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CORPORATE LAW PROJECT

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More information about the Corporate Law Project is available at:

<http://www.business-humanrights.org/SpecialRepPortal/Home/CorporateLawTools>.

A NOTE FROM THE UN SPECIAL REPRESENTATIVE ON BUSINESS AND HUMAN RIGHTS
September 2010

This survey is an independent submission to a project on corporate law and human rights under my mandate as Special Representative of the UN Secretary-General on Business and Human Rights: the “Corporate Law Project”. I am delighted that nineteen leading corporate law firms from around the world have agreed to make submissions to this project, and thank them for their engagement. The willingness of so many firms to provide their services pro bono in order to expand the common knowledge base indicates that corporate law firms worldwide appreciate that human rights are relevant to their clients’ needs.

It is important at the outset to understand how this project fits into my wider work. I was appointed in 2005 by then UN Secretary-General Kofi Annan with a broad mandate to identify and clarify standards of corporate responsibility and accountability regarding human rights, including the role of states. In June 2008, after extensive global consultation with business, governments and civil society, I proposed a policy framework for managing business and human rights challenges to the United Nations Human Rights Council (Council). The Framework of “Protect, Respect and Remedy” rests on three differentiated yet complementary pillars: the **state duty to protect** against human rights abuses by third parties, including business, through appropriate policies, regulation, and adjudication; the **corporate responsibility to respect human rights**, which in essence means to act with due diligence to avoid infringing on the rights of others; and **greater access for victims to effective remedy**, judicial and non-judicial. You can read more about the Framework in my 2008, 2009 and 2010 reports to the Council, available at my website: <http://www.business-humanrights.org/SpecialRepPortal/Home>.

The Council unanimously welcomed what is now commonly referred to as the U.N. Framework and extended my mandate by another three years, tasking me with “operationalizing” the Framework—that is, to provide “practical recommendations” and “concrete guidance” to states, businesses and others on the Framework’s implementation. There has already been considerable uptake of the U.N. Framework by all relevant stakeholders. It has also enjoyed unanimous backing in the Council; strong endorsements by international business associations and individual companies; and positive statements from civil society.

A key aspect of the first pillar, the **state duty to protect**, is that states should foster corporate cultures respectful of rights both at home and abroad, through all appropriate avenues. In particular, I have been exploring the opportunities and challenges that corporate and securities law can provide in this regard. Corporate law directly shapes what companies do and how they do it. Yet its implications for human rights remain poorly understood. The two have often been viewed as distinct legal and policy spheres, populated by different communities of practice.

The Corporate Law Project will allow me to explore this area further by gaining knowledge from over 40 jurisdictions as to how national laws and policies dealing with incorporation and listing; directors’ duties; reporting; stakeholder engagement; and corporate governance more generally currently require, facilitate or discourage companies from respecting human rights. I am interested not only in what laws currently exist, but also how corporate regulators and courts

apply the law to require or facilitate consideration by companies of their human rights impacts and preventative or remedial action where appropriate.

The project thus formally comprises part of my work on the **state duty to protect**. It will assist me to understand whether and how national corporate law principles and practices currently encourage companies to foster corporate cultures respectful of human rights. I will in turn consider what, if any, policy recommendations to make to states in this area, following consultation with all relevant stakeholders. However it is just one element of my work on the state duty to protect, which also looks at other areas of the law and national policies which might help states to encourage companies to respect human rights.

The project will also support my work on the corporate responsibility to respect and access to effective remedy. In relation to the responsibility to respect, I have explained that in addition to compliance with national laws, the baseline responsibility of companies is to respect human rights. To discharge the responsibility, I have recommended that companies conduct ongoing human rights due diligence whereby they become aware of, prevent, and mitigate adverse human rights impacts. The responsibility exists even where national laws are absent or not enforced because respecting rights is the very foundation of a company's social license to operate. It is recognized as such by virtually every voluntary business initiative, including the UN Global Compact, and soft law instruments such as the International Labour Organization Tripartite Declaration and the OECD Guidelines on Multinational Enterprises. Nevertheless, an understanding of national laws, including corporate law, remains vital to ensure companies understand and comply with their national legal obligations. Moreover, as my 2010 report to the Council highlights, companies may face non-compliance with corporate and securities laws where they fail to adequately assess and aggregate stakeholder-related risks, including human rights risks, and may thus be less likely to effectively disclose and mitigate them, as may be required.

The Corporate Law Project's website is <http://www.business-humanrights.org/SpecialRepPortal/Home/CorporateLawTools>. There you will find the original press release for this project; the research template the firms have agreed to follow; summary reports from two consultations held to date on the project; an over-arching trends paper bringing together the main themes from the firms' surveys; and all completed firm surveys.

My thanks again to all stakeholders who have contributed to this project.



John G. Ruggie
Special Representative of the UN Secretary-General on Business and Human Rights

United States: Executive Summary

The Constitution of the United States, including the Bill of Rights and other Amendments, provides the fundamental framework for the protection of human rights in the U.S., by addressing individual rights and civil liberties that are protected from encroachment by the government. A central role of federal and state government is to enact laws and promulgate regulations that further protect individuals. A wide variety of laws and regulations at both federal and state levels protect and otherwise relate to human rights.

Corporations are established under state law (with rare exceptions) and are granted legal status as persons to facilitate the efficient production of goods and services for the general benefit of society. Corporations must abide by federal and state law and regulation and are held liable for their actions. The laws and regulations that relate to human rights generally apply to corporations as they apply to other persons. Violations of law can result in civil or criminal liability for the corporation and, in certain instances, key decision-makers of the corporation, as well as damage the company's reputation.

The U.S. legal system has its roots in common law, except for the state of Louisiana, which has a civil law tradition. Corporate law matters are regulated at the state level, while securities law matters are regulated at both the state and federal levels. (At the state level, this report focuses on the corporate laws of Delaware, New York and states that have adopted the Model Business Corporation Act, which has been either fully or substantially adopted by 29 states.)

