date of going public.

Glass Lewis believes multi-class voting structures are typically not in the best interests of common shareholders. In the case of a board that adopts a multi-class share structure in connection with an IPO, Glass Lewis will generally issue negative recommendations against directors at the first annual meeting after the company has become public if the company does not submit the multi-class structure to a shareholder vote or adopts a multi-class capital structure that is not subject to a reasonable sunset provision (ie, generally seven years or less). Furthermore, Glass Lewis will generally recommend voting against the governance committee chair at companies with a multi-class share structure and unequal voting rights if the multi-class share structure is not subject to a reasonable sunset provision.

Glass Lewis will generally recommend that shareholders vote in favour of recapitalisation proposals that would eliminate dual-class share structures. Similarly, Glass Lewis will generally recommend voting against proposals to adopt a new class of common stock.

Law stated - 12 May 2023

Shareholders' meetings and voting

Are there any special requirements for shareholders to participate in general meetings of shareholders or to vote? Can shareholders act by written consent without a meeting? Are virtual meetings of shareholders permitted?

Generally, all shareholders, at the record date set by the board, may participate in the corporation's annual general meeting (AGM), and are entitled to vote (unless they hold non-voting shares) in person or by proxy (see DGCL, sections 212(b) and (c) and 213). The proxy appointment may be in writing (although there is no particular form mandated by the DGCL) or provided by telephone or electronically.

In addition, section 14 of the Exchange Act and related SEC regulations set forth substantive and procedural rules with respect to the solicitation of shareholder proxies for the approval of corporate actions at AGMs and special shareholders' meetings. Foreign private issuers are exempt from the provisions of section 14 and related regulations insofar as they relate to shareholder proxy solicitations.

Shareholders may act by written consent without a meeting unless the certificate of incorporation provides otherwise (see DGCL, section 211(b)). The majority of companies in the S&P 500 do not permit shareholder action by written consent.

DGCL, section 211 permits a Delaware corporation to hold a meeting of shareholders virtually if it adopts measures to enable shareholders to participate in and vote at the meeting and verify voter identity, and if it maintains specified records. Prior to 2020, a small but growing number of US companies held virtual annual shareholder meetings, typically in one of two formats: exclusively online with no ability for a shareholder to attend an in-person meeting; or a hybrid approach whereby an in-person meeting is held that is open to online participation by shareholders who are not physically present at the meeting. The primary benefits of virtual shareholder meetings are increased shareholder participation and cost savings.

The number of US companies that held virtual-only annual shareholder meetings skyrocketed in 2020 when the covid-19 pandemic made in-person shareholder meetings impossible or inadvisable. Virtual shareholder meetings, both virtual-only and hybrid format, are becoming commonplace practice as companies and service providers gain more experience.

Currently, ISS prefers a hybrid approach, but it does not have a policy to recommend voting against directors at companies that hold virtual-only meetings. ISS will generally vote for management proposals allowing for virtual meetings so long as they do not preclude in-person meetings. ISS encourages companies holding virtual-only meetings to disclose the circumstances under which virtual-only meetings would be held, and provide shareholders with comparable rights and opportunities to participate electronically as they would have during an in-person meeting. ISS will vote case-by-case on shareholder proposals concerning virtual-only meetings, considering the scope and rationale of the proposal, and concerns identified with the company's prior meeting practices.

Similarly, Glass Lewis prefers a hybrid approach. In egregious cases, Glass Lewis may recommend voting against governance committee members where a company chooses to hold a virtual-only shareholder meeting but does not provide sufficient disclosure in its proxy statement assuring shareholders will be afforded the same rights and opportunities to participate as they would at an in-person meeting.

Some large institutional investors (eg, CalPERS and the New York City Pension Funds) oppose virtual-only shareholder meetings and may vote against directors at companies that hold them.

In March 2022, the CII updated its corporate governance policies to give companies more flexibility with respect to the format of their shareholder meetings. The updated policies state that companies should acknowledge that many investors prefer in-person meetings but should have 'the flexibility to choose an in-person, hybrid or virtual-only format

depending on their shareowner base and current circumstances.' Companies should use virtual technology 'as a tool for broadening, not limiting, shareowner meeting participation' and should disclose the circumstances under which a virtual-only meeting would be held and provide shareholders participating virtually with comparable rights and opportunities as those whom attend in person.

In January 2022, the SEC staff issued updated guidance for conducting shareholder meetings in light of covid-19 concerns. The staff encourages companies to provide shareholder proponents or their representatives with the ability to present their shareholder proposals through alternative means (eg, by phone) if they are unable to appear at the meeting to present them in person.

In 2022, Delaware made a number of changes to the DGCL impacting shareholder meetings. First, Delaware amended section 219 of the DGCL such that the list of shareholders entitled to vote is no longer required to be available during the course of the shareholder meeting. Instead, companies will need to make the list available for examination for a 10-day period ending on the day before the meeting date, either on a reasonably accessible electronic network or during business hours at the company's principal place of business. Second, Delaware amended section 222 of the DGCL to clarify that notice of a shareholder meeting is governed by section 232 of the DGCL, which expressly allows for the electronic delivery of notices. Section 222 was also amended to permit adjournments taken to address technical failures and continue a meeting remotely.

Law stated - 12 May 2023

Shareholders and the board

Are shareholders able to require meetings of shareholders to be convened, resolutions and director nominations to be put to a shareholder vote against the wishes of the board, or the board to circulate statements by dissident shareholders?

Generally, state law provides that every shareholder has the right to petition the court to compel an AGM if the board has failed to hold the AGM within a specified period of time (see DGCL, section 211). Special shareholders' meetings may be called by anyone authorised to do so in the company's certificate of incorporation or by-laws. The majority of S&P 500 companies permit shareholders meeting a minimum beneficial ownership requirement (such as 20 per cent or 10 per cent) to call special meetings.

Any shareholder of a reporting company who is eligible to bring matters before a shareholders' meeting under state law and the company's certificate of incorporation and by-laws may, at the shareholder's own expense, solicit shareholder proxies in favour of any proposal including director nominations. Such shareholder proxy solicitations must comply with section 14 of the Exchange Act and related SEC regulations, but need not be approved by the board.

Under circumstances detailed in Rule 14a-8 under the Exchange Act, a reporting company must include a shareholder's proposal in the company's proxy materials and identify the proposal in its form of proxy. The shareholder may also submit a 500-word supporting statement for inclusion in the company's proxy solicitation materials. This allows the proponent to avoid the costs associated with an independent solicitation. The SEC adopted rule amendments in 2020 that increased the eligibility requirements for submitting a shareholder proposal to a tiered approach depending on the level of ownership and the relevant holding period: at least US$2,000 if held for at least three years, at least US$15,000 if held for at least two years, and at least US$25,000 if held for at least one year.

Under specific circumstances, a company is permitted to exclude a shareholder proposal from its proxy solicitation, typically after obtaining 'no-action' relief from the SEC staff that concurs that there is a legal basis to exclude the proposal under Exchange Act Rule 14a-8 (eg, if the proposal deals with a matter relating to the company's ordinary business operations).

In November 2021, the SEC's Division of Corporation Finance issued guidance that makes it more difficult for

companies to exclude shareholder proposals under Rule 14a-8. New Staff Legal Bulletin No. 14L (CF) rescinds prior interpretive guidance and offers useful insight into how the Division staff will evaluate future no-action requests seeking exclusion of shareholder proposals on the basis of the widely-used 'ordinary business' and 'economic relevance' exceptions. The new guidance will likely result in the exclusion of fewer shareholder proposals, particularly those that raise human capital-related issues that have a broad societal impact (even if not significant to the company) or that request companies to adopt targets and timeframes to address climate change as long as they do not dictate how management must do so.

In July 2022, the SEC proposed rule amendments that would update three of the substantive bases for exclusion of shareholder proposals: the 'substantial implementation' exclusion in Rule 14a-8(i)(10), the 'duplication' exclusion in Rule 14a-8(i)(11), and the 'resubmission' exclusion in Rule 14a-8(i)(12). The proposed amendments would provide the following:

- A proposal may be excluded as substantially implemented if 'the company has already implemented the essential elements of the proposal.'
- A proposal 'substantially duplicates' another proposal if it 'addresses the same subject matter and seeks the same objective by the same means.'
- A proposal constitutes a resubmission if it 'substantially duplicates' a prior proposal, using the same test proposed in the previous bullet.

Since 2011, companies may not exclude from their proxy materials shareholder proposals (precatory or binding) relating to by-law amendments establishing procedures for shareholder nomination of director candidates and inclusion in the company's proxy materials, as long as the proposal is otherwise not excludable under Rule 14a-8. This amendment to Rule 14a-8 has facilitated the development of 'proxy access' via private ordering at companies chartered in states where permissible, as shareholders are able to institute a shareholder nomination regime via binding by-law amendment or request, via precatory shareholder proposal, that such a by-law be adopted by the board. The private ordering process to adopt proxy access has gained considerable momentum since the beginning of 2015.

In November 2021, the SEC adopted changes to the federal proxy rules to require the use of 'universal' proxy cards. The new rules change the methods by which public companies and shareholders have solicited proxies for decades, and allow shareholders to vote for a mix of management and dissident nominees in a contested director election. The new rules will reshape the process by which hostile bidders, activist hedge funds, social and environmental activists, and other dissident shareholders may utilise director elections to influence corporate governance and policy at public companies. The new rules also amend certain forms of proxy and disclosure requirements relating to voting options and standards that apply to all director elections, whether or not contested. The rules are now effective for shareholder meetings held after 31 August 2022.

Shareholders may act by written consent without a meeting unless the certificate of incorporation provides otherwise. The majority of companies in the S&P 500 do not permit shareholder action by written consent.

Law stated - 12 May 2023

Controlling shareholders' duties

Do controlling shareholders owe duties to the company or to non-controlling shareholders? If so, can an enforcement action be brought against controlling shareholders for breach of these duties?

Controlling shareholders owe a fiduciary duty of fair dealing to the corporation and minority shareholders when the

controlling shareholder enters into a transaction with the corporation. When a controlling shareholder transfers control of the corporation to a third party, this obligation may be extended to creditors and holders of senior securities as well. A controlling shareholder who is found to have violated a duty to minority shareholders upon the sale of control may be liable for the entire amount of damages suffered, instead of only the purchase price paid or for the amount of the control premium. Minority shareholders can bring claims against a controlling shareholder for breach of fiduciary duty on either a derivative or direct basis, depending on the nature of the harm suffered.

Law stated - 12 May 2023

Shareholder responsibility

Can shareholders ever be held responsible for the acts or omissions of the company?

Shareholders' liability for corporate actions is generally limited to the amount of their equity investment. In unusual circumstances, exceptions may apply.

Law stated - 12 May 2023

Employees

What role do employees have in corporate governance?

Employees have no formal role in corporate governance at public companies in the United States. However, it is not uncommon for employees to own shares of the corporation's stock directly or through employee stock option or retirement plans. Stock ownership enables employees to participate in corporate governance as shareholders.

A recent Delaware Chancery Court opinion clarified that, as with directors, a corporate officer's fiduciary duties encompass a duty of oversight. (In re McDonald's Corp Stockholder Derivative Litig (Del Ch 2023)). Accordingly, officers of Delaware corporations, like directors, must (1) make a good-faith effort to put in place reasonable information systems to generate the information necessary to address risks and report upward to higher-level officers or the board and (2) not consciously ignore red flags indicating that the company may suffer harm. Officers will not be held liable for violations of the duty of oversight unless they are shown to have acted in bad faith.

Unlike the duties of directors, the scope of an officer's duty of oversight may be limited to the context in which the officer operates. For example, although a CEO or chief compliance officer has a 'company-wide oversight portfolio,' a chief legal officer may be responsible only for oversight of risks within the legal function. The court noted, however, that where red flags are 'sufficiently prominent,' any officer has a duty to report upward to the CEO or the board.

Corporate officers are well advised to continue to ensure that they are receiving periodic information and conducting regular reviews of risks in their areas of responsibility and that CEOs and chief compliance officers in particular are receiving such reporting on an enterprise-wide basis. Memorialisation of these risk reviews may also help in establishing that officers have endeavoured to fulfill their oversight duties in good faith.

Law stated - 12 May 2023

CORPORATE CONTROL

Anti-takeover devices

Are anti-takeover devices permitted?

In general, anti-takeover devices are permitted. However, there are limits on what types of devices are allowed.

The shareholder rights plan or 'poison pill' is a device adopted by boards to grant existing shareholders the right to purchase large amounts of additional stock for a nominal price if and when an outsider acquires a certain amount of shares (eg, 15 per cent of the outstanding capital). This greatly dilutes the potential acquirer's holdings. Poison pills can usually be 'redeemed' or 'disarmed' by the board of directors before they are 'triggered'. Thus, a poison pill forces a potential acquirer to either negotiate with the existing board or incur the time and expense of initiating a proxy fight to replace the existing directors with directors friendly to the acquirer (who can then redeem the poison pill).

Variations on the traditional poison pill have been designed to make it even more difficult for potential hostile acquirers by restricting the ability of newly placed directors to redeem the poison pill. For example, a 'dead-hand' provision in a poison pill provides that only the specific directors who originally approved the adoption of the poison pill may redeem it. A 'no-hand' poison pill cannot be redeemed at all, and a 'chewable' poison pill gives the incumbent directors a specific period to negotiate before the pill becomes effective. Some states allow the use of dead-hand, no-hand and chewable poison pills (although Delaware does not permit the use of dead-hand or no-hand poison pills). Shareholder activists and proxy advisory firms tend to disfavour poison pills that have not been approved by shareholders. For 2021, the proxy advisory firm Institutional Shareholder Services (ISS) revised its policies to clarify that it will generally recommend voting against all directors if a board unilaterally adopts a poison pill, whether in the short-term or long-term, that includes a dead-hand provision. For 2023, ISS clarified that it will consider the trigger threshold as an additional factor when evaluating the appropriateness of the board's actions in adopting a short-term pill that is not put to a vote. ISS indicated that trigger thresholds of 5 to 10 per cent are very low.

In March 2022, the Council of Institutional Investors updated its corporate governance policies, which now ask companies to hold a shareholder vote on a poison pill within the first 12 months after adoption. The updated policies also state that companies should avoid asking shareholders to approve pills with 'long lifespans, onerous and overly broad 'acting in concert' provisions on shareowners' communications with peers, and pills with excessively low trigger thresholds that may inadvertently target passive investors'.

State corporate law does not prescribe the disclosure of poison pills. However, the Securities and Exchange Commission (SEC) requires reporting companies to disclose any by-law and charter provisions (eg, a poison pill) that would delay, defer or prevent a change in control in the course of an extraordinary corporate transaction, such as a merger, sale transfer or reorganisation. The rights underlying poison pills may also require SEC registration.

A variety of other anti-takeover devices and practices are also available. Courts have upheld the use of the following anti-takeover devices:

- acquisition of another business to increase the chances that the threatened takeover will raise antitrust considerations;
- adoption of voting and other procedures that make it difficult for an acquirer of a majority of voting shares to replace the board of directors (such as board classification, for example, into three classes of directors, pursuant to which one-third of the board is elected every year);
- imposition of restrictions on business combinations with significant shareholders without board approval ('freeze-out' – the default position in Delaware: Delaware General Corporate Law (DGCL), section 203);
- institution of a suit to enjoin the offer for violations of antitrust laws, rules regulating tender offers or other legal grounds;
- issuance, or proposed issuance, of additional shares to persons who oppose the takeover (a lock-up);
- amendment of basic corporate documents to make a takeover more difficult;
- buyout of the aggressor;
- inclusion of supermajority voting requirements in the corporate charter;
- issuance of dual classes of common stock;
- greenmail (but subject to 50 per cent federal excise tax);
- provision of extremely large severance payments to key executives whose employment is terminated following a

change in control (golden parachutes);
- undertaking of defensive acquisitions;
- purchase of the corporation's own shares to increase the market price of the stock; and
- imposition of restrictions in connection with the creation of debt that frustrate an attempted takeover.

Under the New York Stock Exchange (NYSE) and Nasdaq Stock Market (Nasdaq) listing rules, listed companies are prohibited from using defensive tactics that would disparately reduce or restrict the voting rights of existing shareholders (eg, the adoption of time-phased voting plans or the issuance of super voting stock).

Law stated - 12 May 2023

Issuance of new shares

May the board be permitted to issue new shares without shareholder approval? Do shareholders have pre-emptive rights to acquire newly issued shares?

