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United States
Corporate Governance

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This country-specific Q&A provides an overview of corporate governance laws and regulations applicable in United States.

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United States: Corporate Governance

1. What are the most common types of corporate business entity and what are the main structural differences between them?

The most common types of business organizations in the United States are corporations, limited liability companies ("LLCs") and general or limited partnerships. Two of the more substantive differences between corporations, on the one hand, and general and limited partnerships, on the other hand, relate to tax treatment and governance. Partnerships are generally taxed on a "pass-through" basis, with no entity level tax, unlike corporations, which are generally taxed at the level of the corporation. With respect to governance, corporations are managed by a board of directors, to which the management of the corporation reports, whereas a partnership is managed by its general partner. Limited liability companies combine the features of corporations and partnerships, with limited liability to its members and the choice to be managed either by a board or by the members directly, and the availability of an election to be taxed on a "pass-through" basis, like a partnership.

These various types of legal entity exist under U.S. state, as opposed to federal, law, with Delaware being the most popular jurisdiction of incorporation or formation.

2. What are the current key topical legal issues, developments, trends and challenges in corporate governance in this jurisdiction?

The corporate governance dialog in the United States among companies, investors and other market participants remains robust, and a topic that occupies significant attention in the boardroom of U.S. public companies. Many "best practices" long advocated by shareholder groups—including say-on-pay, the dismantling of shareholder defenses, majority voting in director elections and the declassification of boards—have been codified in rules and regulations or voluntarily adopted by a majority of S&P 500 companies. Boards of directors are responsible for overseeing and guiding the strategy of a company. The global business climate is currently characterized by rapidly changing business conditions, and significant "known unknowns." For example, the past two years have seen a dramatic increase in AI applications, with many U.S. companies adopting AI in some form, which has had cascading effects on adjacent industries such as energy, semiconductors and data centers. The regulatory climate also remains in a state of flux, with increased judicial and executive branch scrutiny of federal regulations and a potentially more volatile geopolitical environment. With this backdrop of significant uncertainty, the oversight function of the board is more important than ever.

U.S. public companies are also influenced by institutional investors—especially the largest index funds—which yield significant influence and voting power and have increasingly sought to assert their views on a wide array of corporate governance issues.

A key corporate governance trend throughout 2024 was the continued shift of focus away from "ESG", in the wake of cultural and political clashes over its meaning and purpose. "Anti-ESG" legislation adopted by several states has created legal and financial hurdles, and institutional investors have backed away from the term amid public criticism and congressional subpoenas. Boards are increasingly tasked with helping companies navigate these politically charged and polarizing issues and must consider if, when and how their companies should engage on divisive topics, taking into account shifting stakeholder sentiments and potential risks to reputational capital.

3. Who are the key persons involved in the management of each type of entity?

A corporation is managed by its board of directors, natural persons who are elected by the shareholders of the corporation. The board of directors appoints officers to manage the day-to-day affairs of the corporation. A partnership is managed by its general partner, who may be a natural person or an entity. In a limited partnership, which is composed of limited partners and at least one general partner, the limited partners generally may not be involved in the day-to-day management of the limited partnership, at the risk of forfeiting limited liability. An LLC may elect to be managed by a board of managers (similar to a board of directors), who will often hire officers to oversee day-to-day affairs, or to have the LLC be managed by one or more of its members. Under the laws of most U.S. states, LLCs are managed by the members unless they select otherwise in the governing documents of the company.

4. How are responsibility and management power divided between the entity's management and its economic owners? How are decisions or approvals of the owners made or given (e.g. at a meeting or in writing)?

While specific decisions are a matter of state law, day-to-day management decisions are generally made by officers of the applicable entity, while strategic direction and the approval of extraordinary actions, such as the approval of the sale of the entity or a merger, generally require the approval of the board and, in some cases, the approval of the entity's owners.

The laws of most U.S. states provide that any action that requires approval of the equity holders can be obtained by a written consent, rather than calling and holding a meeting of the equity holders, unless otherwise set forth in governing documents. For entities whose securities are publicly traded, and thus registered under the United States Securities Exchange Act of 1934, as amended (the "Exchange Act"), the United States Securities and Exchange Commission (the "SEC") has established detailed rules focused on ensuring adequate disclosure to a company's equity holders, which may impact the ability to quickly obtain consent in writing to a decision.

5. What are the principal sources of corporate governance requirements and practices? Are entities required to comply with a specific code of corporate governance?

The main sources of substantive corporate governance rules are the laws of the state in which the entity is formed, stock exchange listing requirements and, to a lesser extent, regulation by the SEC. Within these parameters, a company has reasonable flexibility in implementing a corporate governance framework and memorializing that framework in its organizational documents. The SEC's rules generally focus on ensuring adequate disclosure rather than compelling any particular governance practice, with audit committee independence requirements and certain requirements under the Sarbanes-Oxley Act standing out as notable exceptions.