At the federal level, corporations with publicly traded securities are regulated by the Securities and Exchange Commission, which is an independent agency of the U.S. government that was established for the purpose of maintaining fair and orderly markets and protecting investors. The SEC is responsible for, among other things, enforcing and interpreting federal securities laws, regulatory rule-making, overseeing the activities of brokers, investment advisers and rating agencies, overseeing the stock exchanges and private regulatory organizations in the securities, accounting and auditing fields, and coordinating U.S. securities regulation with federal, state and foreign regulators.

The New York Stock Exchange and the Nasdaq Stock Market are the primary stock exchanges in the United States upon which companies list, and they impose certain requirements on listed companies as a condition for listing (with their rules subject to SEC approval); there are also several regional stock exchanges.

Corporations (with rare exceptions) are incorporated pursuant to the corporate law of a particular state. They are granted legal status separate from their shareholders, who have limited liability for corporate actions. The corporate form developed and is recognized in law because it is a means of facilitating the accumulation of capital so that it can be put to use for the production of goods and services, which is of general benefit to society. Apart from abiding by laws and regulations, corporations owe no specific duty to society. However, they are permitted to use corporate resources for public welfare, humanitarian, educational or philanthropic purposes where consistent with the interests of the company and its shareholders. They are also encouraged by a variety of forces to act ethically and in socially and environmentally responsible ways above the

requirements of law and regulation. It is common for corporations in the U.S. to engage in such activities because, in part due to reputational interests, it is often good business to do so.

Generally, state law provides that the corporation is managed by or under the direction of the board of directors. It is common practice for the board of directors to delegate the day to day management of the corporation to professional managers. Corporate directors are generally required to exercise ordinary care and prudence in the conduct of corporate affairs (the “duty of care”) and act in good faith in the best interests of the corporation and its shareholders (the “duty of loyalty”). Corporate managers have similar duties. Certain states have enacted “other constituency” statutes which expressly allow directors to consider the effect of a particular board decision on other non-shareholder constituencies, including employees, creditors, the community and the broader society.

Directors are required to provide oversight of management’s performance of delegated duties. This includes oversight of risk management, legal and ethical compliance and other areas that could potentially impact human rights. Oversight of risk management and compliance necessitates periodic review by the board of corporate processes designed to prevent and detect violations of law or undue risk taking, which may include human rights abuses. A component of such processes is an effective compliance and ethics program (which not only helps communicate the desired behavior and establish a culture of ethics and compliance but also helps to minimize potential corporate liability under the U.S. Federal Sentencing Guidelines), including a code of conduct and ethics (which a company is required to have on certain minimal terms by NYSE and Nasdaq listing standards).

Public companies are required to comply with a wide range of disclosure obligations under the federal securities laws, including a requirement to inform investors of all material information, including material foreseeable risks. For example, a public company will need to disclose if the potential for a human rights violation or other third party impact such as environmental damage, or the reputational or legal consequences from an alleged violation, poses a material risk to the operations of the company. Some companies choose to disclose information relating to their compliance with human rights practices even where such information is not material. Such disclosure may be made in response to shareholder proposals or other requests for such information, or on the company’s own initiative.

State laws do not generally impose specific requirements for board composition, although directors must be natural persons and may be subject to minimum age requirements in some states (e.g., 18 years in New York). However, state laws generally permit corporations to address qualification requirements for directors, such as a requirement to own shares; such requirements could be set forth in a corporation’s charter, bylaws or other document such as corporate governance guidelines. Under federal securities laws and regulations, individuals who have been found to violate certain provisions may be prohibited from serving on the board of a public company. The NYSE and Nasdaq require that boards of listed companies be composed of a majority of directors who do not have material relationships (other than as a director) to the corporation or its senior management team.

Human Rights Survey: United States Corporate Law

Setting the Legal Landscape

1 Briefly explain the broader legal landscape regarding business and human rights.

Each corporation is bound by the laws and regulations of its state of incorporation, federal laws and regulations, and the laws and regulations of domestic and foreign jurisdictions in which it operates. Many of these laws and regulations relate to human rights. Violations of law can result in civil or criminal liability of the corporation and, in certain instances, of key decision-makers of the corporation, as well as damage the company's reputation.

At the broadest level, human rights are protected by the U.S. Constitution (as amended by the Bill of Rights and other Amendments and as interpreted by the U.S. Supreme Court) and by state constitutions. These documents set forth those fundamental individual rights and civil liberties such as freedom of speech, assembly and religion, freedom from slavery and involuntary servitude, the right to keep and bear arms, freedom from cruel and unusual punishment, and the right to trial by a jury of one's peers, that are protected from government action. They also include certain prohibitions of discrimination on the basis of race and gender.

A central role of federal and state government is to enact laws and promulgate regulations that further protect individuals from the actions of non-governmental persons and entities. Corporations must comply with a wide variety of laws and regulations at both federal and state levels that protect and otherwise relate to human rights, including all of the rights enunciated in the United Nations Global Compact. Some of the federal statutes that relate to human rights include the Civil Rights Act (prohibiting discrimination on the basis of race, color, national origin, sex or religion), the Americans with Disabilities Act (prohibiting discrimination against people with disabilities in employment, transportation, public accommodation, communications and governmental activities), the Fair Labor Standards Act (establishing a minimum wage and prohibiting the employment and abuse of child workers), the Equal Pay Act (requiring that men and women in the same workplace be given equal pay for equal work), the Occupational Safety and Health Act (ensuring workers a place of employment free from recognized hazards to safety and health), the Family and Medical Leave Act (providing certain employees with job-protected leave to balance work and family responsibilities), the Labor-Management Relations Act (prohibiting unfair labor practices, permitting collective bargaining and regulating industrial action), the Alien Tort Claims Act (permitting U.S. courts to hear cases brought by foreign citizens for tortious conduct committed outside the U.S., which may include human rights violations), and a host of legislation pertaining to equal opportunity laws as administered by the Equal Employment Opportunity Commission and to the environment as administered by the Environmental Protection Agency. In general, in the U.S. the protection of human rights is viewed as a governmental responsibility in the first instance and is carried out through the laws and regulations – and enforcement – that government provides. Many states also have statutes that address requirements in these areas, but these are not discussed herein.