Under Delaware law, the board is permitted to issue new shares without shareholder approval up to the amount of authorised capital set forth in the company's certificate of incorporation. Authorisation of additional shares for issuance will require shareholder approval. The SEC rules require registration of shares prior to their being issued unless an exception applies. In addition, the rules of the NYSE and Nasdaq require that shareholder approval be obtained prior to:

- any adoption of an equity compensation plan pursuant to which officers or directors may acquire stock, subject to limited exceptions;
- issuance of common stock to directors, officers or substantial security holders if the number of shares of common stock to be issued exceeds either 1 per cent of the number of shares of common stock or 1 per cent of the voting power outstanding before the issuance, with some exceptions including if the issuance is a cash sale for a price that is at least a specified minimum price (NYSE), or could result in an increase in outstanding common shares or voting power of 5 per cent or more (Nasdaq);
- issuance of common stock that will have voting power equal to or greater than 20 per cent of the voting power prior to such issuance or that will result in the issuance of a number of shares of common stock that is equal to or greater than 20 per cent of the number of shares of common stock outstanding prior to such issuance, subject to certain exceptions, including any public offering for cash or if the issuance is in connection with an acquisition of the stock or assets of another company and the issuance alone or when combined with any other present or potential issuance of common stock in connection with such acquisition is equal to or exceeds the 20 per cent threshold; and
- issuance of securities that will result in a change of control of the company.

Under Delaware law, shareholders do not have any pre-emptive rights to acquire newly issued shares unless pre-emptive rights are expressly granted to shareholders in the certificate of incorporation (DGCL, section 102(b)(3)) or are granted to shareholders on a contractual basis.

Law stated - 12 May 2023

Restrictions on the transfer of fully paid shares

Are restrictions on the transfer of fully paid shares permitted and, if so, what restrictions are commonly adopted?

Under the DGCL, section 202, restrictions on the transfer and ownership of fully paid securities are permitted. A corporation may impose these restrictions in its certificate of incorporation or by-laws, or through an agreement among shareholders. However, any restrictions imposed after the issuance of securities are not binding on those securities, unless the shareholders of the securities are parties to an agreement or voted in favour of the restriction. All permitted restrictions must be noted conspicuously on the certificate representing the restricted security, or, in the case of uncertificated shares, contained in the notice sent to the registered owner. Regardless of any such restrictions, all sales or transfers of securities by public (or private) corporations must be made pursuant to (or subject to an exemption under) the Securities Act of 1933.

Law stated - 12 May 2023

Compulsory repurchase rules

Are compulsory share repurchases allowed? Can they be made mandatory in certain circumstances?

Under the DGCL, section 253, a corporation owning at least 90 per cent of the outstanding shares of each class of the stock of a corporation may merge that other corporation into itself without requiring shareholder approval (known as a 'freeze-out' or 'short-form' merger). Minority shareholders who object to the merger are entitled to appraisal rights.

In addition, corporations may issue shares of stock subject to redemption by the corporation at its option or at the option of the holders of the stock upon the occurrence of certain events.

If a corporation chooses to issue shares subject to redemption, then it must state the time, place and rate at which the stock will be redeemed in the certificate of incorporation or in a board resolution on the issue.

There are two restrictions on a corporation's ability to redeem its own shares. First, state laws, such as the DGCL, section 151, require that immediately following the redemption the corporation must have at least one class or series of stock with full voting powers that is not subject to redemption. The second restriction only applies to listed corporations. Under listing rules, these companies must promptly notify, and provide specified information to, the NYSE or Nasdaq, as applicable, before they take any action that would result in the full or partial redemption of a listed security.

Law stated - 12 May 2023

Dissenters' rights

Do shareholders have appraisal rights?

Under the DGCL, section 262, shareholders who do not vote in favour of a merger or consolidation are entitled to an appraisal by the Delaware Court of Chancery of the fair value of their shares unless:

- the shares were listed on a national securities exchange (for example, the NYSE or Nasdaq);
- the shares were held of record by more than 2,000 holders; or
- the merger or consolidation did not require a shareholder vote.

Notwithstanding the applicability of the above points, appraisal rights will be available if shareholders are required to accept anything other than:

1. shares of the surviving or resulting company;
2. shares listed on a national securities exchange;
3. cash in lieu of fractional shares; or
4. any combination of (1) to (3).

For example, a shareholder will retain his or her appraisal rights if he or she is required to accept cash, debt or shares of a private company in exchange for his or her shares in the company to be merged or consolidated.

Law stated - 12 May 2023

RESPONSIBILITIES OF THE BOARD (SUPERVISORY)

Board structure

Is the predominant board structure for listed companies best categorised as one-tier or two-tier?

The predominant board structure for listed companies in the United States is one-tier. The Delaware General Corporation Law (DGCL), section 141 states:

> *'[The] business and affairs of every corporation organised under this chapter shall be managed by or under the direction of a board of directors, except as may be otherwise provided in this chapter or in its certificate of incorporation.'*

The board of directors delegates managerial responsibility for day-to-day operations to the chief executive and other senior executives. Members of senior management may serve on the board, but they are not organised as a separate management board.

Law stated - 12 May 2023

Board's legal responsibilities

What are the board's primary legal responsibilities?

The primary legal responsibility of the board is to direct the business and affairs of the corporation (see DGCL, section 141). While the functions of a board are not specified by statute, it is generally understood, as noted in the American Law Institute's Principles of Corporate Governance and other codes of best practice, that board functions typically include:

- selecting, evaluating, fixing the compensation of and, where appropriate, replacing the CEO and other members of senior management;
- developing, approving and implementing succession plans for the CEO and senior executives;
- overseeing management to ensure that the corporation's business is being run properly;
- reviewing and, where appropriate, approving the corporation's financial objectives and major corporate plans, strategies and actions;
- understanding the corporation's risk profile and reviewing and overseeing the corporation's management of risks;

- reviewing and approving major changes in the auditing and accounting principles and practices to be used in preparing the corporation's financial statements;
- establishing and monitoring effective systems for receiving and reporting information about the corporation's compliance with its legal and ethical obligations, and articulating expectations and standards related to corporate culture and the 'tone at the top';
- understanding the corporation's financial statements and monitoring the adequacy of its financial and other internal controls, as well as its disclosure controls and procedures;
- evaluating and approving major transactions, such as mergers, acquisitions, significant expenditures and the disposition of major assets;
- providing advice and counsel to senior management;
- reviewing the process for providing adequate and timely financial and operational information to management, directors and shareholders;
- establishing the composition of the board and its committees, board succession planning and determining governance practices;
- retaining independent advisers to assist the board and committees;
- assessing the effectiveness of the board, its committees or individual directors; and
- performing such other functions as are necessary.

Law stated - 12 May 2023

Board obligees

Whom does the board represent and to whom do directors owe legal duties?

Directors are elected by shareholders. They are fiduciaries of the corporation and its shareholders. Directors represent the shareholding body as a whole, and not any particular set of shareholding constituents. If a corporation becomes insolvent, directors continue to owe their fiduciary duties to the corporation, not directly to creditors; however, creditors will have standing to assert derivative claims. See North American Catholic Educational Programming Foundation Inc v Gheewalla (Del 2007).

Law stated - 12 May 2023

Enforcement action against directors

Can an enforcement action against directors be brought by, or on behalf of, those to whom duties are owed? Is there a business judgment rule?

Shareholders can bring suits against the directors on their own behalf or on behalf of the corporation (a derivative suit), depending on the nature of the allegation. To institute a derivative suit, a shareholder must first make a demand to the board of directors that the corporation initiate the proposed legal action on the corporation's own behalf. However, if the shareholder can show that bringing such a demand would be futile, it is not required.

Directors will not be held liable for their decisions, even if such decisions harm the corporation or its shareholders, if the decisions fall within the judicially created safe harbour known as the 'business judgment rule'. The rule states a judicial presumption that disinterested and independent directors make business decisions on an informed basis and with the good faith belief that the decisions will serve the best interests of the corporation. If a board's decision is challenged in a lawsuit, the court will examine whether the plaintiff has presented evidence to overcome this presumption. If the presumption is not overcome, the court will not investigate the merits of the underlying business decision.

This helps courts avoid second-guessing board decisions, and protects directors from liability when they act on an informed and diligent basis and are not otherwise tainted by a personal interest in the outcome. This is true even if the decision turns out badly from the standpoint of the corporation and its shareholders.

Law stated - 12 May 2023

Care and prudence

Do the duties of directors include a care or prudence element?

Directors owe duties encompassing both a duty of care and a duty of loyalty to the corporation and to the corporation's shareholders.

Although grounded in common law, the duty of care has been codified in more than 40 states. Most state statutes require that directors discharge their responsibilities in good faith, with the care that an ordinarily prudent person in a like position would exercise under similar circumstances, and in a manner that the director reasonably believes to be in the corporation's best interests. Conduct that violates the duty of care may also – in certain circumstances – violate the good faith obligation that is a component of the duty of loyalty. For example, a failure to provide oversight of 'mission-critical' risks (which requires, among other things, a reliable information and reporting system) could give rise to a claim for breach of the duty of care and the obligation of good faith. See In Re Caremark International Inc Derivative Litigation (Del Ch 1996), Stone v Ritter (Del 2006) and Marchand v Barnhill (Del 2019) (discussed below).

The duty of loyalty prohibits self-dealing and misappropriation of assets or opportunities by board members. Directors are not allowed to use their position to make a personal profit or achieve personal gain or other advantage. The duty of loyalty includes a duty of candour that requires a director to disclose to the corporation any conflicts of interest. Transactions that violate the duty of loyalty can be set aside, and directors can be found liable for breach. Thus, whenever a board is considering a transaction in which a director has a personal interest, the material facts about the director's relationship or interest in the transaction should be disclosed to the board and a majority of the disinterested directors should authorise the transaction. Alternatively, the material facts should be disclosed to shareholders, for a vote to approve the transaction.

In 2003, the Delaware Court of Chancery rendered an important opinion concerning the 'duty of good faith' of corporate directors (In Re The Walt Disney Co (Del Ch 2003)). In this opinion, the court held that directors who take an 'ostrich-like approach' to corporate governance and 'consciously and intentionally disregard their responsibilities', adopting a 'we don't care about the risks' attitude may be held liable for breaching their duty to act in good faith. The opinion was rendered on a motion to dismiss for failure to state a claim. The opinion is notable for its sharp focus on the importance of good faith, in addition to due care and loyalty, when considering director conduct. By characterising the alleged lack of attention by directors as a breach of the duty of good faith rather than a breach of the duty of care, the court effectively stripped the directors of the protection afforded by the Delaware Director Protection Statute (which allows adoption of a provision in the certificate of incorporation 'eliminating or limiting the personal liability of a director to the corporation or its shareholders for monetary damages for breach of a fiduciary duty as a director' with some exceptions (DGCL, section 102(b)(7)).

In 2005, the Delaware Court of Chancery rendered another opinion in connection with the same Disney litigation that further defines the contours of the duty of good faith (In Re The Walt Disney Co (Del Ch 2005)). In this opinion, the court focused on the element of intent in identifying whether a breach of the duty of good faith has occurred. Generally, the court determined, the duty of good faith is not satisfied where a director 'intentionally acts with a purpose other than ... the best interests of the corporation'; where a director 'intend[s] to violate applicable ... law'; or where a director 'intentionally fails to act in the face of a known duty to act'. With respect to the specific case at hand, however, the court ruled that the Disney directors did not, in fact, breach their duty of good faith because they did make some business judgments and, therefore, their conduct did not meet the intent elements enumerated by the court as necessary to

constitute a breach of the duty of good faith.

In 2006, the Delaware Supreme Court upheld the Delaware Court of Chancery's ruling that the Disney directors were not liable.

The Supreme Court also provided guidance with respect to the contours of the duty of good faith, describing the following two categories of fiduciary behaviour as conduct in breach of the duty of good faith: conduct motivated by subjective bad faith (that is, actual intent to do harm); and conduct involving 'intentional dereliction of duty, a conscious disregard for one's responsibilities'. The Supreme Court further held that gross negligence on the part of directors 'clearly' does not constitute a breach of the duty of good faith.

In 2006, the Delaware Supreme Court held in Stone v Ritter (Del 2006) that 'good faith' is not a separate fiduciary duty. The Supreme Court stated that 'the obligation to act in good faith does not establish an independent fiduciary duty that stands on the same footing as the duties of care and loyalty' and the fiduciary duty of loyalty 'encompasses cases where the fiduciary fails to act in good faith'.

The duty of directors to provide oversight is based on the concept of good faith. In the oversight context, courts focus on whether the board has taken adequate steps to determine that the corporation's business and affairs are being properly administered by the company's officers and management. Boards are expected to ensure that reasonable information and reporting systems are implemented and maintained to provide the board and senior management with timely, accurate information to support informed decisions and so that directors can reach informed judgments concerning the corporation's performance.

In six recent instances, a Delaware court declined to dismiss a claim alleging that directors had not satisfied their duty to exercise oversight. In one case, the Delaware Supreme Court found that the plaintiff adequately pled that the directors failed to implement any monitoring or reporting system related to the most central safety and legal compliance risk facing the company (Marchand v Barnhill (Del 2019)). In another case, the Delaware Chancery Court found that the plaintiff adequately pled that the directors failed to appropriately monitor compliance systems and controls (In Re Clovis Oncology, Inc Derivative Litigation (Del Ch 2019)). That decision suggests that Delaware courts will impose a higher standard on directors of companies operating in the midst of mission-critical regulatory compliance risk. In January 2020, the Delaware Chancery Court found that a plaintiff adequately pled that the directors failed to implement and properly oversee a pipeline integrity reporting system which resulted in a pipeline rupture and oil spill (Inter-Marketing Group USA v Armstrong (Del Ch 2020)). In addition, the Delaware Chancery Court found that the plaintiff adequately pled that the directors failed to make a good faith effort to put in place a board-level system for monitoring the company's financial reporting (Hughes v Hu (Del Ch 2020)). The Delaware Chancery Court also found that the plaintiffs adequately stated a 'Caremark' claim for oversight liability in a case involving board failure to remediate legal issues disclosed in public filings (Teamsters Local 443 Health Services & Insurance Plan v Chou (Del Ch 2020)). Finally, in September 2021, the Delaware Chancery Court found that the alleged absence of structures to inform the Boeing Co board about the 'mission critical' issue of aircraft safety gave rise to a reasonable inference that the directors acted in bad faith in breach of their duty of oversight (In re Boeing Co Derivative Litig (Del Ch 2021)).

Law stated - 12 May 2023

Board member duties

To what extent do the duties of individual members of the board differ?

Generally, all board members owe the same fiduciary duties regardless of their individual skills. However, case law suggests that when applying the standard of due care (namely, that a director acted with such care as an ordinarily prudent person in a like position would exercise under similar circumstances) subjective considerations, including a director's background, skills and duties, may be taken into account. For example, 'inside' directors – usually officers or senior executives – are often held to a higher standard because they more actively participate in and have greater

knowledge of the corporation's activities.

A recent Delaware Chancery Court opinion clarified that, as with directors, a corporate officer's fiduciary duties encompass a duty of oversight. (In re McDonald's Corp Stockholder Derivative Litig (Del Ch 2023)). Accordingly, officers of Delaware corporations, like directors, must (1) make a good-faith effort to put in place reasonable information systems to generate the information necessary to address risks and report upward to higher-level officers or the board and (2) not consciously ignore red flags indicating that the company may suffer harm. Officers will not be held liable for violations of the duty of oversight unless they are shown to have acted in bad faith.

Unlike the duties of directors, the scope of an officer's duty of oversight may be limited to the context in which the officer operates. For example, although a CEO or chief compliance officer has a 'company-wide oversight portfolio,' a chief legal officer may be responsible only for oversight of risks within the legal function. The court noted, however, that where red flags are 'sufficiently prominent', any officer has a duty to report upward to the CEO or the board.

Corporate officers are well advised to continue to ensure that they are receiving periodic information and conducting regular reviews of risks in their areas of responsibility and that CEOs and chief compliance officers in particular are receiving such reporting on an enterprise-wide basis. Memorialisation of such risk reviews may also help in establishing that officers have endeavored to fulfill their oversight duties in good faith.

Additionally, in 2004, the Delaware Court of Chancery rendered an important opinion concerning the fiduciary duties of directors with special expertise (Emerging Communications Shareholders' Litigation (Del Ch 2004)). In Emerging Communications , the Court held a director in breach of his duty of good faith for approving a transaction 'even though he knew, or at the very least had strong reason to believe' that the per share consideration was unfair. The Court, in part, premised the culpability of the director (described in the opinion as a 'principal and general partner of an investment advisory firm') on his 'specialised financial expertise, and . . . ability to understand [the company's] intrinsic value, that was unique to [the company's] board members'. As the Court also found that the director in question was not 'independent' of management, the Emerging Communications decision should not necessarily be interpreted as a pronouncement holding directors with 'specialised expertise' to a higher standard of care in general.

Law stated - 12 May 2023

Delegation of board responsibilities

To what extent can the board delegate responsibilities to management, a board committee or board members, or other persons?

