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Rights of Minority Shareholders

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General Report

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GENERAL REPORT ON RIGHTS OF MINORITY SHAREHOLDERS

INTRODUCTION

The purpose of this General Report is to outline a worldwide perspective on rights of minority shareholders in public and privately held corporations, as such perspectives represent a very useful tool to understand the need for innovative changes in rules to allow greater powers to minorities, in ways that increase their ability to defend themselves from majority expropriation, in the wake of corporate governance world crisis in the midst of globalization. Thus, the matter implies a great responsibility and a clear challenge for lawyers and jurists in the everlasting search of justice and fairness. Of this subject matter, we further discuss in this paper.

This Report has been prepared after reviewing eleven National Reports drafted by brilliant and dedicated lawyers and jurists of different jurisdictions, continents and cultures which have enhanced our corporate understanding: Brazil, Germany, Hungary, India, Iran, Italy, Japan, Latvia, Lithuania, Spain and Sweden. Therefore, this work has been possible thanks to the great effort of the National Reporters, and to the kind and strong support of the President and Vice Presidents of the Corporate Law Commission. In view of that, we have attempted to give the appropriate standing to each and every contribution.

To facilitate the reading of this work, we have followed the questions raised at the time of kindly submitting to you this General Report, with the multiple perspectives on rights of minorities.

QUESTIONNAIRE ON RIGHTS OF MINORITY SHAREHOLDERS

I. CURRENT SCENARIO

1.1 How and to what extent are minority shareholders protected in publicly and privately held corporations, either as to legal or firm's level protection?

Most Jurisdictions reported that rights of minority shareholders are protected mainly through legislation (Civil Code, Commercial Code, Companies Act , other Laws and administrative regulation), in one or another manner; and most of them to a limited extent, except in some jurisdictions where there are instruments for a higher protection.

The minority shareholders are also protected by means of the respective by-laws and Articles of Incorporation, by Corporate Governance provisions and practices established by private commissions, and by the entering into shareholders' agreements.

Of the particular treatment of such rights by the different Jurisdictions, we inform as follows:

Brazil. Legal body: Corporate Law n. 6,404 of December 1976, as amended by Law n. 9,457 of May 1997, and by Law n. 10,303 of October 2011. In addition minority shareholders have protection of their rights through the undertaking of shareholders' agreements in the business context of the implementation of Corporate Governance.

Germany. Legal bodies: Limited Liability Companies Act, Stock Companies Act, Civil and Commercial Codes in the case of partnerships and Corporate Governance Codex (established by a private commission).

Some of the most important rights granted to minorities in Germany are related to: right of equal treatment, right to convene shareholders' meetings and to amend the agenda; right to request information; right to appoint and revoke management; right to receive dividends; right to challenge resolutions and disadvantageous insolvency plans; right to terminate shareholding through fair market compensation; right to audit; and also related to: corporate governance responsibility; restraints on competition; and capital maintenance. Important to mention that the level of protection is quite high in the case of listed stock corporations.

Hungary. Legal body: Civil Code-Act V of 2013. However, better protection for minority shareholders may be incorporated into the articles of association in case of privately held companies, and into the by-laws of the publicly held.

In Hungary, some of the most relevant rights of minorities are related to the following matters: requesting convocation of the supreme body, where members of the business association together control at least five per cent of voting rights; requesting special audits; initiating enforcement of claims; prohibition of derogation by the companies' instrument of formation of Civil Code provisions that protect minorities; right to make additions to the agenda where a group of shareholders together controlling at least five per cent of the votes, in a private limited company. Also interesting to mention that a general meeting may not be held by conferencing (not in a conventional way) if objected -indicating the reason- by a group of shareholders controlling at least five per cent of the total number of votes.

India. Legal body: the legal framework for protection of minority shareholders is the Companies Act of 2013, but oppression and mismanagement are still in force pursuant to the old Companies Act of 1956.

Some key statutory provisions protecting minority shareholders are connected with: the obligation of listed companies to formulate a policy for dealing with all related party transactions, which ensure great participation of minorities of important matters of the companies; the introduction of e-voting for all companies having 1000 or more shareholders. Also in India in order to protect their investment, minorities negotiate for various contractual rights.

Iran. Legal body: Commercial Code ratified in 1933. Few articles of said Code are considered as protective regulations in public and private joint stock companies i.e. collective voting rights for appointment of directors; right to be informed of the financial status, and possibility to claim against directors.

Iran regulations suffer from having no specific law that would duly and directly address the main issues of corporate governance; however, Tehran Stock Exchange ratified an instruction called the By-Law on the Principles of Corporate Governance that provides guidelines on the corporate governance in public stock companies (fairness, transparency, accountability and responsibility), principles of which could be voluntarily taken into account by the directors and managers of public and private joint stock companies.

Italy. Legal bodies: Civil Code, Consolidated Law of Financial Intermediation and Regulations of the Financial Authority for stock companies. It is also possible to ensure minorities protection by means of shareholders' agreements, where only the subscribers are liable for the damages caused to the other ones, and where only a

damage action is available in case of breach of relevant provisions thereof.