Corporations are subject to a well-developed common law and statutory system relating

to their internal governance, tort claims and property rights. Corporations must abide by federal and state law and regulation and are held liable for their actions. The laws and regulations that relate to human rights generally apply to corporations as they apply to other persons. Violations of law can result in civil or criminal liability for the corporation and, in certain instances, key decision-makers of the corporation, as well as damage the company's reputation. Public companies are required to disclose material risks of their business operations and could be subject to shareholder proposals relating to human rights and other social issues.

In addition, corporations are encouraged to implement and monitor effective compliance programs, which under the U.S. Federal Sentencing Guidelines can mitigate corporate criminal penalties. One component of such a program is a code of conduct and ethics, which sets forth expectations of appropriate behavior that goes beyond mere compliance with the law. In addition, codes of conduct and ethics, at least on certain minimal terms, are required by the listing standards in place at the New York Stock Exchange (the "NYSE") and the Nasdaq Stock Market ("Nasdaq"). Failure of a corporation to implement an effective compliance program could potentially lead to personal civil liability of directors and officers to shareholders.

Regulatory Framework

2 To what legal tradition does the jurisdiction belong, i.e. civil/common law, mixed?

The U.S. legal system has its roots in common law. Judicial interpretation (or "case law") supplements and interprets legislatively-enacted statutes to form a binding (or at times persuasive) system of precedents. In 49 out of the 50 states in the United States, the rights and duties of officers, directors and shareholders are governed by a common law regime that supplements and interprets corporate law statutes. The State of Louisiana is the only state rooted in a civil law tradition.

This report will focus on Delaware, New York and those states that have substantially adopted the Model Business Corporation Act (the "Model Act").

Delaware corporate law, codified in the Delaware General Corporation Law (the "DGCL"), is notably flexible and is regularly updated to reflect current developments. Corporate law litigation in Delaware is handled by a specialized system of courts with highly experienced judges, which has led to Delaware having a more extensive and sophisticated corporate law jurisprudence than other states. Delaware case law often has persuasive weight in other states throughout the United States and, in some cases, internationally.

New York corporate law is codified in the New York Business Corporation Law (the "NY BCL") which, like Delaware corporate law, has been supplemented by a large body of case law interpretation.

The Model Act was developed initially in 1950 and has since been regularly updated by the American Bar Association's Corporate Laws Committee to serve as a free-standing general corporate statute that can be enacted partially or in its entirety by a state legislature. To date, 29 jurisdictions have adopted all or substantially all of the Model Act, and four jurisdictions have adopted statutes based on the 1969 edition of the Act.

3 Are corporate/securities laws regulated federally, provincially or both?

Corporate formation, director duties and shareholder rights are regulated at the state level. The issuance of securities is regulated at both the state and federal level.

At the federal level, the primary legislation governing the offering and sale of securities include the Securities Act of 1933 (the “Securities Act”) and the Securities Exchange Act of 1934 (the “Exchange Act”), each as amended and supplemented by rules and regulations promulgated by the Securities and Exchange Commission (the “SEC”). The dual objectives of the Securities Act are to require that investors receive material information concerning securities being offered for sale and to prohibit deceit, manipulation and fraud in the sale of such securities. The Securities Act regulates (subject to certain exceptions) all offerings and sales of securities in the United States, whether by public or private companies. The Exchange Act (which incorporates the Foreign Corrupt Practices Act) regulates, among other things, the organization and operation of the financial marketplace, the activities of brokers, dealers and other financial market participants, accounting controls and records, bribery of foreign officials, and disclosure of information by public companies.

Each state has its own securities laws, known as “Blue Sky Laws,” which generally apply to the offer and sale of securities but not to other aspects of the securities markets. Each state has its own regulatory agency to administer these laws. These laws may have limited applicability to offerings of securities made on a national basis if, for example, the securities are listed (or approved for listing) on the NYSE or Nasdaq.

4 Who are the government corporate/securities regulators and what are their respective powers?

The primary federal securities regulator is the SEC, an independent agency of the U.S. government established to protect investors and maintain fair, orderly and efficient markets. The SEC regulates disclosures made in connection with securities offerings and by publicly-held companies, securities trading and licensing of market participants including securities exchanges, brokers and dealers, investment advisors and mutual funds. The SEC is responsible for, among other things, enforcing and interpreting federal securities laws, regulatory rule-making, overseeing the activities of brokers, investment advisers and rating agencies, overseeing the exchanges and private regulatory organizations in the securities, accounting and auditing fields, and coordinating U.S. securities regulation with federal, state and foreign regulators. The SEC is authorized to bring civil and administrative enforcement actions against individuals and companies it suspects have violated the securities laws.

In addition, each state has a Secretary of State (or equivalent) tasked with maintaining a record of the status of each corporate entity organized within its jurisdiction and providing certifications of filed records. In certain circumstances, the Secretary of State may have the authority to amend or revoke a corporate charter.

Generally, under state law, the Attorney General of a particular state provides oversight of corporations within that state and has the power to investigate and prosecute violations of corporate law by corporations incorporated or operating in that state. For instance, in Delaware, the Attorney General can file a complaint with the Court of Chancery to

revoke or forfeit a charter of any corporation for abuse, misuse or nonuse of its corporate powers, privileges or franchises. Furthermore, the Attorney General or another official has authority to enforce the state's securities law. For example, in New York the Attorney General has the power to investigate and take enforcement action against securities fraud, including to seek from a court equitable and monetary remedies, and in furtherance of an investigation can subpoena any document from anyone doing business in New York.