State corporate law generally provides that the business and affairs of the corporation shall be managed by or under the direction of the board of directors. The board has wide-ranging authority to delegate day-to-day management and other aspects of its responsibilities both to non-board members and to board committees and even individual directors. Typically, the board delegates wide powers to the corporation's senior managers. State laws generally make a distinction between the matters a board must address directly and those it may delegate to officers or other agents of the corporation, or to board committees. For example, under DGCL, section 141(c), the board of a company incorporated prior to 1 July 1996 cannot delegate the power to:

- adopt, amend or repeal any by-law of the corporation;
- amend the corporation's certificate of incorporation (except that a board committee may make certain specified decisions relating to the rights, preferences or issuance of authorised stock, to the extent specifically delegated by the board);
- adopt an agreement of merger or consolidation;
- recommend to shareholders the sale, lease or exchange of all or substantially all of the corporation's property and assets;

- recommend to shareholders a dissolution of the corporation or a revocation of a dissolution;
- approve, adopt or recommend to shareholders any action or matter that is required by the DGCL to be submitted to shareholders for approval;
- declare a dividend, unless that power is expressly provided for in the certificate of incorporation, resolution or by-laws; and
- authorise the issuance of stock or adopt a certificate of ownership and merger, unless that power is expressly provided for in the certificate of incorporation, resolution or by-laws.

The Public Company Accounting Reform and Investor Protection Act of 2002 (the Sarbanes–Oxley Act) and the New York Stock Exchange (NYSE) and Nasdaq Stock Market (Nasdaq) listing rules also require that each listed company has an audit committee comprising independent directors who have responsibility for certain audit and financial reporting matters. As required by the Dodd–Frank Wall Street Reform and Consumer Protection Act of 2010 (the Dodd–Frank Act), the NYSE and Nasdaq listing rules also require that each listed company has a compensation committee comprising independent directors who are responsible for certain matters relating to executive compensation. The NYSE listing standards require that each listed company have a nominating or corporate governance committee comprising independent directors who are responsible for director nominations and corporate governance. The Nasdaq listing rules require independent directors (or a committee of independent directors) to have responsibility for certain decisions relating to director nominations. These committees are permitted to delegate their responsibilities to subcommittees solely comprising one or more members of the relevant committee.

Directors may also reasonably rely on information, reports and recommendations provided by officers, other agents and committees on matters delegated to them (see DGCL, section 141(e)). Nevertheless, the board retains the obligation to provide oversight of its delegates, to act in good faith and to become reasonably familiar with their services or advice before relying on this advice.

Law stated - 12 May 2023

Non-executive and independent directors

Is there a minimum number of 'non-executive' or 'independent' directors required by law, regulation or listing requirement? If so, what is the definition of 'non-executive' and 'independent' directors and how do their responsibilities differ from executive directors?

The NYSE and Nasdaq listing rules require that independent directors comprise a majority of the board. Controlled companies (ie, companies in which more than 50 per cent of the voting power is held by an individual, group or another company) and foreign private issuers are exempt from this requirement.

Under the NYSE rules, for a director to be deemed 'independent', the board must affirmatively determine that he or she has no material relationship with the company. A material relationship can include commercial, industrial, banking, consulting, legal, accounting, charitable and familial relationships, among others. Under the NYSE rules, directors having any of the following relationships may not be considered independent:

- a person who is an employee of the listed company or is an immediate family member of an executive officer of the listed company;
- a person who receives, or is an immediate family member of a person who receives, compensation directly from the listed company, other than director compensation or pension or deferred compensation for prior service (provided this compensation is not contingent in any way on continued service), of more than US$120,000 per year;
- a person who is a partner of, or employed by, or is an immediate family member of a person who is a partner of,

or employed (and works on the listed company's audit) by a present or former internal or external auditor of the company;

- a person, or an immediate family member of a person, who has been part of an interlocking compensation committee arrangement; or
- a person who is an employee or is an immediate family member of a person who is an executive officer, of a company that makes payments to or receives payments from the listed company for property or services in an amount that in a single fiscal year exceeds the greater of 2 per cent of this other company's consolidated gross revenues or US$1 million.

In applying the independence criteria, no individual who has had a relationship as described above within the past three years can be considered independent (except in relation to the test set forth in the final bullet point above, which is concerned with current employment relationships only). The Nasdaq listing rules take a different but similar approach to defining independence.

For NYSE and Nasdaq companies, only independent directors are allowed to serve on audit, compensation and nominating or governance committees. The Sarbanes–Oxley Act, section 301, defines an independent director for audit committee purposes as one who has not accepted any compensation from the company other than directors' fees and is not an 'affiliated person' of the company or any subsidiary. NYSE and Nasdaq listing standards require NYSE and Nasdaq companies to have an audit committee that satisfies the requirements of Rule 10A-3 under the Securities Exchange Act of 1934. That rule, which embodies the independence requirements of the Sarbanes–Oxley Act, section 301, provides that an executive officer of an 'affiliate' would not be considered independent for audit committee purposes. As required by the Dodd–Frank Act, the NYSE and Nasdaq developed heightened independence standards for compensation committee members that became effective during 2014. Under these standards, in affirmatively determining the independence of a director for compensation committee purposes, the board of directors must 'consider' all factors specifically relevant to determining whether a director has a relationship to the listed company that is material to that director's ability to be independent from management in connection with the duties of a compensation committee member, including the source of compensation received by the director and whether the director is affiliated with the company or any subsidiary.

Law stated - 12 May 2023

Board size and composition

How is the size of the board determined? Are there minimum and maximum numbers of seats on the board? Who is authorised to make appointments to fill vacancies on the board or newly created directorships? Are there criteria that individual directors or the board as a whole must fulfil? Are there any disclosure requirements relating to board composition?

The DGCL, section 141(b) requires that the board of directors comprises one or more members, each of whom must be a natural person. Beyond the requirement for at least one director, corporate law does not set a minimum or a maximum. As a practical matter, a board should be of a size sufficient to accommodate an appropriate amount of experience, independence and diversity for the full board and its committees. The number of directors is fixed by or in the manner provided in the by-laws or certificate of incorporation; typically the by-laws will specify a range and the board will fix the exact number of directors by resolution. Directors need not be shareholders of the corporation. The certificate of incorporation or the by-laws may provide for director qualifications and address who is authorised to fill vacancies on the board. Generally, the board is authorised to fill vacancies.

The NYSE and Nasdaq require that listed companies have an audit committee comprising at least three members.

Nasdaq requires listed companies to have a compensation committee comprising at least two members; the NYSE does not require a minimum number of members of the compensation committee.

ISS has stated that a company should have no fewer than six nor more than 15 directors, with a board size of between nine and 12 directors 'considered ideal'.

The Securities and Exchange Commission (SEC) requires companies to provide the following proxy statement disclosures relating to board composition:

- which directors qualify as 'independent' under applicable independence standards; and
- for each director and nominee:
  - name, age and positions and offices held with the company;
  - term of office as a director;
  - any arrangements or understandings between the director or nominee and any other person pursuant to which the director or nominee was or is to be selected as a director or nominee;
  - family relationships with any director, nominee or executive officer;
  - business experience and other public company directorships over the past five years;
  - the particular experience, qualifications, attributes or skills that led the board to conclude that the person should serve as a director of the company; and
  - whether the director or nominee has been involved in certain kinds of legal proceedings during the past 10 years.

There is no legal requirement or listing rule that mandates a certain number of female or minority directors, with a few exceptions. In September 2018, a California law was enacted that required California-headquartered publicly held domestic or foreign corporations to have at least one female director by the end of 2019 and, depending on board size, up to three female directors by the end of 2021. In April 2022, a judge in the Los Angeles County Superior Court struck down the law as unconstitutional, holding that it posed a 'total and fatal' conflict with the California Constitution's Equal Protection Clause by requiring corporations to use suspect demographic classifications in the selection of board members to the exclusion of other people from different races, sexual orientations or gender identities. A similar California law enacted in 2020 that required such corporations to have at least one director from an underrepresented community by the end of 2021 and, depending on board size, up to three directors from underrepresented communities by the end of 2022, was also struck down as unconstitutional for similar reasons. Several other states have enacted or are considering legislation that would encourage greater board diversity or require disclosure about board diversity.

There is increasing concern in the institutional investor community about the lack of gender and racial diversity on public company boards of directors, as well as long-tenured directors and lack of board refreshment. In 2017, the New York City Pension Funds announced a letter-writing campaign known as the Boardroom Accountability Project 2.0 targeting over 150 US public companies focused on board composition (eg, experience or skill-sets, tenure and diversity), board refreshment and director succession planning. The New York City Pension Funds will vote against all directors at companies with no female directors and against governance committee members at companies with just one female director. In October 2019, the New York City Pension Funds launched the Boardroom Accountability Project 3.0 urging public companies to adopt a diversity search policy requiring that qualified female and racially and ethnically diverse candidates be included in the pool of nominees from which directors and CEOs are selected, and that director searches include candidates from non-traditional backgrounds, such as government, academic or non-profit organisations.

Under its proxy voting guidelines, BlackRock encourages boards to have at least two female directors and at least one director from an underrepresented group and 'should aspire' to 30 per cent diversity of membership. BlackRock may vote against members of the nominating/governance committee of a company that 'has not adequately explained their

approach to diversity in their board composition'. Generally, companies should disclose diversity aspects relevant to the business and how these characteristics align with the long-term strategy and business model, as well as the process by which director candidates are identified and selected, including whether outside resources were engaged and whether a diverse slate of nominees is considered for all board seats.

Under Vanguard's proxy voting policy for US portfolio companies, boards should represent diversity of personal characteristics including at least gender, race and ethnicity (disclosed on an aggregate or individual director basis) as well as other attributes including tenure, skills and experience (disclosed on an individual basis). Vanguard may vote against the nominating and/or governance committee chair (or other director if needed) if a company's board is making insufficient progress in its diversity composition and/or in addressing its board diversity-related disclosures, taking into account applicable market regulations and expectations along with additional company-specific context. Vanguard generally will vote for a shareholder proposal seeking enhanced disclosure about board diversity, such as workforce demographics, the board's role in overseeing material diversity, equity, and inclusion (DEI) risks and other material social risks, the company's approach to board composition, inclusive of board diversity, and/or adoption of targets or goals related to board diversity, and inclusion of directors' diversity of personal characteristics (including gender, race, ethnicity and national origin) or skills and qualifications if such information is not already disclosed.

State Street Global Advisors expects all listed companies to have at least one female board member and all Russell 3000 companies to have at least 30 per cent women directors. If these requirements are not met, State Street may vote against the nominating committee chair or the board chair (or all nominating committee members if the failure lasts for three consecutive years). State Street may waive the gender diversity guidelines if a company provides a specific, timebound plan to add the requisite number of women to the board. State Street also expects S&P 500 companies to disclose, at minimum, the gender, racial and ethnic composition of its board and have at least one director from an underrepresented racial or ethnic community on its board. State Street will vote against the nominating committee chair at S&P 500 companies that do not meet this requirement. Further, State Street noted that it may vote against the nominating committee chair at S&P 500 companies that do not disclose certain US Equal Employment Opportunity Commission data (ie, an EEO-1 report).

ISS will generally recommend withholding or voting against the nominating committee chair (and potentially other directors) at all companies where there are no women on the board or the board has no apparent racially or ethnically diverse members, unless there was at least one woman or racially/ethnically diverse director at the preceding annual meeting and the board commits to restore gender or racial/ethnic diversity by the next annual meeting.

In 2022, ISS updated its E&S QualityScore scoring tool to include new or expanded factors relating to diversity, equity and inclusion at the board and executive level (including whether there are LGBTQ+ directors and ethnically diverse directors) and voluntary public disclosure of EEO-1 reports.

As of 2023, at Russell 3000 companies, Glass Lewis will generally recommend voting against the nominating committee chair of a board that is not at least 30 per cent gender diverse and the entire nominating committee of a board with no gender diverse directors. For companies outside the Russell 3000, Glass Lewis will generally recommend voting against the nominating committee chair if there are no gender diverse directors.

Finally, as of 2023, at Russell 1000 companies, Glass Lewis will generally recommend voting against the nominating committee chair of a board that does not have at least one director from an underrepresented community. Glass Lewis may refrain from issuing negative voting recommendations against directors at companies that have provided a sufficient rationale or plan to address the lack of diversity on the board.

Furthermore, as of 2023, Glass Lewis will generally recommend votes against the nominating committee chair at Russell 1000 companies that have not provided any disclosure in their proxy statements in any of the following categories: (1) the board's current percentage of racial/ethnic diversity, (2) whether the board's definition of diversity explicitly includes gender and/or race/ethnicity, (3) whether the board has adopted a 'Rooney Rule' policy requiring women and minorities to be included in the initial pool of candidates when selecting new director nominees and (4)

board skills disclosure. Additionally, Glass Lewis will recommend votes against the nominating committee chair at companies that have not provided any disclosure of individual or aggregate racial/ethnic minority demographic information.

Since January 2021, Goldman Sachs will not take a company public unless it has at least two diverse board candidates, one of whom must be female. As of 2023, Goldman Sachs Asset Management votes against the entire board at any company with no female directors, and against all nominating committee members at any company that does not have at least 10 per cent women directors and at least one other diverse director. At S&P 500 companies, Goldman Sachs will vote against nominating committee members at any company with a board that does not have at least one diverse director from an underrepresented ethnic group.

SEC rules currently require companies to provide proxy statement disclosure regarding whether and, if so, how the nominating committee considers diversity in identifying nominees for director and, if the nominating committee has a policy with regard to the consideration of diversity in identifying director nominees, how this policy is implemented and how the nominating committee or the board assesses the effectiveness of its policy. Under guidance issued by the SEC in 2019, if the board or nominating committee considered 'certain self-identified diversity characteristics' (eg, race, gender, ethnicity, religion, nationality, disability, sexual orientation or cultural background) when determining an individual's specific experience, qualifications, attributes or skills for board membership, then the SEC expects the company to disclose those characteristics and how they were considered in the nomination process. The guidance also requires a company to disclose how its diversity policy, if any, takes into account nominees' self-identified diversity attributes and any other qualifications (eg, diverse work experiences, military service or socio-economic or demographic characteristics).

In August 2021, the SEC approved changes to the Nasdaq listing rules relating to board diversity. The rule changes require each Nasdaq-listed company, subject to certain exceptions, to (1) publicly disclose annually in an aggregated form, to the extent permitted by applicable law, information on the voluntary self-identified gender and racial characteristics and LGBTQ+ status of the company's board of directors, and (2) have, or explain why it does not have, at least two directors who are diverse, including at least one director who self-identifies as female and at least one director who self-identifies as either an underrepresented minority or LGBTQ+. Companies will be required to have at least one diverse director by 31 December 2023 and at least two diverse directors by 31 December 2025 or 31 December 2026, depending on the size of the company and its stock market exchange tier. A Nasdaq-listed company with a board of five or fewer members will be required to have, or explain why it does not have, at least one diverse director by 31 December 2023.

For purposes of the new Nasdaq rules, (1) 'diverse' means an individual who self-identifies as a female, an underrepresented minority or LGBTQ+, (2) 'female' means an individual who self-identifies her gender as a woman, without regard to the individual's designated sex at birth, (3) 'underrepresented minority' means an individual who self-identifies as one or more of the following: Black or African American, Hispanic or Latinx, Asian, Native American or Alaska Native, Native Hawaiian or Pacific Islander, or Two or More Races or Ethnicities, and (4) 'LGBTQ+' means an individual who self-identifies as any of the following: lesbian, gay, bisexual, transgender, or as a member of the queer community.

Law stated - 12 May 2023

Board leadership

Is there any law, regulation, listing requirement or practice that requires the separation of the functions of board chair and CEO? If flexibility on board leadership is allowed, what is generally recognised as best practice and what is the common practice?

There is no legal requirement or listing rule that mandates that the positions of board chair and CEO be held separately

or jointly. Corporate boards are generally free to decide for themselves the leadership structure of the board and company (although the corporate charter or by-laws could provide otherwise). Shareholder proposals calling for a separation of the board chair and CEO roles have become increasingly since the late 2000s; these proposals tend to receive relatively high shareholder support (typically less than majority although one proposal did pass in 2022).

The NYSE and Nasdaq listing rules require that the non-management directors meet without management present on a regular basis. Under the NYSE rules, companies are required to either choose and disclose the name of a director to preside during executive sessions or disclose the method it uses to choose someone to preside (for example, a rotation among committee chairs). Although the NYSE rules do not set forth other specific duties for the presiding director, some companies have a 'lead independent director' perform the presiding function while also having a role in agenda-setting and determining the information needs of the outside directors. The Nasdaq listing rules also require that boards convene executive sessions of independent directors, but do not include a presiding director disclosure requirement.

In 2009, the SEC adopted rules requiring each reporting company to disclose the board's leadership structure and why the company believes it is the best structure for the company. Each company must disclose whether and why it has chosen to combine or separate the CEO and board chair roles. Where these positions are combined, the company must disclose whether and why the company has a lead independent director and the specific role the lead independent director plays in the leadership of the company.