6. How is the board or other governing body constituted? Does the entity have more than one? How is responsibility for day-to-day management or oversight allocated?

The board of directors of a corporation and the board of managers of an LLC are generally elected by the shareholders and members respectively. While many corporations (and substantially all public corporations) and LLCs establish board committees to advise and assist the full board, there is not generally more than one board of directors. The board of directors serves as both a monitor and a partner of the management team that runs the day-to-day affairs of the company. To be effective, a board must find the right balance between its monitoring and advising functions, and between engaging in a "hands-on" approach to oversight and giving management the latitude necessary to operate the business.

7. How are the members of the board appointed and removed? What influence do the entity's owners have over this?

Generally, the directors of most U.S. public companies are elected annually, at the company's annual meeting of shareholders. The board of directors of some U.S. public companies are divided into classes, with directors of each class elected to staggered three-year terms, referred to as a classified board structure. The prevalence of classified boards among U.S. public companies has diminished greatly in the past 15 years, and classified boards now represent a relatively small minority of U.S. public companies. The election of directors is generally prescribed by the governing documents of the applicable entity.

8. Who typically serves on the board? Are there requirements that govern board composition or impose qualifications for board members regarding independence, diversity, tenure or succession?

Companies seek directors with the right mix of business experience, financial expertise, integrity, commitment, judgment, competence and professionalism, as well as diversity of perspectives and backgrounds, among other qualities. The most important factors in determining the effectiveness of a board are the quality of the people who serve as directors and their ability to work together.

There are a number of substantive requirements imposed by the SEC and the U.S. securities exchanges. For example, the NYSE and Nasdaq generally require listed companies to maintain independence requirements, subject to specified exceptions. The NYSE and Nasdaq also have committee-level requirements, including that all members of the audit committee be financially literate and independent in accordance with SEC standards.

There are additional rules for independent oversight of executive compensation and the director nomination process. A company's corporate governance guidelines may (but are not required to) address other substantive qualification requirements, including limitations on the number of boards on which a director may sit and director tenure, retirement and succession standards.

9. What is the role of the board with respect to setting and changing strategy?

The board of directors is the corporate body primarily responsible for setting and changing the strategy of a corporation. The board undertakes this function with input from the management of the company, and may (and often does) seek the input of outside advisors, including financial and legal advisors and consultants. Ultimately, the board has the final word on the company's strategic direction.

10. How are members of the board compensated? Is their remuneration regulated in any way?

Director compensation at U.S. public companies generally consists of a mix of cash and equity payments, in an effort to align directors' incentives with those of the company. The share of stock-based compensation has increased in recent years. Average director compensation has nearly doubled in the past decade, and the average total director compensation is now in excess of $300,000 annually. While directors are not employees and compensation is not their primary motivation for serving, offering appropriate and competitive compensation is an important factor in attracting high quality directors. The SEC requires meaningful annual disclosures with respect to director compensation practices, but companies have broad latitude to set director compensation as they see fit.

11. Do members of the board owe any fiduciary or special duties and, if so, to whom? What are the potential consequences of breaching any such duties?

The fiduciary duties of directors are governed by the law of the state in which the applicable entity is organized. Generally, most state laws provide that directors owe a duty of care and a duty of loyalty. The essence of a director's duty of care is the obligation to exercise informed business judgment. The duty of loyalty requires a director to consider the interests of the company and its shareholders rather than his or her personal interests, or the interests of other persons or entities. Directors may be held liable for breaches of fiduciary duties, although actual personal liability for directors is rare.

12. Are indemnities and/or insurance permitted to cover board members' potential personal liability? If permitted, are such protections typical or rare?

Yes, the laws of most U.S. states permit a corporation to limit or eliminate altogether the liability of directors for monetary damages for breaches of fiduciary duty, other than liability for (1) breaches of the duty of loyalty, (2) acts or omissions not in good faith or that involve intentional misconduct or a knowing violation of law, (3) the unlawful payment of a dividend or unlawful stock purchase or redemption by the company and (4) any transaction from which the director derived an improper personal benefit. Most public companies also obtain directors' and officers' insurance, to insure both the company and its directors with respect to potential liabilities. These protections are commonplace among U.S. public companies.

13. How (and by whom) are board members typically overseen and evaluated?

Boards of NYSE-listed companies are required to conduct annual performance evaluations of the board itself and board committees, and the nominating and corporate governance committee must be tasked with "oversee[ing] the evaluation of the board and management." While not required by Nasdaq, the annual board evaluation is now a nearly universal practice, with 98% of companies engaging in some form of annual board evaluation/assessment process.