A variety of state and federal administrative agencies and self-regulating organizations also regulate particular industries or company activities. For example, the Financial Industry Regulatory Authority ("FINRA"), a non-governmental regulator for all securities firms in the United States, examines securities firms, writes rules, enforces its rules and the federal securities laws, informs and educates the public, provides trade reporting and other industry utilities, and administers a dispute resolution forum for investors and registered firms.

5 Does the jurisdiction have a stock exchange(s)?

There are two major national listing bodies, the NYSE and Nasdaq. Corporations must comply with applicable listing requirements as a condition of having their securities listed on either exchange. There are also several regional stock exchanges including, among others, the Chicago Stock Exchange and the Boston Stock Exchange.

Incorporation and Listing

6 Do the concepts of "limited liability" and "separate legal personality" exist?

The concepts of "separate legal personality" and "limited liability" exist in the U.S. Separate legal personality is grounded in the notion that upon incorporation, a corporation has a legal identity as a person with attendant legal rights, privileges and liabilities. However, courts may "look through" a corporation's separate legal personality (the "corporate veil") to its underlying owners if a corporation is inadequately capitalized, does not maintain corporate records, does not observe corporate formalities and does not have functioning officers and directors and if maintaining separate legal personality would be abusive.

Shareholders of a corporation have limited liability, pursuant to which their liability is limited to the amount of their investment in the company. Shareholders will not be held personally liable for the corporation's debts and other liabilities, except in certain limited circumstances where the corporation's separate legal personality may be ignored.

7 Did incorporation or listing historically, or does it today, require any recognition of a duty to society, including respect for human rights?

Corporations are granted separate legal status with limited liability to shareholders to facilitate the accumulation of capital and the efficient production of goods and services for the benefit of society. Dave Packard, co-founder of Hewlett-Packard Company explained the rationale with simple elegance in 1939, stating "a group of people get together and exist as an institution that we call a company so that they can accomplish something collectively that they could not accomplish separately – they make a contribution to society, a phrase which sounds trite but is fundamental."

Apart from abiding by laws and regulations, corporations owe no specific duty to society. However, they are permitted to use corporate resources for public welfare, humanitarian, educational or philanthropic purposes where consistent with the interests of the company and its shareholders. They are also encouraged by a variety of forces to act ethically and in socially and environmentally responsible ways above the requirements of law and regulation. It is common for corporations in the U.S. to engage in such activities because, in part due to reputational interests, it is often good business to do so.

In certain industries, corporations may be subject to regulatory requirements that include a public interest component, for example in broadcasting and certain utilities industries.

Thirty states, including New York, expressly permit directors to consider the impact of a decision on a broad range of constituents (so-called “other constituency” statutes) in determining what action is in the best interests of the corporation (see questions 11 and 12, below), although generally as fiduciaries directors may consider the interests of other constituencies in relation to the impact on the corporation’s business and reputation, whether or not they are expressly permitted to do so by statute. In addition, some states provide that the corporate articles of incorporation and/or bylaws may address corporate social responsibility. For example, the Oregon Business Corporation Act (discussed in commentary to the Model Act) expressly permits a corporation’s articles of incorporation to include a provision “authorizing or directing the corporation to conduct the business of the corporation in a manner that is environmentally and socially responsible.” While the statute does not require a corporation to consider social issues or to include reference to them in its articles of incorporation, it recognizes the legitimacy of, and encourages, Oregon corporations operating in an environmental and socially responsible manner by specifically permitting such corporations to regulate internally that they be operated in a manner that is environmentally and socially responsible. Notwithstanding that the New York and Delaware corporation statutes do not specifically address whether the charter or bylaws may include provisions relating to corporate social responsibility, there appears to be nothing to prevent a company from including such provisions.

Companies listed on the NYSE or Nasdaq are required to maintain codes of conduct and ethics for their directors, officers and employees which set forth standards of expected conduct. These codes must address certain matters such as compliance with law and typically also address other human rights matters such as employment discrimination.

8 Do any stock exchanges have a responsible investment index, and is participation voluntary? (See e.g. the Johannesburg Stock Exchange’s Socially Responsible Investment Index.)

In June 2009, Nasdaq launched the NASDAQ OMX CRD Global Sustainability 50 Index, which is “an equally weighted equity index that serves as a benchmark for stocks of companies that are taking a leadership role in sustainability performance reporting and are traded on a major U.S. stock exchange.” There are also a number of indices such as the Dow Jones Sustainability Indices and the FTSE4Good Index Series that include companies based on operations in line with certain defined socially or environmentally responsible business practices. In addition, investment funds offer various types of responsible investment portfolios, covering both NYSE and Nasdaq companies (see question 20).

Directors Duties

9 To whom are directors' duties generally owed (i.e. to the company, non-shareholders etc)?

Generally, state law provides that the corporation is managed by or under the direction of the board of directors. It is common practice for the board of directors to delegate the day to day management of the corporation to professional managers. Corporate directors are fiduciaries and owe duties of care and loyalty to the corporation and its shareholders. The duty of care generally requires directors to exercise ordinary care and prudence in the conduct of corporate affairs. The duty of loyalty generally requires directors to act in good faith in the best interests of the corporation and its shareholders and prohibits self-dealing and misappropriation of assets or opportunities by board members. The duty of loyalty further encompasses a duty of candor which requires directors to disclose any conflicts of interest. Corporate managers have similar duties.

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 harbor known as the "business judgment rule." The business judgment rule creates 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 the courts avoid second-guessing board decisions, and protects directors from liability when they act on an informed and diligent basis, and their action is 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.

According to the American Law Institute, the standard of care a director needs to meet to satisfy its duty of care in making a decision can be satisfied even where there is no economic gain to the corporation from the decision. For instance, corporate actions aimed at maintaining the confidence of business organizations with which the corporation deals, fostering the morale of employees, encouraging favorable (or forestalling unfavorable) governmental regulation, providing lawful assistance in connection with lobbying or referenda activities or voluntarily adopting a course of conduct that may otherwise be mandated are all permissible corporate goals, even though they may not directly increase corporate profits.