Independent board leadership is also supported by governance effectiveness guidance that expresses a 'best practice' consensus that boards should have some form of independent leadership. Several best practice codes recommend a clear division of responsibilities between a board chair and CEO to ensure that the board maintains its ability to provide objective judgement concerning management. Some recommend that the board should separate the roles of board chair and CEO, while others recommend designating a lead outside or independent director for certain functions. For example, the Report on Director Professionalism by the National Association of Corporate Directors (NACD) recommends appointing an independent board leader to:

- organise the board's evaluation of the CEO and provide feedback;
- chair sessions of the non-executive directors;
- set the agenda (with the CEO or chair and CEO); and
- lead the board in anticipating and responding to a crisis.

Many companies have recently expanded the responsibilities of the independent lead director in light of the increased appreciation of the importance of independent board leadership (see also the Report of the NACD Blue Ribbon Commission on Fit for the Future: An Urgent Imperative for Board Leadership issued in 2019). These can include, in addition to the items set forth above from the NACD report:

- presiding over board meetings at which the chair is not present;
- approving board schedules;
- approving information provided to the board;
- serving as a liaison between the chair and the independent directors;
- having the authority to call meetings of the independent directors or the full board;
- being available for consultation and direct consultation with major shareholders;
- advising on, recommending or approving the retention of outside advisers and consultants who report to the board; or
- guiding, leading or assisting with the board and director self-assessment process, the CEO succession planning process or the board's consideration of CEO compensation.

Furthermore, under its proxy voting guidelines, ISS will generally vote for shareholder proposals requiring that the board chair position be filled by an independent director, taking into consideration the following:

- the scope of the proposal;
- the company's current board leadership structure;
- the company's governance structure and practices; and
- any other relevant factors that may be applicable.

Many companies combine the roles of CEO and chair; however, separation of the roles has become increasingly prevalent at Standard & Poor's (S&P) 500 companies over the past 10 years – the roles were separated at 57 per cent of S&P 500 companies in 2022, up from 43 per cent in 2012. Chairs who qualified as independent were in place at 36 per cent of S&P 500 companies in 2022 compared with 23 per cent in 2012. The vast majority of companies that do not have an independent chair have appointed an independent lead or presiding director.

Law stated - 12 May 2023

Board committees

What board committees are mandatory? What board committees are allowed? Are there mandatory requirements for committee composition?

Since 1999, the NYSE and Nasdaq listing rules have required that listed companies have audit committees consisting entirely of independent directors (prior to that time, a majority of independent directors had been a long-standing audit committee requirement for companies listed on the NYSE). In 2003, the NYSE and Nasdaq adopted listing rules that also require companies to have compensation and nominating or governance committees (or committees that perform those functions) consisting entirely of independent directors, although Nasdaq permits nomination decisions (and, until 2014, permitted certain executive compensation decisions) to be made by a majority of independent directors. The Sarbanes–Oxley Act requires that all boards of companies with listed securities have audit committees composed entirely of directors who receive no compensation from the company other than directors' fees and are not affiliated with the company. In addition, companies are required to disclose the name of at least one audit committee member who is an 'audit committee financial expert' as defined by the SEC, or explain why they do not have one. The NYSE and Nasdaq rules also require that the audit committee comprises at least three members and impose requirements with respect to the financial literacy of audit committee members. Since 2014, each Nasdaq listed company must have, and certify that it has and will continue to have, a compensation committee of at least two members, each of whom must be an independent director; the NYSE does not require a minimum number of members of the compensation committee. As required by the Dodd–Frank Act, the NYSE and Nasdaq each adopted heightened independence standards for compensation committee members that became effective in 2014 and require the board to 'consider' the source of compensation received by the director and whether the director is affiliated with the company or any subsidiary, when determining if a director is independent for purposes of serving on the compensation committee.

Law stated - 12 May 2023

Board meetings

Is a minimum or set number of board meetings per year required by law, regulation or listing requirement?

Under state law, the corporation's by-laws or certificate of incorporation prescribe the requirements for board meetings and may or may not prescribe a set number of meetings; it is typical for companies to not specify a minimum number of meetings in the certificate of incorporation or by-laws. Generally, it is believed that a board should meet at least once per financial-reporting quarter. However, most boards of large publicly traded corporations meet more frequently. For example, companies represented on the S&P 500 held 8.3 board meetings on average in 2022. SEC rules require companies to disclose the total number of board and committee meetings held during the past year and provide details regarding director attendance at these meetings.

ISS and Glass Lewis will issue negative vote recommendations with respect to directors who failed to attend a minimum of 75 per cent of the aggregate of his or her board and committee meetings (with some exceptions).

Law stated - 12 May 2023

Board practices

Is disclosure of board practices required by law, regulation or listing requirement?

The SEC requires disclosure of certain board practices, including disclosures about the identity and compensation of directors and the composition and activities of the audit, compensation and nominating committees.

Under the NYSE listing rules, listed companies are required to adopt and disclose 'corporate governance guidelines' that address:

- qualification standards for directors;
- responsibilities of directors;
- director access to management and, as necessary, independent advisers;
- compensation of directors;
- continuing education and orientation of directors;
- management succession; and
- an annual performance evaluation of the board.

Nasdaq-listed companies are not required to adopt corporate governance guidelines, but many have done so as a best practice.

The NYSE rules also require listed companies to adopt and disclose charters for their compensation, nominating or governance and audit committees.

The compensation committee's charter must detail the committee's purpose and responsibilities, which include reviewing and approving corporate goals and objectives relevant to CEO compensation, evaluating the CEO's performance in light of those goals and objectives, setting his or her compensation level based on this evaluation, making recommendations to the board with respect to non-CEO executive officer compensation, incentive-based compensation plans and equity-based plans and producing a compensation committee report on executive compensation required by SEC rules to be included in the company's proxy statement. The charter must also provide that the committee will perform an annual self-evaluation. In addition, pursuant to the Dodd–Frank Act, the NYSE and Nasdaq adopted listing standards that became effective in 2014 requiring compensation committees to consider specified independence factors prior to engaging consultants and other advisers and giving compensation committees the authority and discretion to retain or obtain the advice of consultants and other advisers at the company's expense.

The nominating or governance committee's charter must detail the committee's purpose and responsibilities. These include:

- identifying the board's criteria for selecting new directors;
- identifying individuals who are qualified to become board members;
- selecting or recommending that the board select nominees for election at the next annual general meeting;
- developing and recommending to the board a set of corporate governance principles for the corporation; and
- overseeing the evaluation of the board and management.

In addition, the charter must include a provision for an annual performance evaluation of the committee. Unlike the NYSE, Nasdaq does not include a requirement with respect to the charter for the nominating or governance committee, although companies are required to certify that they have adopted a formal written charter or board resolution, as applicable, addressing the nominations process.

The audit committee charter must specify the committee's purpose, which must include: assisting board oversight of the integrity of the company's financial statements, the company's compliance with legal and regulatory requirements, the independent auditor's qualifications and independence and the performance of the company's internal audit function and independent auditors; and preparing the report that SEC rules require to be included in the company's annual proxy statement. The NYSE listing rules require that the charter must also detail the duties and responsibilities of the audit committee, including:

- the ability to hire and fire the company's independent auditor and other registered public accounting firms;
- establishing whistle-blowing policies and procedures for handling complaints or concerns regarding accounting, internal accounting controls or auditing matters;
- at least annually:
  - obtaining and reviewing a report by the independent auditor describing the independent auditor's internal quality control procedures;
  - reviewing any material issues raised by the auditor's most recent internal quality control review of themselves or peer review, or any inquiry or investigation by governmental or professional authorities within the preceding five years; and
  - assessing the auditor's independence;
- discussing the annual audited financial statements and quarterly financial statements with management and the independent auditor;
- discussing earnings press releases, as well as financial information and earnings guidance that is given to analysts and rating agencies;
- obtaining the advice and assistance of outside legal, accounting or other advisers, as necessary, with funding to be provided by the company;
- discussing policies with respect to risk assessment and risk management;
- meeting separately, from time to time, with management, with the internal auditors and with the independent auditor;
- reviewing with the independent auditor any audit problems or difficulties and management's response to such issues;
- setting clear hiring policies for employees or former employees of the independent auditor;
- reporting regularly to the board of directors; and
- evaluating the audit committee on an annual basis.

The Nasdaq listing rules also require an audit committee to have a charter addressing all of its duties and responsibilities under the Sarbanes–Oxley Act, including: having the sole power to hire, determine the funding for and oversee the outside auditors; having the authority to consult with and determine the funding for independent counsel and other advisers; and having the responsibility to establish procedures for receipt of complaints.

In addition, both the NYSE and Nasdaq rules require that companies adopt and disclose a code of conduct applicable to directors, officers and employees that addresses conflicts of interest and legal compliance. The NYSE rules also require that the code address corporate opportunities, confidentiality, fair dealing and protection of company assets.

Public companies post their corporate governance guidelines, board committee charters, codes of conduct and other governance documents on their corporate websites, typically under a heading such as 'corporate governance' or 'investor relations'.

In summer 2022, the SEC's Division of Corporation Finance launched a new comment letter initiative urging targeted public companies to enhance their disclosures about the board's leadership structure and role in risk oversight. The stated reason for the initiative is that the Division Staff have noticed that the disclosure required by Item 407(h) of Regulation S-K has become increasingly standardised rather than tailored to a company's individual circumstances. Disclosure should provide investors with insights about why a company has chosen its particular board leadership structure (regardless of the type of leadership structure selected) or how a company's board is discharging its risk oversight responsibilities in light of the specific challenges facing its business.

Law stated - 12 May 2023

Board and director evaluations

Is there any law, regulation, listing requirement or practice that requires evaluation of the board, its committees or individual directors? How regularly are such evaluations conducted and by whom? What do companies disclose in relation to such evaluations?

Under the NYSE listing rules, listed companies are required to adopt and disclose 'corporate governance guidelines' that address, among other things, an annual performance evaluation of the board. According to the rules, the 'board should conduct a self-evaluation at least annually to determine whether it and its committees are functioning effectively'. The NYSE listing rules also require that each of the audit, compensation and nominating and governance committee charters provide for an annual performance evaluation of the committee. Companies listed on Nasdaq do not have similar requirements, but many still engage in self-evaluation as a matter of good governance practice. In addition, independent auditors often inquire into the board's evaluation of the audit committee as part of the auditor's assessment of the internal control environment.

There has been a greater focus on director evaluations in recent years as investors are increasingly concerned about board quality and refreshment mechanisms in light of long director tenures, rising mandatory retirement age limits and perfunctory director renomination decisions. A robust performance evaluation of individual directors can help inform the renomination decision process.

In 2022, 98 per cent of boards at S&P 500 companies reported conducting an annual performance evaluation. Forty-seven per cent of S&P 500 boards disclose that they have some form of individual director evaluation. In 2022, 25 per cent of S&P 500 companies reported that they retained an independent expert to facilitate the evaluation process, compared to 20 per cent in 2021 and only 2 per cent in 2017.

The NYSE listing rules include 'overseeing the evaluation of the board and management' as a responsibility of the nominating or governance committee that must be included in its committee charter. Boards should determine the evaluation methodology, for example, the use of a written survey or interviews, or both, followed by a facilitated discussion, and will determine who will lead the evaluation process (eg, the chair, lead director or a third-party facilitator). A composite report of the feedback and any related recommendations are typically distributed to the board, committee or individual directors by the party leading the evaluation and discussed at a meeting.

In 2014, the Council of Institutional Investors (CII) issued a report calling for enhanced disclosure relating to board evaluation. Specifically, the CII provided 'best in class' examples of disclosure that explain the mechanisms of the

evaluation process and discuss the key takeaways from the most recent evaluation. The CII acknowledged that the latter type of disclosure is uncommon among US public companies but is more prevalent in Europe and Australia. In 2019, the CII Research and Education Fund, an affiliate of the CII, issued an updated guide to encourage enhanced disclosure relating to board evaluation and endorse certain evaluation best practices. US public companies can expect more pressure to disclose their self-evaluation processes, especially in circumstances where shareholders have concerns about governance failures, the absence of regular director turnover or board composition generally.

In 2017, the New York City Pension Funds announced a letter-writing campaign targeting over 150 US public companies focused on board composition and refreshment. The group asked to engage with directors about the company's processes for refreshing the board, including an explanation of the evaluation process for individual directors and a description of processes for encouraging underperforming directors to come off the board.

The Report of the NACD Blue Ribbon Commission on Building the Strategic-Asset Board issued in 2016 also discusses board evaluation best practices in the context of other continuous improvement board processes.

Law stated - 12 May 2023

REMUNERATION

Remuneration of directors

How is remuneration of directors determined? Is there any law, regulation, listing requirement or practice that affects the remuneration of directors, the length of directors' service contracts, loans to directors or other transactions or compensatory arrangements between the company and any director?

The remuneration of directors is generally a matter for the board of directors, or a committee of the board (usually, the compensation committee or the nominating or governance committee), to determine.

In determining the appropriate amount of compensation to be paid to directors, many boards and compensation or nominating or governance committees rely on the advice of independent compensation consultants, whose expertise lies in analysing compensation trends in industry or other market segments. The Securities and Exchange Commission (SEC) amended its regulations in 2012 to require enhanced disclosure with respect to a company's use of compensation consultants.

Boards should exercise caution when approving equity compensation plans that permit equity awards to be made to non-employee directors. Even if such a plan includes meaningful limits on the amount of equity that directors can award themselves and the plan is approved by shareholders, the directors must abide by their fiduciary duties when making awards under the plan (In Re Investors Bancorp, Inc (Del 2017)).

Compensation given to all directors must be disclosed by reporting companies. Under the Public Company Accounting Reform and Investor Protection Act of 2002 (the Sarbanes–Oxley Act), audit committee members can only receive director's fees (including fees for committee work) from the companies they serve. In addition, the board must consider the source of compensation of a director when considering his or her suitability for compensation committee service. The New York Stock Exchange (NYSE) requires listed companies to adopt and disclose corporate governance guidelines, which are required to address, among other things, the compensation of directors. Since 2016, Nasdaq Stock Market (Nasdaq) listed companies have been required to disclose compensatory arrangements between directors or nominees and third parties in connection with that person's candidacy or service as a director ('golden leashes').

There is no law, regulation or listing requirement that affects the length of directors' service contracts. Rather, directors are elected for a term by the shareholders and it is up to each company to determine whether to place any limits on the number or length of such terms, although NYSE listing rules provide that directors' terms of office should not exceed

three years.

Term limits are very rare among large public companies, but retirement age policies are common. The average tenure of directors at S&P 500 companies is 7.8 years. Forty-six per cent of independent directors on S&P 500 boards have served five years or less, 28 per cent have served for six to 10 years, 14 per cent have served for 11 to 15 years, and 13 per cent have served for 16 years or more. Sixty-seven per cent of S&P 500 boards have an average tenure between 6 and 10 years. The corporate governance assessment tool of the proxy advisory firm Institutional Shareholder Services (ISS) tracks the proportion of non-executive directors who have 'lengthy tenure', which for US companies is defined as nine or more years. While most institutional investors do not support individual term and age limits applicable to directors, some are adopting policies focused on average director tenure or individual director tenure (eg, by generally considering long-tenured directors to not be independent).

Section 402 of the Sarbanes–Oxley Act prohibits companies from extending or maintaining personal loans to their directors, other than certain consumer credit arrangements (eg, home improvement or credit card loans) made in the ordinary course of business of a type generally made available by the company to the public and on market terms or terms no more favourable than offered by the company to the general public.

The duty of loyalty restricts directors from competing with the corporation. Thus, while directors are not precluded from engaging in other businesses, they may not:

- use their position as directors to prevent the corporation from competing with their other businesses;
- divert corporate assets to their own uses or the uses of their other businesses;
- disclose the corporation's trade secrets or confidential information to others;
- lure corporate opportunities, business or personnel away from the corporation; or
- receive, unbeknown to the corporation, a commission on a corporate transaction.

Under the corporate opportunity doctrine, directors cannot divert to themselves an opportunity that belongs to the corporation. An opportunity belongs to the corporation if the corporation has a right to it, a property interest in it, an expectancy interest in it, or if by 'justice' it should belong to the corporation. The corporation may renounce any interest or expectancy in an opportunity in its certificate of incorporation or by an action of its board of directors (see the Delaware General Corporation Law, section 122(17)). At times, a director's interest may still conflict with the interests of the corporation. Conflicts that cannot be avoided must be fully disclosed by the interested director and any action that needs to be taken should be taken by vote of the disinterested directors.

Law stated - 12 May 2023

Remuneration of senior management

How is the remuneration of the most senior management determined? Is there any law, regulation, listing requirement or practice that affects the remuneration of senior managers, loans to senior managers or other transactions or compensatory arrangements between the company and senior managers?

The remuneration of a corporation's CEO and senior management is generally a matter for the board of directors, or a committee of the board (usually, the compensation committee), to determine.