14. Is the board required to engage actively with the entity's economic owners? If so, how does it do this and report on its actions?

In addition to annual meetings (discussed below), there are increasing expectations that U.S. public companies, including sometimes members of the board, engage with the company's shareholders with respect to significant corporate governance matters, extraordinary transactions and other matters of significance to the corporation. Companies are increasingly using their public filings as an opportunity to highlight their engagement with shareholders. The percentage of Fortune 100 companies disclosing these engagement efforts in their proxy statements is in excess of 90%. Effective shareholder engagement is particularly important when a company finds itself under attack from activist investors or facing a hostile takeover bid or other corporate crisis.

15. Are dual-class and multi-class capital structures permitted? If so, how common are they?

Dual- and multi-class capital structures are generally permitted by state law and the rules of the principal U.S. stock exchanges. They have, in fact, become more common in the past 20 years, driven in part by initial public offerings of technology companies, with founders using high-vote stock to maintain control even after becoming publicly listed. Since 2015, 10% of all companies that have completed their IPO had dual-class stock.

Dual-class structures are viewed negatively by many in the corporate governance community, and may face other restrictions (including, among other things, inclusion in certain indexes). Advice should be sought before implementing a dual-class voting structure.

16. What financial and non-financial information must an entity disclose to the public? How does it do this?

U.S. public companies must disclose quarterly and annual reports, including unaudited financial information on a quarterly basis and audited financial information on an annual basis. In addition, the SEC requires the filing of current reports on Form 8-K with respect to specified corporate events. Additionally, the SEC and stock exchange listing rules mandate the disclosure of other non-financial information, including matters related to corporate governance, executive compensation and other matters. Some of this information must be included in a corporation's proxy statement. All of this information is generally made publicly available on the SEC's EDGAR filing system.

17. Can an entity's economic owners propose matters for a vote or call a special meeting? If so, what is the procedure?

Yes, there are mechanisms for a U.S. public company's shareholders to propose matters for a vote at the company's annual meeting, and also to have those matters included in the company's annual proxy statement. The process for doing so is regulated by the company's organizational documents and the rules and regulations of the SEC.

In addition, many U.S. companies have adopted rights to allow shareholders to call a special meeting, or to act by written consent, in between annual meetings. The specific limitations around these rights, often including share ownership thresholds, are specified in the company's organizational documents. Companies have broad discretion in setting these limitations, which can range from restrictive to highly permissive. The prevailing trend in U.S. public company governance has been towards more permissive shareholder rights to call special meetings and to act by written consent.

18. What rights do investors have to take enforcement action against an entity and/or the members of its board?

Shareholder litigation in the U.S. public company context is relatively common compared to most non-U.S. jurisdictions. Common forms of litigation against the company and its board include: (1) derivative lawsuits (brought by shareholders of a company on behalf of the corporation); (2) actions asserting breaches of fiduciary duty; (3) actions arising pursuant to any provision of the corporate statute of the state of jurisdiction; and (4) actions asserting claims governed by the internal affairs of the corporation. U.S. public companies may also be the subject of disclosure-based claims, brought under U.S. federal securities laws and related state laws.

19. Is shareholder activism common? If so, what are the recent trends? How can shareholders exert influence on a corporate entity's management?

Shareholder activism is common in the United States and, indeed, the development of shareholder activism has largely taken place in the U.S. public company context. Global activist activity reached new highs in 2024, driven by record-setting campaign volume in Q1 and Q2. In the United States, no public company is immune from activist pressure, with household names such as Walt Disney Co., Starbucks, Southwest Airlines, Texas Instruments, Norfolk Southern and others subject to pressure and attack from activist investors during 2024. In the United States, there were 123 major activist campaigns undertaken in 2024 (compared to 114 in 2023).

Activist pressure can be asserted privately (non-public engagement with the board and management), publicly through disclosures and shareholder communications (*e.g.*, white papers, fight decks, etc.), direct communication with shareholders and, in more extreme situations, proxy fights in which the activist seeks to replace corporate directors with individuals more supportive of the activists position.

20. Are shareholder meetings required to be held annually, or at any other specified time? What information needs to be presented at a shareholder meeting?

The requirement to hold an annual meeting of shareholders, and the timing and information requirements in connection with that meeting, are generally governed by the law of the state in which the company is formed and, for listed companies, proxy disclosure requirements imposed by the rules and regulations of the SEC. Most U.S. states require that a meeting of shareholders be held annually, with the ability of the company to delay the meeting in some circumstances. Under the rules applicable to the solicitation of proxies, companies are required to make disclosures with respect to the nominees for election as director, executive and director compensation matters, corporate governance practices and with respect to other proposals to be voted on at the meeting of shareholders.