Under some circumstances, the duties of directors expand to include the interests of creditors. Under Delaware law, directors of an insolvent corporation continue to owe their fiduciary duties to the corporation, not directly to creditors; however creditors will have standing to assert derivative claims on behalf of the corporation, which may be asserted based on violations of the duties of directors to the corporate entity (see North American Catholic Educational Programming Foundation Inc. v. Gheewalla (Del. 2007)). New York, in contrast, adheres to the "trust fund" doctrine of director fiduciary duties to creditors (see N. Y. Credit Men's Adjustment Bureau v. Weiss (N.Y. 1953)). Under this doctrine, the assets of an insolvent corporation are treated as similar to a trust fund and

are to be managed for the benefit of the corporation's creditors. Thus, the directors have a duty to protect the assets, as if they were trustees for the benefit of the creditors, and creditors may seek redress against directors for violation of this duty.

10 Are there duties to avoid legal risk and damage to the company's reputation? If so, are they duties in their own right or are they incorporated into other duties?

As discussed above, directors are fiduciaries for the corporation and its shareholders and, as such, have a duty to manage corporate affairs in what they reasonably believe is in the best interest of the corporation and its shareholders. In fulfilling their duties as fiduciaries, directors as a general matter of corporate law must consider the broad range of risks that may impact the corporation's affairs, including risks of violation of law and harm to the corporation's reputation which can both be implicated by human rights abuses. As noted in the response to question 1 above, corporations are increasingly subject to laws and regulations that relate to human rights. Board responsibilities include overseeing management's efforts -- including the adoption and implementation of policies, processes and controls -- designed to assure that the corporation is in compliance with legal requirements and that corporate management is positioned to identify and manage or mitigate risks, including those related to human rights. Oversight of risk management and compliance necessitates periodic review by the board of corporate processes designed to prevent and detect violation of law or undue risk taking including human rights abuses. One component of such processes is an effective compliance and ethics program (which not only helps communicate the desired behavior and establish a culture of ethics and compliance but also helps to minimize potential corporate liability under the U.S. Federal Sentencing Guidelines), including a code of conduct and ethics (which a company is required to have on certain minimal terms by NYSE and Nasdaq listing standards).

11 More generally, are directors required or permitted to consider the company's impacts on non-shareholders, including human rights impacts on the individuals and communities affected by the company's operations? Is the answer the same where the impacts occur outside the jurisdiction? Can or must directors consider such impacts by subsidiaries, suppliers and other business partners, whether occurring inside or outside the jurisdiction? (See e.g. s. 172 UK Companies Act 2006)

In carrying out their fiduciary duties with respect to the management and direction of corporate affairs as discussed above, as a general matter directors are permitted to consider the corporation's impact on non-shareholders, including the human rights impacts on the individuals and communities affected by the company's operations, whether or not within the jurisdiction of incorporation. This consideration may encompass actions and associated impacts of subsidiaries, suppliers and business partners, both within and outside the jurisdiction of incorporation. Such considerations must, however, be consistent with (at the least in the sense of being not opposed to) the pursuit of the best interest of the corporation and its shareholders. The nature and degree of the consideration to be given to non-shareholder constituencies falls within the broad business judgment discretion that is accorded directors in managerial matters.

Corporations are permitted to use corporate resources for public welfare, humanitarian, educational or philanthropic purposes where consistent with the interests of the company

and its shareholders. They are also encouraged by a variety of forces to act ethically and in socially and environmentally responsible ways above the requirements of law and regulation. It is common for corporations in the U.S. to engage in such activities because, in part due to reputational interests, it is often good business to do so.

The Model Act specifically permits corporations to “make donations for the public welfare or for charitable, scientific or educational purposes.” According to the American Law Institute Principles of Corporate Governance (the “ALI Principles”), which summarizes general propositions of corporate law broadly recognized in most states, provisions similar to those of the Model Act support the propriety of directors considering ethical considerations when taking corporate action, as it would be anomalous to permit donations of money for public welfare or charitable purposes while prohibiting consideration of ethical principles. In particular, Section 2.01 of the ALI Principles provides that “[e]ven if corporate profit and shareholder gain are not thereby enhanced, the corporation, in the conduct of business...may take into account ethical considerations that are reasonably regarded as appropriate to the responsible conduct of business,” while the commentary notes that “[c]orporate officials are not less morally obliged than any other citizens to take ethical considerations into account, and it would be unwise social policy to preclude them from doing so.”

Thirty states, including New York, expressly permit directors to consider the effect of board action or inaction on constituencies other than shareholders. Directors are not, however, required to subordinate the interests of shareholders to other interests. While these “other constituency” statutes emphasize that directors may consider a broad range of interests, it is generally recognized that a board of directors may do so absent such a statutory provision given the broad scope of director discretion and the link between responsible corporate citizenry, corporate reputation and business performance.

The “other constituency” statutes expressly permit directors to consider: (1) the long- and short-term interests of the corporation and its shareholders; (2) employees, customers, suppliers and creditors; (3) the community and social interests; and (4) the economy of the state and nation. Of the states that have adopted constituency statutes, 29 include consideration of factors from the first three basic categories and 14 of those also include factors from the fourth category. For example, under this framework, in Georgia-Pacific Corp. v Great Northern Nekoosa Corp. (D. Me. 1989), the Maine federal district court cited Maine’s “other constituency” statute in finding that a 120 day delay in the board’s response to a tender offer proposal was not unreasonable where, “Maine law suggests that the directors of a corporation should also consider the interests of the company’s employees, its customers and suppliers, and communities in which offices of the corporation are located.”