The NYSE listing rules require that a compensation committee comprising independent directors determines the amount of compensation paid to the CEO and makes recommendations to the board with respect to non-CEO executive officer compensation. These provisions are interpreted broadly, such that a compensation committee or group of independent directors, as the case may be, must approve each specific element of CEO compensation at all listed

companies. Since 2014, the Nasdaq listing rules have required that CEO and executive officer compensation be determined by a compensation committee comprising at least two independent directors.

In addition, applicable tax and securities rules require the approval of independent directors to grant equity-based awards (eg, stock option and restricted stock awards) to senior management, and best practice would have the board or compensation committee approve the compensation paid to key members of senior management. Historically, the Internal Revenue Code, section 162(m), provided tax incentives for certain performance-based compensation decisions when made by a committee of outside directors. With the enactment of tax reform in the United States in 2017, this performance-based compensation exemption has been eliminated except with respect to grandfathered arrangements. The responsibility between the board (or compensation committee) and the CEO in determining the elements and amount of compensation paid to senior managers (other than the CEO) differs from company to company and, even within a company, from element of compensation to element of compensation.

In determining the appropriate amount of compensation to be paid to the CEO and other senior managers, many boards and compensation committees rely on the advice of independent compensation consultants, whose expertise lies in analysing compensation trends in industry or other market segments. The SEC amended its regulations in 2012 to require enhanced disclosure with respect to a company's use of compensation consultants.

In August 2022, the SEC adopted a final rule that requires certain public companies to disclose information regarding the relationship between executive compensation and actual financial performance, beginning with their proxy statements for the 2023 proxy season. This new disclosure, also known as pay-versus-performance, implements section 953(a) of the Dodd-Frank Act.

Section 402 of the Sarbanes–Oxley Act prohibits companies from extending or maintaining personal loans to their executive officers, other than certain consumer credit arrangements (eg, home improvement or credit card loans) made in the ordinary course of business of a type generally made available by the company to the public and on market terms or terms no more favourable than offered by the company to the general public.

Law stated - 12 May 2023

Say-on-pay

Do shareholders have an advisory or other vote regarding remuneration of directors and senior management? How frequently may they vote?

Since 2011, the Dodd–Frank Wall Street Reform and Consumer Protection Act of 2010 has required US public companies to conduct a separate shareholder advisory vote on:

- executive compensation – to be held at least once every three calendar years;
- whether the advisory vote on executive compensation should be held every year, every two years or every three years – to be held at least once every six calendar years; and
- certain 'golden parachute' compensation arrangements in connection with a merger or acquisition transaction that is being presented to shareholders for approval.

The predominant practice is to hold a shareholder advisory vote on executive compensation every year.

In August 2022, the SEC adopted a final rule that requires certain public companies to disclose information regarding the relationship between executive compensation and actual financial performance, beginning with their proxy statements for the 2023 proxy season. This new disclosure, also known as pay-versus-performance, implements section 953(a) of the Dodd-Frank Act.

US public companies are not required to seek shareholder approval of cash compensation for directors. The NYSE and Nasdaq listing rules require companies to obtain shareholder approval of equity compensation plans applicable to directors and executive officers.

Law stated - 12 May 2023

DIRECTOR PROTECTIONS

D&O liability insurance

Is directors' and officers' liability insurance permitted or common practice? Can the company pay the premiums?

Companies may purchase and typically do maintain directors' and officers' liability insurance to protect directors and officers against the risk of personal liability (see the Delaware General Corporation Law (DGCL), section 145(g)). Although this coverage has become substantially more expensive, it is usually available and has not been limited by legislative and regulatory actions. Companies are allowed to pay the premiums for directors' and officers' liability insurance.

Law stated - 12 May 2023

Indemnification of directors and officers

Are there any constraints on the company indemnifying directors and officers in respect of liabilities incurred in their professional capacity? If not, are such indemnities common?

A company may indemnify a director for liability incurred if that director: acted in good faith; acted in a manner that he or she reasonably believed was in the best interests of the company; and in the case of a criminal proceeding, had no reasonable cause to believe his or her conduct was unlawful (see DGCL, section 145). Many companies employ such indemnities.

Law stated - 12 May 2023

Advancement of expenses to directors and officers

To what extent may companies advance expenses to directors and officers in connection with litigation or other proceedings against them or in which they will be a witness?

Under Delaware law, expenses (including attorneys' fees) incurred by an officer or a director in defending any civil, criminal, administrative or investigative action, suit or proceeding may be paid by the corporation in advance of the final disposition of this action, suit or proceeding upon receipt of an undertaking by or on behalf of this director or officer to repay such amount if it shall ultimately be determined that such person is not entitled to be indemnified by the corporation, for example, because of a lack of good faith (see DGCL, section 145(e)). Delaware courts have consistently interpreted DGCL, section 145(e) as granting corporations discretion to determine whether to advance litigation expenses to a covered director or officer.

Law stated - 12 May 2023

Exculpation of directors and officers

To what extent may companies or shareholders preclude or limit the liability of directors and officers?

The Delaware Director Protection Statute allows the shareholders of a corporation to provide additional protection to corporate directors through the adoption of a provision in the certificate of incorporation 'eliminating or limiting the personal liability of a director to the corporation or its shareholders for monetary damages for breach of a fiduciary duty as a director' (DGCL, section 102(b)(7)). Such an exculpation provision, however, may not shield directors from liability for: breaches of the duty of loyalty; 'acts or omissions not in good faith or which involve intentional misconduct or a knowing violation of law'; unlawful payments of dividends or unlawful stock purchases or redemptions; or 'any transaction from which the director derived an improper personal benefit'.

In August 2022, Delaware approved amendments to the DGCL which allow Delaware corporations to adopt officer exculpation provisions in their certificates of incorporation, thus expanding such protections to certain corporate officers (with the additional exception that claims against officers will not be barred 'in any action by or in the right of the corporation') including the president, chief executive officer, chief operating officer, chief financial officer, chief legal officer, controller, treasurer or chief accounting officer, the company's most highly compensated executive officers as identified in SEC filings and other officers who consent to being identified as an officer and to service of process. A number of US public companies are seeking shareholder approval of officer exculpation charter amendments at their 2023 annual meetings.

For 2023, ISS will evaluate on a case-by-case basis proposals to amend governance documents to provide for officer exculpation, taking into account the stated rationale and other specified factors. Additionally, ISS will consider the extent to which the proposal would eliminate liability for monetary damages for violating the duty of loyalty but noted that it will generally not support such proposals even if allowed under state law. Glass Lewis will generally recommend voting against any officer exculpation charter amendment proposals unless a compelling rationale is provided by the board, and the provisions are reasonable (ie, they do not go beyond the fullest extent permitted by law).

Law stated - 12 May 2023

DISCLOSURE AND TRANSPARENCY

Corporate charter and by-laws

Are the corporate charter and by-laws of companies publicly available? If so, where?

Corporate certificates of incorporation are publicly available for a small fee from the office of the secretary of state in the state of incorporation. By-laws of private companies are generally not publicly available because they are not required to be filed with the secretary of state. If the corporation is a reporting company, its certificate of incorporation and by-laws are also available as exhibits to various forms filed with the Securities and Exchange Commission (SEC), which can be accessed over the internet free of charge from EDGAR, the SEC database, which is accessible via the SEC's website .

Law stated - 12 May 2023

Company information

What information must companies publicly disclose? How often must disclosure be made?

Federal securities laws and SEC rules require reporting companies (or companies making public offerings) to disclose a wide variety of information in annual and quarterly reports, as well as in proxy statements and public offering prospectuses. In general, a company must disclose all information that would be material to investors. This includes:

- a business description;
- a description of material legal proceedings;
- detailed disclosure of the risks associated with the business and market risk;
- related person transaction disclosure;
- the number of shareholders of each class of common equity;
- management's discussion and analysis of the company's financial condition and results of operations (MD&A);
- a statement as to whether the company has had any disagreements with its accountants;
- disclosure regarding the effectiveness of disclosure controls and procedures, and changes in and the effectiveness of internal control over financial reporting;
- financial information;
- executive and director compensation; and
- a signed opinion of the company's auditors with respect to the accuracy of the financial information.

This report from the auditors also needs to discuss any critical audit matters communicated (or required to be communicated) to the audit committee or state that the auditors determined that there were no critical audit matters.

Corporations are expected to keep all this public information current by filing 'current' reports whenever certain specified events occur, as well as issuing press releases and providing website disclosure.

Since the passage of the Public Company Accounting Reform and Investor Protection Act of 2002 (the Sarbanes–Oxley Act) and its accompanying SEC implementing rules, reporting companies are also required to disclose all material off-balance sheet transactions, arrangements, obligations (including contingent obligations) and certain other relationships of the company with unconsolidated entities or other persons. In addition, the Sarbanes–Oxley Act requires that a reporting company's financial reports reflect 'all material correcting adjustments' identified by outside auditors.

Section 404 of the Sarbanes–Oxley Act requires that a reporting company's annual report include an internal control report from management containing a statement of the responsibility of management for establishing and maintaining an adequate internal control structure and procedures for financial reporting and an assessment at the end of the company's most recent fiscal year of the effectiveness of the company's internal control structure and procedures for financial reporting. The company's registered public accounting firm must also attest to, and report on, the effectiveness of the company's internal control over financial reporting.

Reporting companies are also required to disclose the 'total compensation' received by the corporation's CEO, its CFO and its three most highly compensated executive officers other than the CEO and CFO (together, the named executive officers) and directors. The information is required to be presented in the form of a summary compensation table listing the name of the employee, the year, salary, bonus, other annual compensation, stock and option awards, changes in pension value and non-qualified deferred compensation earnings, all other forms of compensation and total compensation, as well as several other tables relating to grants of plan-based awards, outstanding equity awards, option exercises and vested stock, pension benefits, non-qualified deferred compensation and director compensation. In addition, reporting companies are required to include a 'compensation discussion and analysis' section in their disclosure documents that explains all material elements of the company's compensation of the named executive officers, and includes a description of the company's compensation philosophy and objectives.

The Jumpstart Our Business Startups Act of 2012 affords 'emerging growth companies' (companies that conducted an IPO after 8 December 2011 and have total annual revenues of less than US$1.235 billion) the flexibility to provide

reduced disclosures relating to financials, MD&A and compensation for a maximum period of five years.

SEC regulations also require the disclosure of certain information concerning any beneficial owner known to the company to possess more than 5 per cent of any class of the corporation's voting securities, including the amount of ownership and percentage and title of the class of stock owned. Any person acquiring more than 5 per cent of the equity of a reporting company also must publicly disclose its intentions with respect to such acquisition. In addition, the Securities Exchange Act of 1934 requires that officers, directors and beneficial owners of 10 per cent or more of a company's equity securities file a statement of ownership each time there has been a change in that person's beneficial ownership of the company's securities.

In addition, special attention is given to corporate governance. Reporting companies must include a copy of the audit committee report in their annual proxy statements. This report must disclose, inter alia, whether the committee has reviewed the audited financial statements with management, recommended that the audited statements be included in the corporation's annual report to the board, and discussed certain matters with independent auditors to assess their views on the auditors' independence, the quality of the corporation's financial reporting and the name of the committee member with financial expertise (if any). Under section 406 of the Sarbanes–Oxley Act, companies are required to disclose whether they have adopted a code of ethics for their senior financial officers. If a company has not adopted such a code it must explain why it has not done so. Certain changes to or waivers of any provision of the code must also be disclosed.

Under the Sarbanes–Oxley Act, the reliability and accuracy of the financial and non-financial information disclosed in a company's periodic reports has to be certified by the company's CEO and CFO. In each quarterly report both officers must certify, among other things, that:

- they reviewed the report;
- to their knowledge the report does not contain a material misstatement or omission and that the financial statements and other financial information in the report fairly present, in all material respects, the financial condition of the company, results of its operations and cash flows for the periods covered in the report;
- they are primarily responsible for the company's controls and procedures governing the preparation of all SEC filings and submissions, not just the periodic reports subject to certification; and
- they evaluated the 'effectiveness' of these controls and procedures and reported to the audit committee any significant deficiencies or material weaknesses in the company's financial reporting controls, together with any corrective actions taken or to be taken. Their conclusions must be disclosed in the certified report.

Companies listed on the New York Stock Exchange are required to disclose their corporate governance guidelines. Committee charters (if any) must be disclosed also.

In 2003, the SEC adopted rules that require reporting companies to disclose in their proxy statements or annual reports certain information regarding the director nomination process, including:

- whether the company has a nominating committee and, if not, how director nominees are chosen;
- whether the members of the nominating committee are independent;
- the process by which director nominees are identified and evaluated;
- whether third parties are retained to assist in the identification and evaluation of director nominees;
- minimum qualifications and standards used in identifying potential nominees;
- whether nominees suggested by shareholders are considered; and
- whether nominees suggested by large, long-term shareholders have been rejected.

These rules also require reporting companies to disclose certain information regarding shareholder communications

with directors, including:

- the process by which shareholders can communicate with directors (and, if the company does not have an established process, why it does not);
- whether communications are screened and, if so, how;
- any policies regarding the attendance of directors at annual general meetings (AGMs); and
- the number of directors that attended the preceding year's AGM.

In 2006, the SEC adopted rules that require reporting companies to disclose in their proxy statements or annual reports certain information regarding the corporate governance structure that is in place for considering and determining executive and director compensation, including:

- the scope of authority of the compensation committee;
- the extent to which the compensation committee may delegate any authority to other persons, specifying what authority may be so delegated and to whom;
- any role of executive officers in determining or recommending the amount or form of executive and director compensation; and
- any role of compensation consultants in determining or recommending the amount or form of executive and director compensation, identifying these consultants, stating whether they are engaged directly by the compensation committee or any other person, describing the nature and scope of their assignment and the material elements of the instructions or directions given to the consultants with respect to the performance of their duties under the engagement.

Moreover, in 2009, the SEC adopted rules requiring companies to provide the following enhanced proxy statement disclosures:

- for each director and nominee, the particular experience, qualifications, attributes or skills that led the board to conclude that the person should serve as a director of the company;
- other directorships held by each director or nominee at any public company during the previous five years (rather than only current directorships);
- expanded legal proceedings disclosure relating to the past 10 years (rather than five years);
- whether and, if so, how the nominating committee considers diversity in identifying nominees for director;
- if the nominating committee has a policy with regard to the consideration of diversity in identifying director nominees, how this policy is implemented and how the nominating committee or the board assesses the effectiveness of its policy;
- the board's leadership structure and why the company believes it is the best structure for the company;
- whether and why the board has chosen to combine or separate the CEO and board chair positions;
- where these positions are combined, whether and why the company has a lead independent director and the specific role the lead independent director plays in the leadership of the company;
- the board's role in the oversight of risk management and the effect, if any, that this has on the company's leadership structure;
- the company's overall compensation policies or practices for all employees generally, not just executive officers, 'if the compensation policies and practices create risks that are reasonably likely to have a material adverse effect on the company'; and
- fees paid to and services provided by compensation consultants and their affiliates if the consultants provide consulting services related to director or executive compensation and also provide other services to the company

in an amount valued in excess of US$120,000 during the company's last fiscal year.

In summer 2022, the SEC's Division of Corporation Finance launched a new comment letter initiative urging targeted public companies to enhance their disclosures about the board's leadership structure and role in risk oversight. The stated reason for the initiative is that the Division Staff have noticed that the disclosure required by Item 407(h) of Regulation S-K has become increasingly standardised rather than tailored to a company's individual circumstances. Disclosure should provide investors with insights about why a company has chosen its particular board leadership structure (regardless of the type of leadership structure selected) or how a company's board is discharging its risk oversight responsibilities in light of the specific challenges facing its business.

In 2010, the SEC also issued an interpretive release on disclosure relating to climate change, which is intended to provide guidance to reporting companies on the application of existing disclosure requirements to climate change and other matters. Also in 2010, the SEC issued an interpretive release relating to disclosure of liquidity and funding risks posed by short-term borrowing practices.

The SEC issued disclosure guidance relating to cybersecurity (2011, which was updated in 2018) and European sovereign debt exposure (2012), among other matters.

In 2011, the SEC approved final rules relating to advisory votes on executive compensation (say-on-pay) pursuant to the Dodd–Frank Wall Street Reform and Consumer Protection Act of 2010 (the Dodd–Frank Act), which also require companies to include a discussion in the proxy statement as to whether and, if so, how the company has considered the results of the most recent say-on-pay vote in determining compensation policies and decisions and, if so, how that consideration has affected the company's executive compensation decisions and policies.

In 2012, the SEC approved final rules mandated by the Dodd–Frank Act requiring proxy statement disclosure regarding compensation consultant conflicts of interest. Such disclosure became required to be included in proxy statements for annual meetings occurring on or after 1 January 2013.