21. Are there any organisations that provide voting recommendations, or otherwise advise or influence investors on whether and how to vote (whether generally in the market or with respect to a particular entity)?

In the United States, proxy advisory services provide voting recommendations on topics including director elections, say-on-pay, shareholder proposals and mergers. In addition to providing company-specific voting recommendations, proxy advisory services publish voting guidelines setting forth their policies on various issues. The two largest proxy advisory firms are ISS and Glass Lewis, which together control nearly the entire proxy advisory market in the United States. Both ISS and Glass Lewis are privately owned for-profit enterprises.

In the last 15 years, the influence of proxy advisory firms increased substantially, and their recommendations have become a powerful (and often decisive) force in influencing corporate governance and voting results.

22. What role do other stakeholders, including debt-holders, employees and other workers, suppliers, customers, regulators, the government and communities typically play in the corporate governance of a corporate entity?

Although considerations with respect to non-equity stakeholders can be—and increasingly are—influential with respect to decision-making at the boards of U.S. public companies, formal governance arrangements are generally focused on equity holders in the United States. Unlike certain non-U.S. jurisdictions, debtholders, employees and workers, regulators and other constituencies are rarely represented directly on the boards of U.S. public companies.

23. How are the interests of non-shareholder stakeholders factored into the decisions of the governing body of a corporate entity?

As discussed above, generally, the directors of a corporation owe two duties to the corporation and its shareholders: the duty of care and the duty of loyalty. Certain states have adopted so-called "expanded constituency statutes," which expressly permit directors to take into account the interests of stakeholders other than shareholders, including employees, customers, suppliers and communities, when taking certain corporate actions. Delaware, the most influential jurisdiction in U.S. corporate law, does not have an expanded constituency statute. Although directors of Delaware corporations must generally ground their decisions in the interests of the corporation and its shareholders, directors can and should consider the interests of other stakeholders in evaluating the best interests of the corporation and its shareholders.

24. What consideration is typically given to ESG issues by corporate entities? What are the key legal obligations with respect to ESG matters?

Beginning several years ago, many corporations in the United States began to focus more on ESG issues, spurred by the growing focus by large institutional investors on these issues. Many corporations began releasing annual "Corporate Sustainability Reports" that highlight a commitment to sustainability, diversity and good governance, and have woven disclosure regarding these matters into their public filings and investor materials.

Over the past two years, the term "ESG" has steadily faded from the investor and corporate lexicon in the

United States, in the wake of cultural and political clashes over its meaning and purpose. "Anti-ESG" legislation has been adopted by several states, creating legal and financial hurdles for companies. Institutional investors have backed away from ESG amid public criticism and congressional subpoenas (for example, BlackRock has publicly disavowed the term for having become too politicized), and companies have significantly cut back on discussion of ESG-related topics during earnings calls.

Many of the risks and opportunities that were previously lumped together under the ESG umbrella remain important to both businesses and investors and will need to be unbundled, assessed and addressed. The recent conflicts and confusion over ESG suggest that the term may have outlived its usefulness. The need to address the environmental, social and governance issues that may materially impact long-term performance and value creation, however, remains as relevant as ever. The onus remains on boards and management to continue to develop strategies that promote superior performance and long-term value creation and to ensure the public markets appreciate these efforts.

25. What stewardship, disclosure and other responsibilities do investors have with regard to the corporate governance of an entity in which they are invested or their level of investment or interest in the entity?

Practically, most institutional investors must report their ownership stakes in public companies at least quarterly, with such reports being due no later than 45 days after the end of the fiscal quarter. Additionally, investors must make a public filing after acquiring beneficial ownership of 5% or more in a company subject to SEC reporting requirements. If the investor is an "active" investor who intends to either influence management or pursue other objectives *(e.g.*, an acquisition of the subject company), the investor must disclose such intentions in a public filing, due no later than five business days after crossing the 5% beneficial ownership threshold.

Additionally, in the last few years, the largest institutional money managers have invested significantly in building out their own corporate governance teams, enabling them to make their own voting decisions with respect to companies in which they are invested.

26. What are the current perspectives in this jurisdiction regarding short-term investment objectives in contrast with the promotion of sustainable longer-term value creation?

The corporate governance landscape in the United States has long been dominated by the "shareholder primacy" model, famously elucidated by Milton Friedman, according to which the sole purpose of a corporation is to create value for the shareholders. More recently, however, academics, corporations and institutional investors have begun to push for a more sustainable model, in which the purpose of a corporation is to create long-term, sustainable value for shareholders and other stakeholders, including employees and the communities in which companies operate. The Business Roundtable's August 2019 statement on the purpose of the corporation, which explicitly rejects a shareholder primacy model, is an example of the move towards long-term thinking that is currently ongoing in the United States.

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