Delaware corporate law does not include “other constituency” provisions. Nevertheless, directors of Delaware corporations are generally considered to have the discretion to consider societal effects in formulating corporate policies and otherwise making business decisions, in determining what conduct is in the best interest of the corporation and its shareholders.

As a general matter, directors are not subject to jurisdictional constraints in considering human rights and other societal effects of proposed corporate actions. Directors have discretion to consider the impact of corporate actions, and the actions of subsidiaries,

suppliers and other business partners, both within and outside the U.S.

12 If directors are required or permitted to consider impacts on non-shareholders to what extent do they have discretion in determining how to do so?

A few of the “other constituency” statutes provide that directors *should* consider the interests of employees, creditors and other constituencies, as well as the interests of shareholders, in making certain corporate decisions or, in some cases, in making all corporate decisions, without stating the weight to be given to non-shareholder (or shareholder) interests, with the implication that directors will use their business judgment in determining the weight to give to non-shareholder interests. Other states provide that directors *may* consider the interests of non-shareholder constituents in making decisions. The New York statute (Section 717(b) of the NY BCL) states that directors are entitled to consider the effects of corporate actions on non-shareholder constituencies when making decisions: “In taking action, . . . a director shall be entitled to consider, without limitation, . . . the effects that the corporation’s actions may have in the short-term or in the long-term upon any of the following: . . .(ii) the corporation’s current employees; (iii) the corporation’s retired employees and other beneficiaries receiving or entitled to receive retirement, welfare or similar benefits from or pursuant to any plan sponsored, or agreement entered into, by the corporation; (iv) the corporation’s customers and creditors; and (v) the ability of the corporation to provide, as a going concern, goods, services, employment opportunities and employment benefits and otherwise to contribute to the communities in which it does business.” We are not aware of any constituency statute that *requires* directors to subordinate shareholder interests to the interests of other constituencies, provided that the corporation would be acting lawfully; rather, the focus is, at most, on a balancing of interests. Moreover, in a few states corporations may opt out of the application of the non-shareholder constituency statute in its entirety.

13 What are the legal consequences for failing to fulfill any duties described above; and who may take action to initiate them? What defenses are available?

Only shareholders and the board of directors on behalf of the corporation may, as a general matter, bring suit for breach by a director of his or her duties to the corporation and its shareholders. In particular, depending on the nature of the allegation, shareholders may also bring lawsuits against the directors of a corporation on behalf of the corporation for damages it has sustained (known as a “derivative suit”) or in appropriate instances for equitable relief. To institute a derivative suit in Delaware, New York and in states that have adopted the Model Act, a shareholder must first make a demand to the board of directors that the corporation initiate the proposed legal action on its own behalf. Such a demand is not required in Delaware and New York if the shareholder can show that bringing such a demand would be futile. The Model Act does not provide an exception for demand futility. The board of directors has broad discretion under the business judgment rule to determine whether or not to take up the demand and only if the demand is wrongfully refused may the shareholder proceed with a derivative lawsuit.

Directors will not be held liable for their decisions, even if such decisions cause harm to the corporation and its shareholders, if the decisions fall within the protection of the business judgment rule discussed above. If a board’s decision is challenged in a lawsuit, the court will examine whether the plaintiff has presented enough evidence to overcome the presumption that the board was disinterested (not conflicted), acting in good faith and

on an informed basis. If the presumption is not overcome, the court will not consider the merits of the underlying business decision. The deference accorded board decisions by the courts through application of the business judgment rule is designed to avoid using the benefit of hindsight to second guess (and imposing liability for) failed board decisions.

The Model Act states that a director will be liable only if it is established that there is no defense based on (1) the articles of incorporation, (2) the safe harbor relating to conflicting interests (where the conflicting interest was fair to the corporation or the director followed the procedures outlined in the Model Act which includes disclosure of the transaction and approval by a majority of the qualified directors), (3) the safe harbor relating to business opportunities (where, prior to becoming legally obligated respecting the opportunity, the director discloses all material facts concerning the business opportunity and either the qualified directors or the shareholders disclaim the corporation's interest in the opportunity) and (4) the business judgment rule. Further, if a party is seeking to hold the director liable for money damages, it will have the burden of establishing that harm to the corporation or its shareholders has been suffered and the harm suffered was proximately caused by the director's challenged conduct.

In addition to civil liability, directors can face criminal liability for certain actions under federal and state law, for example, in relation to insider trading, fraud, misrepresentation, bribery and falsification or alteration of records.

14 Are there any other directors' duties which encourage a corporate culture respectful of human rights?

Directors are required to provide oversight of management's performance of delegated duties. This includes oversight of risk management, legal and ethical compliance and other areas that could potentially impact human rights. A corporate culture that is respectful of human rights can be nurtured by an effective compliance and ethics program. Implementing an effective compliance and ethics program will also serve to mitigate corporate penalties for unlawful conduct undertaken without authorization by employees or agents under the U.S. Federal Sentencing Guidelines. One component of an effective compliance and ethics program is a robust code of conduct and ethics, building on the codes required for listing on NYSE and Nasdaq, with oversight by the board of directors. See also the response to question 10 above.

15 For all of the above, does the law provide guidance about the role of supervisory boards in cases of two tier board structures, as well as that of senior management?

In the unitary board structure that prevails in the U.S., the board of directors typically delegates responsibility to management for the day to day affairs of the corporation, and provides oversight of management's execution of business plans and strategies. This structure is usually codified in the corporation's organizational documents (e.g. certificate or articles of incorporation and bylaws) and reinforced by the customs of the particular corporation (including formal policies such as board guidelines). Both the directors and the senior management owe fiduciary duties to the corporation and should act in a way that minimizes the reputational and legal risk to the corporation. Corporate law and stock exchange listing rules limit the board's ability to delegate certain decisions (e.g. dividends, bylaw amendments and certain committee functions relating to audit,

compensation and director nominations). Corporate law statutes do not describe in significant detail required areas for board focus and activity. However, case law provides significant guidance about what is required of fiduciaries.