In 2012, the Exchange Act was amended by the Iran Threat Reduction and Syria Human Rights Act of 2012 to require public companies to provide disclosure if the company or any of its affiliates (including its directors and officers) has knowingly engaged in certain enumerated activities subject to US trade sanctions involving Iran or specified Iranian entities or nationals as well as certain other non-Iranian persons or entities deemed to promote terrorist activities or the proliferation of weapons of mass destruction. Such disclosure became required to be included in quarterly and annual reports beginning in February 2013.

The Dodd–Frank Act amended the Exchange Act to require disclosure relating to conflict minerals (gold, tantalum, tin and tungsten) originating from the Democratic Republic of Congo or an adjoining country. Since May 2014, public companies have been required to make various disclosures where conflict minerals are necessary to the functionality or production of a product that is either manufactured by the company or by a third party with which the company contracts for such manufacture. A group of business groups filed litigation challenging the conflict minerals rule on several grounds, including that the required disclosure would violate the First Amendment to the US Constitution. In April 2014, the US Court of Appeals for the District of Columbia Circuit found that one disclosure provision of the conflict minerals rule violated the First Amendment but upheld the remainder of the rule. The Court reaffirmed its original ruling in August 2015 and the final judgment in the case was entered in April 2017. In January 2017, the acting chair of the SEC had requested comments on the rule and related guidance through March 2017. In April 2017, the staff of the SEC's Division of Corporation Finance announced that it will not recommend enforcement action if a company fails to comply with certain aspects of the rule relating to due diligence on the source and chain of custody of conflict minerals and an independent private sector audit. The acting chair of the SEC released a statement on the same day announcing that this relief is appropriate because the primary purpose of those requirements is to enable companies to make the disclosure that was found to violate the First Amendment. He directed the SEC staff to develop a recommendation for future SEC action on the rule after taking into consideration the public comments received.

In addition, the Dodd–Frank Act amended the Exchange Act to require 'resource extraction issuers' to disclose specified information regarding payments made to a foreign government or the US federal government for the purpose of commercial development of oil, natural gas or minerals. The SEC adopted a resource extraction disclosure rule in 2012 that was vacated by the US District Court for the District of Columbia in 2013. Later in 2013, the SEC announced that it would redraft the resource extraction rule rather than appeal the ruling. The SEC re-proposed the resource extraction rule in 2015. The SEC rule was repealed in 2017, but the underlying Dodd–Frank Act mandate for SEC rule-making remains intact. The SEC proposed rules in 2019 and the SEC adopted final rules in December 2020 that require resource extraction issuers to make annual filings disclosing payments made to foreign governments or the US federal government for the commercial development of oil, natural gas or minerals.

The Dodd–Frank Act mandated several new executive compensation-related disclosures requiring SEC rule-making, including in relation to the CEO pay ratio, corporate policies on hedging of company stock by directors and employees, 'pay versus performance' and compensation clawback policies requiring the recovery of excess compensation paid to executives. The SEC adopted the CEO pay ratio rule in August 2015 requiring US public companies to disclose the median of the annual total compensation of all company employees except the CEO, the CEO's total annual compensation and the ratio of the former to the latter. Most US public companies first had to comply with the new disclosure requirement in their 2018 annual meeting proxy statements based on 2017 compensation. In December 2018, the SEC adopted a rule that requires a US public company to disclose whether it has adopted practices or policies regarding the ability of its directors and employees (including officers) to hedge the company's equity securities. Most US public companies first had to comply with the new disclosure requirement in their 2020 annual meeting proxy statements. In August 2022, the SEC adopted a final rule to implement section 953(a) of the Dodd-Frank Act that requires certain public companies to disclose information regarding the relationship between executive compensation and actual financial performance, beginning with their 2023 annual meeting proxy statements. Furthermore, in October 2022, the SEC adopted final rules relating to the recovery of erroneously awarded incentive-based executive compensation or 'clawback' policies. The new rules direct the national securities exchanges to establish listing standards that require companies to adopt, disclose and comply with a written clawback policy as a condition to listing. The NYSE and Nasdaq proposed their listing standards on compensation clawbacks in February 2023. The rules also require companies to file their clawback policies an exhibit to their annual reports and to disclose certain information if recovery is triggered under the policy.

In 2018, the SEC issued new interpretive guidance on cybersecurity disclosure that reinforced and expanded upon the 2011 guidance issued by the SEC's Division of Corporation Finance. The guidance illustrates the SEC's increased expectations with respect to how US public companies monitor and disclose cybersecurity risks and incidents. In March 2022, the SEC proposed new cybersecurity rules for public companies that will require them to (1) report material cybersecurity incidents within four days, (2) provide updates on material cybersecurity incidents, (3) provide annual disclosures on the company's cybersecurity risk management framework as well as its cybersecurity governance and (4) provide disclosures concerning the cybersecurity expertise of the company's board of directors. Also in March 2022, President Biden signed into law the Cyber Incident Reporting for Critical Infrastructure Act of 2022 as part of an omnibus appropriations bill, which could overlap with some disclosure obligations of the proposed SEC rules. In May 2022, seven US Senators (all co-sponsors of the Cybersecurity Disclosure Act, which encourages public company boards to play a more effective role in cybersecurity risk oversight), released a letter urging the SEC to finalise cybersecurity disclosure rules for public companies.

Since early 2014, the SEC has engaged in a 'disclosure effectiveness project'. The goal of the project is to review existing disclosure requirements to determine whether modifications should be made to reduce the costs and burdens on public companies while also promoting the disclosure of material information to investors and eliminating duplicative disclosures. In September 2015, the SEC requested comment on the form and content of financial statement disclosures required under Regulation S-X. In April 2016, the SEC issued a concept release seeking public comment on modernising certain business and financial disclosures required by Regulation S-K to be included in public companies' periodic reports. In August 2016, the SEC requested public comment on the compensation and corporate

governance information to be included in US public companies' proxy statements. In March 2017, the SEC approved rules that will require US public companies to provide hyperlinks to the exhibits to their SEC filings, which became effective for the largest category of filers in September 2017. In August 2018, the SEC adopted rule amendments to eliminate or update certain disclosure requirements that have become redundant, duplicative, overlapping, outdated or superseded as a result of more recently updated SEC or generally accepted accounting principles requirements or changes in the information environment. The amendments became effective in November 2018. The SEC adopted rule amendments in March 2019 intended to streamline and improve disclosure requirements applicable to US public companies. The key rule amendments, which became effective in April and May 2019, streamline MD&A disclosure in annual reports, reduce the need to submit confidential treatment requests to the SEC and simplify exhibit filing requirements. In August 2020, the SEC adopted amendments to modernise its rules requiring disclosure about a company's business description, legal proceedings and risk factors. Most notably, the rule amendments require a public company to describe its human capital resources, including any human capital measures or objectives the company focuses on in managing its business, to the extent material to an understanding of the company's business taken as a whole. The amendments became effective in November 2020. Since then, human capital measures have continued to be a major focus of the SEC, in large part due to a high level of investor interest in these matters and the enhanced human capital disclosure requirements. As a disclosure topic human capital management is becoming less principles-based and more prescriptive. The SEC is contemplating proposing further rule amendments that would require additional disclosure regarding human capital management.

In November 2020, the SEC adopted amendments to modernise, streamline and enhance certain financial disclosure requirements in Regulation S-K. The rule amendments, which became effective in February 2021, are intended to improve the quality of MD&A disclosures by emphasising a principles-based approach and reduce the compliance burden on companies by eliminating several more prescriptive requirements.

In January 2020, the SEC issued new interpretive guidance on disclosure of key performance indicators and other metrics in the MD&A section of public companies' periodic reports.

In August 2021, the SEC approved changes to the Nasdaq listing rules relating to board diversity. The rule changes will require each Nasdaq-listed company, subject to certain exceptions, to (1) publicly disclose annually in an aggregated form, to the extent permitted by applicable law, information on the voluntary self-identified gender and racial characteristics and LGBTQ+ status of the company's board of directors, and (2) have, or explain why it does not have, at least two directors who are diverse, including at least one director who self-identifies as female and at least one director who self-identifies as either an underrepresented minority or LGBTQ+. Companies will be required to have at least one diverse director by 31 December 2023 and at least two diverse directors by 31 December 2025 or 31 December 2026, depending on the size of the company and its stock market exchange tier. A Nasdaq-listed company with a board of five or fewer members will be required to have, or explain why it does not have, at least one diverse director by 31 December 2023.

For purposes of the new Nasdaq rules, (1) 'diverse' means an individual who self-identifies as a female, an underrepresented minority or LGBTQ+, (2) 'female' means an individual who self-identifies her gender as a woman, without regard to the individual's designated sex at birth, (3) 'underrepresented minority' means an individual who self-identifies as one or more of the following: Black or African American, Hispanic or Latinx, Asian, Native American or Alaska Native, Native Hawaiian or Pacific Islander, or Two or More Races or Ethnicities, and (4) 'LGBTQ+' means an individual who self-identifies as any of the following: lesbian, gay, bisexual, transgender, or as a member of the queer community.

In December 2022, the SEC adopted rules that significantly alter the Exchange Act Rule 10b5-1 framework and add substantial new disclosure requirements. The amendments add new conditions to the availability of the affirmative defence to insider trading liability, impose new disclosure requirements regarding officer and director trading plans, insider trading policies and timing of certain stock awards, and amend Forms 4 and 5 to require earlier disclosure of gifts and explicit disclosure of Rule 10b5-1 transactions.

In May 2023, the SEC adopted rule amendments to require more detailed disclosure regarding repurchases of a company's registered equity securities. Specifically, the rules will require companies to disclose a table of daily quantitative share repurchase information in quarterly reports (the rule proposal from December 2021 had contemplated next-day reporting of repurchases). The rules will also require narrative disclosure in periodic reports about a company's repurchase programmes and practices and details about a company's adoption and termination of Exchange Act Rule 10b5-1 trading arrangements.

In May 2022, the SEC released a sample letter containing guidance for companies on disclosure obligations relating to Russia's invasion of Ukraine. The letter encourages companies to disclose any direct or indirect exposure to Russia, Belarus or Ukraine, new or heightened cybersecurity risk and actions taken to mitigate such risks, as well as known trends or uncertainties impacting the company's financial condition arising from Russia's invasion of Ukraine. Companies are also encouraged to disclose any material impact of import/export bans or supply chain disruptions. Furthermore, the letter addresses critical accounting estimate disclosures, non-GAAP financial measures, and internal control over financial reporting in the context of the Russia/Ukraine war.

SEC recent developments illustrate a heightened focus on matters related to climate and environmental, social and governance (ESG) with momentum toward the SEC developing a comprehensive ESG disclosure framework and increased scrutiny of climate and ESG disclosures. The SEC is taking a 'whole agency' approach to ESG: rulemaking, enforcement scrutiny and interpretive guidance. In March 2021, the SEC created a Climate and ESG Task Force in its Enforcement Division. Since then, the SEC has investigated and filed a number of ESG-related enforcement actions against public companies based on false or misleading disclosures made in publicly available ESG or sustainability reports. In September 2021, the SEC released a sample letter demonstrating the type of comments the SEC's Division of Corporation Finance has been issuing to companies asking detailed questions regarding climate-related disclosure or the absence of such disclosure in companies' Form 10-Ks. In March 2022, the SEC issued proposed rules that would require public companies to include extensive climate-related information in their registration statements and periodic reports. The proposed rules would require disclosure concerning climate-related risks and impacts, oversight and governance of climate-related risks, climate-related financial statement metrics, climate-related goals, and greenhouse gas emissions. If adopted, the rules would present substantial new disclosure responsibilities for public companies. Whereas many public companies have been issuing voluntary climate-related disclosures outside of SEC filings, the proposed rules would require them to disclose such information in SEC filings according to rigorous disclosure methods, and certain information would be subject to attestation or independent audit requirements. The proposed rules would also indirectly compel companies to have monitoring, accounting, planning, and governance practices in place to enable them to satisfy the proposed disclosure requirements. In June 2022 , the US Supreme Court decided West Virginia et al v Environmental Protection Agency , holding that the Environmental Protection Agency lacks authority under section 7411(d) of the Clean Air Act to limit greenhouse gas emissions from power plants. This limitation of a federal agency's administrative authority may complicate the SEC's landmark climate-related rule proposal.

Law stated - 12 May 2023

HOT TOPICS

Shareholder-nominated directors

Do shareholders have the ability to nominate directors and have them included in shareholder meeting materials that are prepared and distributed at the company's expense?

Since September 2011, companies can no longer exclude from their proxy materials shareholder proposals (precatory or binding) relating to by-law amendments establishing procedures for shareholder nomination of director candidates and inclusion in the company's proxy materials, as long as the proposal is not otherwise excludable under Rule 14a-8.

This amendment to Rule 14a-8 facilitates the development of ‘proxy access’ via private ordering at companies chartered in states where permissible, as shareholders are able to institute a shareholder nomination regime via binding by-law amendment or request, via precatory shareholder proposal, that such a by-law be adopted by the board.

The private ordering process gained considerable momentum during 2015, which saw a significant increase in the number of shareholder proxy access proposals submitted (more than 100) and shareholder support for such proposals (60 per cent of the total proposals voted on passed), as well as an increased frequency of negotiation and adoption of proxy access via board action. In response to shareholder proposals and increasing pressure from institutional investors and proxy advisory firms, nearly 1000 companies have adopted proxy access, including 85 per cent of S&P 500 companies as of May 2023 (up from less than 1 per cent in 2014). Proxy access is extending significantly into the next tier of large public companies with just under 60 per cent of Russell 1000 companies having adopted proxy access as of May 2023. The market standard that has emerged gives a group of up to 20 shareholders who hold 3 per cent of the company’s common stock for at least three years the right to nominate up to 20 per cent of the company’s directors (or at least two directors) using the company’s proxy materials. Proxy access provisions typically include limitations on the use of proxy access (eg, in contested election situations) and require detailed information to be provided in relation to the nominee and the nominating group, among other requirements.

In the past seven years, shareholders have been submitting proposals requesting that companies make amendments to their proxy access by-laws (eg, to increase or remove the limit on the size of the nominating shareholder group). These ‘fix-it’ proposals have largely been excludable if the SEC staff has agreed that the company has substantially implemented the proposal, or failed to receive majority support. Two ‘fix-it’ proposals filed by shareholders passed in 2016, but all others filed since have failed.

In November 2021, the SEC adopted changes to the federal proxy rules to require the use of 'universal' proxy cards. The new rules change the methods by which public companies and shareholders have solicited proxies for decades, and allow shareholders to vote for a mix of management and dissident nominees in a contested director election. The new rules will reshape the process by which hostile bidders, activist hedge funds, social and environmental activists, and other dissident shareholders may utilise director elections to influence control and policy at public companies. The new rules also amend certain form of proxy and disclosure requirements relating to voting options and standards that apply to all director elections, whether or not contested. The rules are now effective for shareholder meetings held after 31 August 2022.

Law stated - 12 May 2023

Shareholder engagement

Do companies engage with shareholders? If so, who typically participates in the company’s engagement efforts and when does engagement typically occur?

Shareholder influence is more potent than ever and continued attention to the quality of shareholder relations has become paramount. Companies are engaging with their key large institutional investors more directly and more frequently to hear their interests and concerns, including from a governance perspective. Whereas engagement with shareholders used to occur primarily during the annual meeting season, companies are now engaging with their shareholders throughout the year. There are several reasons for this, including:

- the advent of the shareholder advisory vote on executive compensation;
- a rise in hedge fund activism;
- proxy advisory firm policies that expect companies to respond to shareholder advisory votes that receive significant (but less than passing) support; and
- shareholder expectations.

Shareholders are also increasingly seeking to engage with companies outside of the shareholder proposal mechanism. For example, in addition to more frequent one-on-one meetings between the company and shareholders, it is becoming more common for large institutional investors to send letters on specific issues of concern to portfolio companies. In recent years, public campaigns of this sort have urged CEOs to disclose a long-term strategic plan to shareholders, the adoption of proxy access and more direct engagement between directors and shareholders. In particular, BlackRock, State Street and Vanguard, three of the largest institutional investors in the United States, have recently become more assertive in pushing for corporate governance reforms and increased director–shareholder engagement at the companies in which they invest.

Members of senior management, such as the CEO and CFO, are typically the company representatives who engage with shareholders. Investor relations personnel may also be involved in shareholder engagement efforts. Outside counsel rarely participates. Directors are becoming more involved in shareholder engagement. Which director is involved depends on the topics to be discussed. Often the lead director or the relevant committee chair will meet with the shareholder along with a member of senior management. For example, the compensation committee chair may be called upon to meet with an investor who has concerns with the company's executive compensation programme.

Directors of US public companies should understand the composition and particular interests of their shareholder base and be actively involved in overseeing the company's shareholder engagement and investor relations efforts. Many companies are also engaging with a broader group of shareholders rather than just the top few holders. Companies are also increasingly providing disclosure regarding their shareholder engagement efforts in their annual meeting proxy statements. In 2015, the Council of Institutional Investors (CII) issued a report calling for enhanced disclosure relating to company-shareholder engagement. Specifically, the CII provided 'best in class' examples of disclosure of engagement policies and practices.