Reporting

16 Are companies required or permitted to disclose the impacts of their operations (including human rights impacts) on non-shareholders, as well as any action taken or intended to address those impacts, whether as part of financial reporting obligations or a separate reporting regime?

Public companies are required to comply with a wide range of disclosure obligations under the federal securities laws, including a requirement to inform investors of all material information, including material foreseeable risks. Information is “material” if there is a substantial likelihood that a reasonable shareholder would consider it significant in its deliberations on voting or buying or selling stock or, stated otherwise, whether it would be viewed by an investor as significantly altering the “total mix” of information made available. A company must make an assessment of whether or not information is material taking into account all relevant qualitative and quantitative factors. For example, a public company will need to disclose if the potential for a human rights violation or other third party impact such as environmental damage, or the reputational or legal consequences from an alleged violation, poses a material risk of liability or of disruption to the operations of the company.

Recently, certain specific disclosure obligations relating to human rights impacts have been imposed on publicly traded companies (and could under future regulations be extended to certain private companies). Section 1502 of the Dodd-Frank Wall Street Reform and Consumer Protection Act (the “Dodd-Frank Act”) provides for SEC rule-making that will require SEC reporting companies to file annual reports as to whether certain “conflict minerals” used in the functionality or production of a product manufactured by the company originated in the Democratic Republic of Congo or adjoining countries. The report, which will be publicly available, must also include a description of the measures taken to exercise due diligence as to the source and chain of custody of the minerals used for the purpose of determining whether the minerals used financed or benefited armed groups that have been identified as perpetrators of serious human rights abuses in certain U.S. government reports. The disclosure requirement is not contingent on the use of the minerals being separately determined to be material to the company’s business. A sponsor of the legislation explained that the disclosure requirement was to encourage companies to source the minerals responsibly.

Some companies choose to disclose information relating to their compliance with human rights matters even where such information is not material (and not otherwise required by law). Such disclosure may be made in response to shareholder proposals seeking information on the company’s practices or other requests for such information. In other instances the information is made available at the corporation’s own initiative. Examples of companies producing social responsibility reports include Microsoft, ExxonMobil, General Electric and Starbucks.

17 Do reporting obligations extend to such impacts or actions outside the jurisdiction; to the impacts or actions of subsidiaries, suppliers and other business partners,

whether occurring inside or outside the jurisdiction?

Disclosure is required for all material information regarding a publicly held corporation's operations and prospects, whether occurring inside or outside the United States. This disclosure requirement extends to impacts or actions of subsidiaries, suppliers and other business partners where such information is material.

18 Who must verify these reports; who can access reports; and what are the legal consequences of failing to report or misrepresentation?

Public companies file reports and registration statements with the SEC; these documents are publicly available and accessible through the SEC website. Annual reports and registration statements contain audited financial statements, while quarterly reports contain unaudited financial statements. The chief executive officer and chief financial officer are required to certify as to the accuracy of the information contained in the annual and quarterly reports, among other things. Many corporations also disclose information via press releases, the corporate website, blogs, social networking and video-sharing websites, brochures, periodicals, television, radio and other methods.

Filings are reviewed by the SEC's Division of Corporation Finance, which can issue comments and require amended filings where appropriate. If a corporation fails to timely file its required SEC reports, it can also lose certain privileges it may have under the securities laws such as the ability to access certain types of capital on an expedited basis. A corporation that fails to file timely reports may also be subject to stock exchange delisting.

The SEC has authority to sanction companies where disclosures include misrepresentations or omit required information. The SEC can seek an injunction prohibiting further acts that violate the securities laws. The SEC can also seek monetary penalties, the return of illegal profits and can bar an individual from serving as a corporate officer or director. In addition, the SEC can seek cease and desist orders, suspension or revocation of broker-dealer and investment advisor registrations, censures, bars from association with the securities industry and civil monetary penalties.

In certain situations an investor has a private right of action under federal securities laws to sue a corporation for monetary damages where the corporation misstated or omitted material facts in disclosures upon which the investor relied in making an investment decision.

Stakeholder Engagement

19 Are there any restrictions on circulating shareholder proposals which deal with impacts on non-shareholders, including human rights impacts?

State laws contain no specific restrictions or prohibitions on shareholder proposals pertaining to human rights.

Rule 14a-8 under the Exchange Act generally requires public companies to include in their annual proxy statements shareholder proposals from eligible shareholders that are significantly related to corporate operations. To be eligible, a shareholder must have

continuously held, for at least one year by the date the proposal was submitted, at least \$2,000 in market value or 1% of the corporation's securities entitled to be voted on the proposal at the meeting and must continue to hold those securities through the date of the meeting.

A corporation may exclude such a proposal if the proposal: (1) is improper under state law or would, if implemented, cause the company to violate any law to which it is subject (including the proxy rules); (2) relates to the redress of a personal claim or grievance against the corporation; (3) relates to ordinary business operations or operations which account for less than 5 percent of the corporation's total assets at the end of its most recent fiscal year, and for less than 5 percent of its net earnings and gross sales for its most recent fiscal year, and is not otherwise significantly related to the corporation's business; (4) could only be implemented by the company if it had certain powers that it lacks; (5) has been substantially implemented by the corporation, conflicts with a corporate proposal, is duplicative of another proposal or has been submitted during previous years and received low votes in favor; or (6) deals with a matter relating to the corporation's ordinary management functions. Proposals can also be excluded on technical grounds (e.g., failure to submit before the deadline, lack of ownership, etc.). The rules do not specifically permit a corporation to exclude shareholder proposals that deal with impacts on non-shareholders, including human rights impacts. Generally, proposals that are related to policy matters are considered significantly related to the corporation's business and may not be excluded. Proposals regarding the corporation's human rights practice and environmental impact generally cannot be excluded from the corporation's proxy statements by reason of their subject matter.