Law stated - 12 May 2023

Sustainability disclosure

Are companies required to provide disclosure with respect to corporate social responsibility matters?

It is common for US public companies to report on corporate social responsibility (CSR) and ESG matters including environmental, social and ethical issues. Several SEC disclosure requirements tend to trigger disclosure of CSR matters, typically in quarterly and annual reports:

- business description disclosure;
- legal proceedings disclosure;
- material known events and uncertainties disclosure included in management's discussion and analysis of the company's financial condition and results of operations;
- risk factor disclosure;
- guidance regarding climate change disclosure; and
- conflict minerals disclosure.

In August 2020, the SEC adopted rules that require disclosure of any human capital measures or objectives that management focuses on in managing the business (such as those that address the attraction, development and retention of personnel) to the extent material to an understanding of the company's business. The amendments became effective in November 2020. Since then, human capital measures have continued to be a major focus of the

SEC, in large part due to a high level of investor interest in these matters and the enhanced human capital disclosure requirements. As a disclosure topic human capital management is becoming less principles-based and more prescriptive. The SEC is contemplating proposing further rule amendments that would require additional disclosure regarding human capital management.

SEC recent developments illustrate a heightened focus on matters related to climate and ESG-related matters and momentum toward the SEC developing a comprehensive ESG disclosure framework and increased scrutiny of climate and ESG disclosures. The SEC is taking a 'whole agency' approach to ESG: rulemaking, enforcement scrutiny and interpretive guidance. In March 2021, the SEC created a Climate and ESG Task Force in its Enforcement Division. Since then, the SEC has investigated and filed a number of ESG-related enforcement actions against public companies based on false or misleading disclosures made in publicly available ESG or sustainability reports. In September 2021, the SEC released a sample letter demonstrating the type of comments the SEC's Division of Corporation Finance has been issuing to companies asking detailed questions regarding climate-related disclosure or the absence of such disclosure in companies' recent Form 10-Ks. In March 2022, the SEC issued proposed rules that would require public companies to include extensive climate-related information in their registration statements and periodic reports. The proposed rules would require disclosure of:

- climate-related risks reasonably likely to have a material impact on the company's business or consolidated financial statements, within the existing definition of materiality
- the actual and potential impacts of material climate-related risks on a company's strategy, business model, and outlook
- the manner in which a company's board oversees climate-related risks and management's role in assessing and managing those risks
- processes for identifying, assessing, and managing climate-related risks
- various climate-related financial statement metrics
- climate-related targets and goals, if the company has set them
- direct (Scope 1) and indirect (Scope 2) greenhouse gas (GHG) emissions data — as well as additional upstream/downstream indirect GHG emissions (Scope 3) if material or if the company has set targets for Scope 3 emissions.

If adopted, the rules would present substantial new disclosure responsibilities for public companies. Whereas many public companies have been issuing voluntary climate-related disclosures outside of SEC filings, the proposed rules would require them to disclose such information in SEC filings according to rigorous disclosure methods, and certain information would be subject to attestation or independent audit requirements. The proposed rules would also indirectly compel companies to have monitoring, accounting, planning, and governance practices in place to enable them to satisfy the proposed disclosure requirements.

In June 2022 , the US Supreme Court decided West Virginia et al v Environmental Protection Agency , holding that the Environmental Protection Agency lacks authority under section 7411(d) of the Clean Air Act to limit greenhouse gas emissions from power plants. This limitation of a federal agency's administrative authority may complicate the SEC's landmark climate-related rule proposal.

Many companies already report on ESG matters voluntarily (eg, as of 2020, 92 per cent of S&P 500 companies and 70 per cent of Russell 1000 companies published annual sustainability or responsibility reports). In late 2019, the US Chamber of Commerce released a set of best practices to guide companies in making voluntary disclosure about ESG topics and steer the development of a widely adopted approach to voluntary ESG reporting without the need for additional regulatory mandates. Companies may be subject to additional disclosure requirements under state law (eg, certain companies doing business in California are required to disclose measures they take to eliminate slavery and human trafficking in their supply chains).

Many companies consider three influential guides when determining if and what to disclose regarding ESG issues: the Global Reporting Initiative Sustainability Reporting Standards, the Sustainability Accounting Standards Board Implementation Guide (the final standards of which were released in November 2018) and the Recommendations of the Task Force on Climate-related Financial Disclosures (TCFD).

In 2018, ISS launched an Environmental & Social (E&S) QualityScore scoring tool that measures the depth and extent of corporate disclosure on environmental and social issues, including sustainability governance, and identifies key disclosure omissions. This metric for institutional investors to use to evaluate the E&S risk of their portfolio companies has prompted greater disclosure of E&S matters by some US public companies.

For 2023, ISS has expanded the scope of its climate accountability policy to apply globally. ISS will recommend voting against the incumbent chair of the responsible committee (or other directors on a case-by-case basis) at companies that are significant greenhouse gas (GHG) emitters (ie, companies in the Climate Action 100+ Focus Group) in cases where ISS determines the company is not taking the minimum steps needed to assess and mitigate climate-related risks, such as according to the TCFD and quantitative GHG emissions reduction targets covering at least a significant portion of the company's direct emissions. For this same group of companies, Glass Lewis expects thorough climate-related disclosures in line with TCFD recommendations and disclosure of explicit and clearly defined oversight responsibilities for climate-related issues, or it may recommend votes against the chair of the committee (or additional committee members) charged with oversight of climate-related issues.

Glass Lewis will generally recommend voting against the governance committee chair of Russell 1000 companies that have not provided explicit disclosure regarding the board's role in E&S risk oversight.

In recent years, large institutional investors have urged companies to disclose how long-term strategy incorporates corporate sustainability considerations. In January 2021, Larry Fink, BlackRock's chair and CEO released his annual letter to the CEOs of its portfolio companies warning that BlackRock will vote against directors at companies that do not make sufficient progress on implementing sustainable business practices and improving their climate change and sustainability-related disclosures. He called for a single global standard for ESG disclosure but, in the meantime, BlackRock continues to endorse the ESG disclosure framework of the Sustainability Accounting Standards Board (SASB) and TCFD recommendations. He also noted that BlackRock expects public companies to incorporate climate risk as part of their oversight of long-term strategies and to disclose how they are addressing climate-related risks. Finally, BlackRock asked companies to disclose their long-term strategies for improving diversity, equity and inclusion in their sustainability reports.

Mr Fink's 2022 annual letter continued to focus on ESG matters and related disclosures. The letter highlighted that BlackRock expects companies to (1) focus more on human capital management and board oversight thereof and (2) set short-, medium- and long-term targets for GHG reductions and issue reports consistent with the TCFD. In his 2023 annual letter, Mr Fink noted that BlackRock continues to view climate risk as an investment risk and advocated for enhanced disclosures about how companies plan to navigate the energy transition.

BlackRock asks companies to disclose a business plan for how they intend to deliver long-term financial performance through the transition to global net zero, consistent with their business model and sector. BlackRock expects companies to demonstrate their plan's resilience under various decarbonisation scenarios and the global aspiration of limiting warming to 1.5 degrees celsius. BlackRock's guidelines also encourage companies to disclose how considerations related to having a reliable energy supply and just transition affect their plans. Finally, BlackRock expects greater disclosure on capital allocations across alternative energy sources and transition technologies to ensure these are consistent with the company's stated transition strategy. While maintaining the desire for reporting aligned with the TCFD recommendations and supported by SASB industry-specific metrics, BlackRock acknowledges that some companies may report using other reporting standards. In those instances, BlackRock requests that companies disclose the metrics that are specific to the company or industry.

In 2018, State Street sent letters to all companies in the S&P 500 encouraging them to proactively disclose their

compliance with the Investor Stewardship Group's corporate governance and sustainability principles. State Street votes against the independent board leader at companies that do not comply with the principles and companies that cannot explain the nuances of their governance structure effectively, either publicly or through engagement.

In its 2023 voting guidelines, State Street Global Advisors endorses TCFD-related disclosures and indicates that it may take voting action against S&P 500 companies that fail to provide sufficient disclosure regarding company-specific climate-related risks and opportunities or board oversight of climate-related risks and opportunities, in accordance with the TCFD framework.

Law stated - 12 May 2023

CEO pay ratio disclosure

Are companies required to disclose the 'pay ratio' between the CEO's annual total compensation and the annual total compensation of other workers?

The SEC adopted the CEO pay ratio rule in August 2015 requiring US public companies to disclose the median of the annual total compensation of all company employees except the CEO, the CEO's total annual compensation and the ratio of the former to the latter. For calendar-year companies, the first disclosure was required in 2018 annual meeting proxy statements based on 2017 compensation. In September 2017, the SEC published guidance to assist US public companies as they prepare for compliance with the CEO pay ratio disclosure rule. Taken as a whole, the guidance makes clear that companies have substantial flexibility in developing their response to the new disclosure requirement.

Law stated - 12 May 2023

Gender pay gap disclosure

Are companies required to disclose 'gender pay gap' information? If so, how is the gender pay gap measured?

US public companies are not required to disclose gender pay gap information. However, in recent years, some investors have filed shareholder proposals primarily at companies in the technology and financial services industries requesting them to measure, disclose and take action to close gender pay gaps. In exchange for withdrawal of the proposals, some of the targeted companies committed to reporting certain pay data by gender and taking steps to reduce any identified gender pay gaps. The first of these reports among US public companies was published by a large financial institution in early 2019. Since 2018, ISS evaluates shareholder proposals seeking reports on a company's pay data by gender, or policies or goals aimed at reducing any gender pay gap, on a case-by-case basis considering specified factors. Glass Lewis adopted a similar policy, which took effect for the 2017 proxy season.

Law stated - 12 May 2023

UPDATE AND TRENDS

Recent developments

Identify any new developments in corporate governance over the past year. Identify any significant trends in the issues that have been the focus of shareholder interest or activism over the past year.

Public companies are facing increased pressures from investors, customers and employees on environmental, social and governance (ESG) issues, especially board diversity, human capital management and climate issues. Human

capital management covers a broad range of workforce matters, including diversity and inclusion, employee satisfaction and engagement, succession and talent management, and ethics, workforce culture and risk. In August 2020, the Securities and Exchange Commission (SEC) adopted rules that require disclosure of any human capital measures or objectives that management focuses on in managing the business (such as those that address the attraction, development and retention of personnel) to the extent material to an understanding of the company's business. The amendments became effective in November 2020. Since then, human capital measures have continued to be a major focus of the SEC, in large part due to a high level of investor interest in these matters and the enhanced human capital disclosure requirements. As a disclosure topic human capital management is becoming less principles-based and more prescriptive. The SEC is contemplating proposing further rule amendments that would require additional disclosure regarding human capital management.

The covid-19 pandemic, together with the shift to a knowledge-based economy, highlighted the value of human capital and triggered changes in business needs, work preferences, the market for human capital, and associated risks (eg, cybersecurity and compliance). Human capital management issues are critical to corporate culture, and are a key area for board oversight. These issues include:

- talent management, including employee recruitment, promotion, and retention;
- employee health and safety;
- fair compensation and benefits, including minimum wage, pay equity, and paid leave;
- DEI at all levels of the company;
- training and career development initiatives;
- workforce management issues, including layoffs;
- efforts to combat discrimination, harassment, and bullying; and
- treatment of whistleblowers.

Calls among investors and other stakeholders for disclosure of EEO-1 workforce demographic data have been gaining traction. Disclosure of EEO-1 reports (which provide a racial, gender and job category breakdown of a company's US workforce) would enable measurement and comparison over time between companies and within individual companies. Sustainability Accounting Standards Board (SASB) Standards for certain industries recommend disclosure of EEO-1 data and recent shareholder proposals have asked for annual disclosures of EEO-1 data. The Office of the New York City Comptroller launched a letter-writing campaign in 2020 urging S&P 100 companies publicly disclose their EEO-1 reports when submitted to the EEOC annually. In December 2022, the NYC Comptroller announced that the number of S&P 100 companies disclosing EEO-1 reports has increased from 14 to more than 90 since 2020 demonstrating the success of the campaign.

US public companies remain under pressure to enhance the diversity of their boards and related disclosures, and the focus has expanded beyond increasing gender diversity to ethnic and racial diversity. In September 2018, a California law was enacted that required California-headquartered publicly held domestic or foreign corporations to have at least one female director by the end of 2019 and, depending on board size, up to three female directors by the end of 2021. In April 2022, a judge in the Los Angeles County Superior Court struck down the law as unconstitutional, holding that it posed a 'total and fatal' conflict with the California Constitution's Equal Protection Clause by requiring corporations to use suspect demographic classifications in the selection of board members to the exclusion of other people from different races, sexual orientations or gender identities. A similar California law enacted in 2020 that required such corporations to have at least one director from an underrepresented community by the end of 2021 and, depending on board size, up to three directors from underrepresented communities by the end of 2022, was also struck down as unconstitutional for similar reasons. Several other states have enacted or are considering legislation that would encourage greater board diversity or require disclosure about board diversity.

In August 2021, the SEC approved changes to the Nasdaq listing rules relating to board diversity. The rule changes will

require each Nasdaq-listed company, subject to certain exceptions, to (1) publicly disclose annually in an aggregated form, to the extent permitted by applicable law, information on the voluntary self-identified gender and racial characteristics and LGBTQ+ status of the company's board of directors, and (2) have, or explain why it does not have, at least two directors who are diverse, including at least one director who self-identifies as female and at least one director who self-identifies as either an underrepresented minority or LGBTQ+. Companies will be required to have at least one diverse director by 31 December 2023 and at least two diverse directors by 31 December 2025 or 31 December 2026, depending on the size of the company and its stock market exchange tier. A Nasdaq-listed company with a board of five or fewer members will be required to have, or explain why it does not have, at least one diverse director by 31 December 2023.

For purposes of the new Nasdaq rules, (1) 'diverse' means an individual who self-identifies as a female, an underrepresented minority or LGBTQ+, (2) 'female' means an individual who self-identifies her gender as a woman, without regard to the individual's designated sex at birth, (3) 'underrepresented minority' means an individual who self-identifies as one or more of the following: Black or African American, Hispanic or Latinx, Asian, Native American or Alaska Native, Native Hawaiian or Pacific Islander, or Two or More Races or Ethnicities, and (4) 'LGBTQ+' means an individual who self-identifies as any of the following: lesbian, gay, bisexual, transgender, or as a member of the queer community.

ISS will generally recommend withholding or voting against the nominating committee chair (and potentially other directors) at all companies where there are no women on the board or the board has no apparent racially or ethnically diverse members, unless there was at least one woman or racially/ethnically diverse director at the preceding annual meeting and the board commits to restore gender or racial/ethnic diversity by the next annual meeting. This policy applies to Russell 3000 or S&P 500 companies and the gender diversity policy will apply to companies outside of those indices beginning in 2023.

In 2022, ISS updated its E&S QualityScore scoring tool to include new or expanded factors relating to diversity, equity and inclusion at the board and executive level (including whether there are LGBTQ+ directors and ethnically diverse directors) and voluntary public disclosure of US Equal Employment Opportunity Commission data (ie, EEO-1 reports).

As of 2023, at Russell 3000 companies, Glass Lewis will generally recommend voting against the nominating committee chair of a board that is not at least 30 per cent gender diverse and the entire nominating committee of a board with no gender diverse directors. For companies outside the Russell 3000, Glass Lewis will generally recommend voting against the nominating committee chair if there are no gender diverse directors.

Finally, as of 2023, at Russell 1000 companies, Glass Lewis will generally recommend voting against the nominating committee chair of a board that does not have at least one director from an underrepresented community. Glass Lewis may refrain from issuing negative voting recommendations against directors at companies that have provided a sufficient rationale or plan to address the lack of diversity on the board.

Furthermore, as of 2023, Glass Lewis will generally recommend votes against the nominating committee chair at Russell 1000 companies that have not provided any disclosure in their proxy statements in any of the following categories: (1) the board's current percentage of racial/ethnic diversity, (2) whether the board's definition of diversity explicitly includes gender and/or race/ethnicity, (3) whether the board has adopted a 'Rooney Rule' policy requiring women and minorities to be included in the initial pool of candidates when selecting new director nominees and (4) board skills disclosure. Additionally, Glass Lewis will recommend votes against the nominating committee chair at such companies that have not provided any disclosure of individual or aggregate racial/ethnic minority demographic information.

Since January 2021, Goldman Sachs will not take a company public unless it has at least two diverse board candidates, one of whom must be female. As of 2023, Goldman Sachs Asset Management votes against the entire board at any company with no female directors, and against all nominating committee members at any company that does not have at least 10 per cent women directors and at least one other diverse director. At S&P 500 companies, Goldman Sachs will vote against nominating committee members at any company with a board that does not have at least one diverse director from an underrepresented ethnic group.

The national focus on racial justice and equity in the United States in 2020 stemming from the killing of George Floyd created new theories of liability in shareholder litigation. Since 2020, dozens of lawsuits have been filed against large public companies alleging that company directors violated their duties to the company and shareholders by, among other things, failing to have a sufficiently racially diverse board, or claiming that the companies' disclosures about diversity-related initiatives misled shareholders. As of April 2023, several of the lawsuits have been dismissed.

Consistent with their fiduciary obligations to act in the interests of the company, including the long-term interests of shareholders, boards have a responsibility to address social justice issues that affect the company's performance, operations, risk profile and relationships with important stakeholders. This calls for more critical, internal evaluation of how corporate activities may contribute to, or may ameliorate, adverse social impacts, for example, with respect to racial inequity and underrepresented and underserved communities.

Employees and consumers are paying more attention to public companies' policies and practices when deciding where to work and what to buy. Moreover, corporate social responsibility is broadly accepted as a legitimate pursuit of public companies, at least so long as there is a reasonable nexus to long-term shareholder value. Accordingly, it becoming somewhat expected for CEOs to issue personal statements or for their companies to issue public statements to take action on social, environmental and political issues.

The SEC adopted controversial rule amendments in 2020 that increased the eligibility requirements for submitting a shareholder proposal to a tiered approach depending on the level of ownership and the relevant holding period: at least US$2,000 if held for at least three years, at least US$15,000 if held for at least two years and at least US$25,000 if held for at least one year. The rule amendments also increased the prior shareholder support thresholds for resubmitting substantially similar shareholder proposals at the same company in future years and clarify that one person may not submit more than one proposal, directly or indirectly, to a company for the same shareholder meeting.

In late 2022, ISS and Glass Lewis released updates to their proxy voting policies for the 2023 proxy season. The key policy updates relate to the following topics:

- board diversity – both gender and racial/ethnic – and related disclosures;
- officer exculpation charter amendment proposals;
- board accountability for climate-related issues and problematic governance and capital structures;
- board accountability for risk oversight failures related to environmental and social issues and cybersecurity;
- director overboarding;
- shareholder proposals requesting racial equity audits or disclosure about political spending and lobbying congruency; and
- compensation-related matters.

In six recent instances, a Delaware court declined to dismiss a claim alleging that directors had not satisfied their duty to exercise oversight. This unprecedented number of 'Caremark' claims surviving a motion to dismiss re-emphasises the importance of board focus on risk oversight, process and controls. This was especially important amid the covid-19 pandemic which presented companies with unique challenges and risks. To avoid any potential 'Caremark' claim, directors must become informed of the critical risks facing the company (including from covid-19), ask questions and take timely and informed actions to ensure that management is addressing those critical risks.

A recent Delaware Chancery Court opinion clarified that, as with directors, a corporate officer's fiduciary duties encompass a duty of oversight. (In re McDonald's Corp Stockholder Derivative Litig (Del Ch 2023)). Accordingly, officers of Delaware corporations, like directors, must (1) make a good-faith effort to put in place reasonable information systems to generate the information necessary to address risks and report upward to higher-level officers or the board and (2) not consciously ignore red flags indicating that the company may suffer harm. Officers will not be held liable for violations of the duty of oversight unless they are shown to have acted in bad faith.

Unlike the duties of directors, the scope of an officer's duty of oversight may be limited to the context in which the officer operates. For example, although a CEO or chief compliance officer has a 'company-wide oversight portfolio', a chief legal officer may be responsible only for oversight of risks within the legal function. The court noted, however, that where red flags are 'sufficiently prominent', any officer has a duty to report upward to the CEO or the board.

Corporate officers are well advised to continue to ensure that they are receiving periodic information and conducting regular reviews of risks in their areas of responsibility and that CEOs and chief compliance officers in particular are receiving such reporting on an enterprise-wide basis. Memorialisation of such risk reviews may also help in establishing that officers have endeavored to fulfill their oversight duties in good faith.

The number of US companies that held virtual-only annual shareholder meetings skyrocketed in 2020 when the covid-19 pandemic made in-person shareholder meetings impossible or inadvisable. Virtual shareholder meetings, both virtual-only and hybrid format, are becoming commonplace practice as companies and service providers gain more experience.

Currently, ISS prefers a hybrid approach but does not have a policy to recommend voting against directors at companies that hold virtual-only meetings. ISS encourages companies holding virtual-only meetings to disclose the circumstances under which virtual-only meetings would be held, and provide shareholders with comparable rights and opportunities to participate electronically as they would have during an in-person meeting. ISS will vote case-by-case on shareholder proposals concerning virtual-only meetings, considering the scope and rationale of the proposal, and concerns identified with the company's prior meeting practices.

Similarly, Glass Lewis prefers a hybrid approach. In egregious cases, Glass Lewis may recommend voting against governance committee members where a company chooses to hold a virtual-only shareholder meeting and does not provide sufficient disclosure in its proxy statement assuring shareholders will be afforded the same rights and opportunities to participate as they would at an in-person meeting.

Some large institutional investors (eg, CalPERS and the New York City Pension Funds) oppose virtual-only shareholder meetings and may vote against directors at companies that hold them.

In March 2022, the CII updated its corporate governance policies to give companies more flexibility with respect to the format of their shareholder meetings. The updated policies state that companies should acknowledge that many investors prefer in-person meetings but should have 'the flexibility to choose an in-person, hybrid or virtual-only format depending on their shareowner base and current circumstances.' Companies should use virtual technology 'as a tool for broadening, not limiting, shareowner meeting participation' and should disclose the circumstances under which a virtual-only meeting would be held and provide shareholders participating virtually with comparable rights and opportunities as those whom attend in person.

In January 2022, the SEC staff issued updated guidance for conducting shareholder meetings in light of covid-19 concerns. The staff encourages companies to provide shareholder proponents or their representatives with the ability to present their shareholder proposals through alternative means (eg, by phone) if they are unable to appear at the meeting to present them in person.

The Delaware Director Protection Statute allows the shareholders of a corporation to provide additional protection to corporate directors through the adoption of a provision in the certificate of incorporation 'eliminating or limiting the personal liability of a director to the corporation or its shareholders for monetary damages for breach of a fiduciary

duty as a director' (DGCL, section 102(b)(7)), with certain exceptions. In August 2022, Delaware approved amendments to the DGCL which allow Delaware corporations to adopt officer exculpation provisions in their certificates of incorporation, thus expanding such protections to certain corporate officers (with the additional exception that claims against officers will not be barred 'in any action by or in the right of the corporation') including the president, chief executive officer, chief operating officer, chief financial officer, chief legal officer, controller, treasurer or chief accounting officer, the company's most highly compensated executive officers as identified in SEC filings and other officers who consent to being identified as an officer and to service of process. A number of US public companies are seeking shareholder approval of officer exculpation charter amendments at their 2023 annual meetings.

For 2023, ISS will evaluate on a case-by-case basis proposals to amend governance documents to provide for officer exculpation, taking into account the stated rationale and other specified factors. Additionally, ISS will consider the extent to which the proposal would eliminate liability for monetary damages for violating the duty of loyalty but noted that it will generally not support such proposals even if allowed under state law. Glass Lewis will generally recommend voting against any officer exculpation charter amendment proposals unless a compelling rationale is provided by the board, and the provisions are reasonable (ie , they do not go beyond the fullest extent permitted by law).

In late summer 2022, the SEC's Division of Corporation Finance launched a new comment letter initiative urging targeted public companies to enhance their disclosures about the board's leadership structure and role in risk oversight. The stated reason for the initiative is that the Division Staff have noticed that the disclosure required by Item 407(h) of Regulation S-K has become increasingly standardised rather than tailored to a company's individual circumstances. Disclosure should provide investors with insights about why a company has chosen its particular board leadership structure (regardless of the type of leadership structure selected) or how a company's board is discharging its risk oversight responsibilities in light of the specific challenges facing its business.

In December 2022, the SEC adopted rules that significantly alter the Exchange Act Rule 10b5-1 framework and add substantial new disclosure requirements. The amendments add new conditions to the availability of the affirmative defence to insider trading liability, impose new disclosure requirements regarding officer and director trading plans, insider trading policies and timing of certain stock awards, and amend Forms 4 and 5 to require earlier disclosure of gifts and explicit disclosure of Rule 10b5-1 transactions. In 2023, both the SEC and the US Department of Justice have shown a renewed interest in insider trading, including by bringing an enforcement action and criminal indictment, respectively, against a company executive for alleged misuse of a Rule 10b5-1 trading plan.

In May 2022, the SEC released a sample letter containing guidance for companies on disclosure obligations relating to Russia's invasion of Ukraine. The letter encourages companies to disclose any direct or indirect exposure to Russia, Belarus or Ukraine, new or heightened cybersecurity risk and actions taken to mitigate such risks, as well as known trends or uncertainties impacting the company's financial condition arising from Russia's invasion of Ukraine. Companies are also encouraged to disclose any material impact of import/export bans or supply chain disruptions. Furthermore, the letter addresses critical accounting estimate disclosures, non-GAAP financial measures, and internal control over financial reporting in the context of the Russia/Ukraine war.

Since late 2022, the US Department of Justice Antitrust Division (DOJ) has issued a series of warning letters to companies and individuals with purported 'interlocking directorates', alleging violations of section 8 of the Clayton Antitrust Act, then issued a press release announcing several director resignations in response. Under section 8, an individual or entity is prohibited from serving as a director or board-appointed officer of two or more competing companies. Section 8 has traditionally been enforced as part of the Hart-Scott-Rodino (HSR) merger review process, whereby merging parties submit mandatory information about their businesses and competitive overlaps. With these letters, DOJ signaled that it is willing to dedicate both time and resources to identify interlocking directorates in publicly available information (eg, Form 10-Ks), outside of the HSR process.

Shareholder activism

Shareholders are continuing to engage companies and press for reforms in the areas of shareholder rights and board composition and quality, but they are also increasing their focus on ESG issues, such as climate change, diversity, and board effectiveness, and the impact of ESG issues on companies' financial performance. ESG is no longer a fringe issue of interest only to special issue investors – particularly after the widespread impacts of the covid-19 pandemic and the racial and social justice movements in 2020. Mainstream institutional investors are recognising that attention to ESG and corporate social responsibility affects portfolio company financial performance. The rising interest in ESG among investors is apparent in the sharp rise in US-domiciled assets under management using ESG strategies, increasing submissions of shareholder proposals relating to ESG issues, as well as in the focus of engagement efforts.

The 2022 proxy season saw unprecedented numbers of environmental & social (E&S) shareholder proposals submitted – 564 were filed in 2022 compared to 467 filed in 2021. 33 E&S shareholder proposals received majority support in 2022, a decrease from a record 39 in 2021. The most prevalent types of E&S proposals called for setting and publishing targets for reducing greenhouse gas emissions or conducting independent racial equity and civil rights audits. While the number of E&S shareholder proposals spiked in 2022, average support dropped compared to 2021. Companies are more willing than in the past to negotiate withdrawals with proponents. In the 2022 proxy season, some of the more prescriptive proposals that were not withdrawn and went to a vote received lower support from institutional investors like BlackRock.

There was a decrease in the number of governance-related shareholder proposals submitted and voted on in 2022 – 307 were filed in 2022 compared to 374 filed in 2021. Thirty-five governance-related shareholder proposals received majority support in 2022, down from 54 in 2021. A high concentration of the governance proposals called for companies to enhance shareholders' rights to call special meetings.

Governance-related shareholder proposals were the most prevalent category of proposals submitted in 2021. They primarily addressed the following topics: the right to act by written consent, independent chairs and the right to call special meetings. 38 governance proposals passed, most of which related to majority voting (16 proposals) and shareholder action by written consent (9 proposals).

In July 2022, the SEC proposed rule amendments that would update three of the substantive bases for exclusion of shareholder proposals: the 'substantial implementation' exclusion in Rule 14a-8(i)(10), the 'duplication' exclusion in Rule 14a-8(i)(11), and the 'resubmission' exclusion in Rule 14a-8(i)(12). The proposed amendments would provide the following:

- A proposal may be excluded as substantially implemented if 'the company has already implemented the essential elements of the proposal.'
- A proposal 'substantially duplicates' another proposal if it 'addresses the same subject matter and seeks the same objective by the same means.'
- A proposal constitutes a resubmission if it 'substantially duplicates' a prior proposal, using the same test proposed in the previous bullet.

The proposed amendments represent a continuation of the SEC's efforts to streamline the no-action review process and provide market participants with clear, objective, and specific frameworks for evaluating whether or not a shareholder proposal is excludable under Rule 14a-8.

The most common shareholder proposals filed so far in the 2023 proxy season call for an independent chair, setting and publishing targets for reducing greenhouse gas emissions and requiring shareholder approval for severance pay arrangements.

Boards are facing mounting pressure from investors to integrate ESG considerations into corporate strategies and operations and to disclose information relating to ESG matters. Activists are increasingly bringing ESG-related campaigns seeking changes to board composition or strategic direction at target companies that they argue will

increase the stock price. ESG themes can be the main focus of an activism campaign, supplement activist investors' traditional requests (such as M&A, share repurchases, dividends and director seats), or both.

In November 2021, the SEC adopted changes to the federal proxy rules to require the use of 'universal' proxy cards. The new rules change the methods by which public companies and shareholders have solicited proxies for decades, and allow shareholders to vote for a mix of management and dissident nominees in a contested director election. The new rules will reshape the process by which hostile bidders, activist hedge funds, social and environmental activists, and other dissident shareholders may utilise director elections to influence control and policy at public companies. The new rules also amend certain form of proxy and disclosure requirements relating to voting options and standards that apply to all director elections, whether or not contested. The rules are now effective for shareholder meetings held after 31 August 2022.

In August 2022, ISS issued a special situations research note on the new, mandatory universal proxy card rules instituted by the SEC. In its note, ISS declared the new rules the 'superior' way for shareholders to exercise their voting franchise and observed that this system will make it 'dramatically easier' and 'cheap' for activist shareholders to launch proxy fights. ISS also offered perspectives on how the new system could help activists in their campaigns. Public companies should pay close attention to these perspectives in light of the weighty influence of ISS's proxy voting recommendations on the outcomes of contested director elections. The most notable of ISS's perspectives are that under the new framework, directors' individual qualifications may come into greater focus relative to the merits of an overall slate and that a board's 'weakest' members may now become more vulnerable in a proxy contest.

This 2023 proxy season is shaping up to be an uncommon tempest for companies and shareholders alike: macro-economic conditions are stressing corporate performance, trading multiples are depressed, and — last, but not least — the universal proxy card regime has finally come into effect.

Universal proxy cards dramatically alter how shareholders vote for directors at contested shareholder meetings. Whether they will cause companies, dissidents, proxy advisers, and shareholders to change their behavior in proxy contests has been hotly debated by market participants and observers since even before the universal proxy card rule was originally proposed by the SEC in 2016. Now that universal proxy cards are mandatory for all contested director elections, these predictions are starting to give way to preliminary observations.

Here are some initial key observations as to how the mandated use of the universal proxy card has changed the tactical and legal considerations of a proxy contest so far in the 2023 proxy season:

- Success in a proxy contest has not been guaranteed by having a slate composed of highly qualified candidates, nor by having a compelling argument that is disconnected from the composition of the slate.
- Dissidents are seeking to exploit the change to candidate-based voting in the universal proxy card to warp settlement negotiations in their favor, leading certain activists to take aggressive settlement positions.
- Taking advantage of the elimination of the 'short slate' rule in the universal proxy card rules, some activists are more frequently nominating larger and 'control' slates to achieve favorable leverage in negotiating settlements.
- Because only validly nominated candidates must be included on a universal proxy card, advance notice provisions are even more important for companies to obtain relevant information about dissidents and their candidates and ensure that dissidents comply with the requirements of the new rules.
- Special interest and other non-traditional activists may seek to leverage the universal proxy card to make nominations and launch proxy campaigns with non-traditional objectives, but despite expressed interest these activists have not yet successfully taken advantage of this possibility in large numbers.

We expect the dynamics of proxy campaigns to remain in flux for several years as activists, companies, and other market participants continue to assess and respond to the impact of the new universal proxy card regime.

Law stated - 12 May 2023

Jurisdictions

Australia	Kalus Kenny Intelex
Brazil	Loeser e Hadad Advogados
China	BUREN NV
France	Aramis Law Firm
Germany	POELLATH
India	Chadha & Co
Japan	Anderson Mōri & Tomotsune
Kenya	Robson Harris Advocates LLP
Malta	GVZH Advocates
Mexico	Chevez Ruiz Zamarripa
Netherlands	BUREN NV
Nigeria	Streamsowers & Köhn
South Korea	Lee & Ko
Switzerland	BianchiSchwald LLC
Thailand	Chandler MHM Limited
Turkey	Gün + Partners
USA	Sidley Austin LLP