The number of shareholder proposals regarding the formation of committees on human rights and disclosure of human rights standards increased between 2003 and 2008 (from one proposal in 2003 to 25 proposals in 2008), but has decreased since 2008 (16 proposals in both 2009 and 2010). Levels of support are typically low (an average of 11.6% support in 2008, 17.9% in 2009 and 15.9% in 2010) and no proposals have passed, although we note that at least one proxy advisor as a matter of policy will generally recommend to shareholder clients that they vote in favor of proposals regarding disclosure of a corporation's or its suppliers' human rights standards or policies unless such information is already publicly disclosed.

20 Are institutional investors, including pension funds, required or permitted to consider such impacts in their investment decisions?

The Department of Labor issued guidelines on the legal standards imposed on fiduciaries of pension funds and other employee benefit plan trusts by sections 403 and 404 of Title I of the Employee Retirement Income Security Act, which became effective on October 17, 2008. Under these guidelines the fiduciaries of employee benefit plans, including trustees, investment managers and others responsible for the management of employee benefit plans assets may "never subordinate the economic interests of the plan to unrelated objectives, and may not select investments on the basis of any factor outside the economic interest of the plan..." However, where two or more investments are equal in economic value, fiduciaries may choose between the alternatives on the basis of a factor other than economic interest. This exception would permit fiduciaries to make a decision based on social policies in the case of economically equal alternatives. Other institutional investors may be subject to similar fiduciary considerations. Some state pension funds are

required to take certain social policy considerations into account when making investment decisions and some private endowment and other funds have a policy of doing so.

There also are no legal restrictions preventing the establishment of private investment funds dedicated to socially-conscious investments. Certain funds use this strategy as a key element of their marketing and business model. For example, Walden Asset Management evaluates the social performance of portfolio companies in the areas of products and services, environmental impact, workplace conditions, community impact and corporate governance, and advocates for change through engagement with companies and sponsorship of shareholder proposals.

21 Can non-shareholders address companies' annual general meetings?

Annual general meetings are, by definition, meetings of shareholders. Non-shareholders have no legal right to attend or address such meetings. Attendance by non-shareholders is at the invitation of the corporation only.

Other issues of corporate governance

22 Are there any other laws, policies, codes or guidelines related to corporate governance that might encourage companies to develop a corporate culture respectful of human rights, including through a human rights due diligence process?

As discussed above, corporations are required to comply with many laws and regulations which relate to human rights. Corporations are also encouraged to implement and monitor effective compliance programs (which would include a code of conduct and ethics as required by the NYSE and Nasdaq), which under the U.S. Federal Sentencing Guidelines can mitigate corporate criminal penalties. Failure of a corporation to implement an effective compliance program could potentially lead to personal civil liability of directors and officers to shareholders.

In addition, generally corporations appreciate that the negative publicity surrounding human rights violations could harm their reputation and brand image. For these and other reasons, corporations adopt policies that address acceptable behaviors and the protection of human rights. Some choose to emphasize their commitment to human rights through social responsibility reports. In addition, many corporations voluntarily participate in corporate social responsibility initiatives including, among others, the United Nations Global Compact, which promotes corporate responsibility, and the Global Network Initiative, which is aimed at protecting and advancing freedom of expression and privacy in information and communications technologies.

23 Are there any laws requiring representation of particular constituencies (i.e. employees, representatives of affected communities) on company boards?

State and federal laws do not generally have specific board composition requirements, although directors are required to be natural persons and need to meet age requirements in some states (e.g., 18 years in New York). In addition, directors of public companies must not be subject to an SEC ban on being a director. The federal Clayton Act also

restricts interlocking directorships between competitors. State laws generally permit a corporation to set qualification requirements for directors.

The NYSE and Nasdaq require that the boards of listed companies be composed of a majority of independent directors. Under NYSE Listing Company Manual Section 303A.02, “[n]o director qualifies as ‘independent’ unless the board of directors affirmatively determines that the director has no material relationship with the listed company (either directly or as a partner, shareholder or officer of an organization that has a relationship with the company).” Under Nasdaq Marketplace Rule 5605(2), “‘independent director’ means a person other than an Executive Officer or employee of the Company or any other individual having a relationship which, in the opinion of the Company’s board of directors, would interfere with the exercise of independent judgment in carrying out the responsibilities of a director.” Certain family, employment and close consulting and business relationships are presumptively or *per se* “material” under NYSE and Nasdaq listing rules, and therefore serve to disqualify a director from being considered by the board to be independent. The NYSE and Nasdaq require listed companies to have an audit committee comprised of independent directors who satisfy a heightened standard of independence and who are financially literate (including one member who must have financial expertise). The Dodd-Frank Act also requires compensation committee members of listed companies to meet heightened standards of independence; however, implementing rules have not yet been proposed at the time of writing.

SEC rules require public companies to disclose, for each director and nominee, the specific experience, qualifications, attributes or skills that led the board to conclude that the person should serve as a director of the company, in light of the company’s business and structure, as well as whether and, if so, how the nominating committee considers diversity in identifying nominees for director. If the nominating committee or the board has a policy with regard to the consideration of diversity in identifying director nominees, the SEC rules require disclosure of how this policy is implemented and how the nominating committee or the board assesses the effectiveness of its policy.

24 Are there any laws requiring gender, racial/ethnic representation; or nondiscrimination generally, on company boards?

While there are no laws requiring corporations to have certain racial/ethnic/gender representation on their boards, public companies are required to disclose whether and if so how the nominating committee (or the board) considers diversity in identifying nominees for director (see question 23). Most corporate boards recognize the value that diverse experiences and skill sets bring to board decision-making, and many recognize the specific value in diversity reflective of customers and employees. According to the 2009 Spencer Stuart Board Index, 89% of S&P 500 companies have at least one woman on the board, 53% have two or more women and women comprise 16% of all independent directors. Moreover, at S&P 200 companies, 85% have at least one minority director and minorities account for 15% of all directors.