Japan. Legal body: Companies Act that provides for specific rights to minority shareholders, divided into a) economic rights i.e. reception of dividends and residuals; and ii) concerning the management of a company, i.e. rights to vote at shareholders meetings, to propose agenda at shareholders meetings, to bring derivative suits, and to check accounting books and records.

Act requires a company to treat shareholders equally, depending on the number and content of shares held by those shareholders (the so called “shareholder equal treatment principle”). Any actions breaching the above would be void. Companies may create also additional rules to protect rights of shareholders in the Articles of Incorporation, although they are quite simple and just provide matters which are required to be included by way of laws.

Latvia. Legal body: the new Commercial Law (2002) regulates the relationship between the shareholders and the different types of companies (including LLC’s and stock companies). However, this law provides for few regulations concerning the protection of minorities. The Commercial Law contains both imperative provisions and other ones which can be modified in the Articles of Association of the companies.

Commercial law is based on codified law, thus, minority shareholders commonly resort to the protection provided by law and fail to incorporate other protection measures such as private arrangements.

Lithuania. Legal Body: the Civil Code regulates among others, the right to conclude

shareholders agreements and to lodge claims against unlawful shareholders decisions; The Law on Companies that provides among others, the right to information, to initiate general meetings of shareholders and audits, and to submit proposals for the agenda; the Law on Markets in Financial Instruments and the Law the Securities Law, also relevant for some aspects of protection of minorities.

In addition, the European Union Directive 88/627/EEC (the Large Holding Directive) was implemented in this Jurisdiction. The Directive as we know, is devoted to the creation of disclosure standards.

At the legal level, the protection of minorities is minimal. By the documents of incorporation and by shareholders agreements, the minority may be granted with broader protection of its rights. Important to mention that in Lithuania, minority shareholders of public companies are given protection through a tender offer which is mandatory at the level of acquisition of forty per cent of all shares.

Spain. Legal body: the Companies Act does not establish a specific instrument to protect the minority shareholders other than the exit and subsequent payback to the oppressed shareholder (“in game rule”). However, minority shareholders can have other types of remedies such as derivative suits executed as a purely compensatory mechanism (equivalent roughly to social responsibility actions).

Under certain circumstances shareholders have a right to exit the company, cancelling their membership and reclaiming the invested amount. These rights belong to all shareholders and do not require a minimum percentage of capital for their exercise. Even though, it is the minority shareholder who will usually benefit from this protection, when the majority adopts decisions of particular importance that affect the essence, object or configuration of the company itself.

Shareholders voting against the corresponding resolutions will be entitled to withdraw from a company in cases such as: involvement in a cross-border intra-community merger the resulting company of which will have its registered office in another Member State; takeover by a European company with registered office in another Member State; formation of a European holding. The withdrawal will be automatic in the case of shareholders who by operation of the transformation, acquire personal liability for the company debts and do not vote in favor of the resolution.

Sweden. Legal bodies: the Corporate Governance Code for listed companies, and the Companies Act which is based on the principle that it is the majority that has the power to make decisions.

But in order to prevent the majority to oppress the minority, the Act contains rules that limit the majority's freedom of action, such as: (1) fair-play rules (the rule of equal rights in the company and the general clause): the latter states that neither the general meeting, the board of directors, nor a managing director may take a decision that is likely to provide an unfair advantage to a shareholder or any other person, to the disadvantage of the company or any other shareholder; (2) rules concerning insight in the company: every individual shareholder has the right to have a matter addressed at the general meeting; the company's board must convene an extraordinary general meeting if so requested by a minority of the shareholders that together hold 10% or more of the shares; an appointment of a minority shareholders' auditor; the appointment of one or several special examiners; to demand distribution of a dividend at the annual general meeting (3) the minority's right to make principal decisions for the company, and (4) the minority's right to be bought out of the company in certain cases.

1.2 Do they have in essence real choices, or are the ones that are in the hands of the dominant group, either managers or major shareholders, or are they restricted to those that do not challenge the majority power, representing the status quo?

Six of the Jurisdictions responded to this question generally in an affirmative manner: **Brazil, Germany** in certain cases depending on the type of company, **Hungary, India** by means of judicial redressal but as a last option, **Italy** in the case of LLC and stock companies unlisted, and **Latvia**; other four Jurisdictions, not in a positive way: **Iran, Japan, Spain** where shareholders' agreements become the only method to really protect the minorities in publicly and privately held corporations, and **Sweden** where the right to demand distribution of dividends is the only one of such an active nature; whereas **Lithuanian** Reporter pointed out that real choices of minority shareholders are limited and not effective enough in practice.

1.3 Has the law and precedents of your country evolved in ways that increase minority shareholders ability to defend against expropriation by those in control (misuse of assets, reallocation of profits, transfer pricing, etc.) ?

Most of the National Reporters answered that their Jurisdictions have made considerable efforts to promote and defend rights of minorities: **Brazil**, where the last reform of its Corporate Law reintroduced Tag Along and raised the minimum mandatory dividend for preferred shares; **Hungary**, where less than 5% of stockholders can request special audits or initiate the enforcement of claims if the by-laws so stipulate; **India**, where one of the important measures after the Satyam Scam, is the Related Party Transaction, whereby minority shareholders have been successfully

involved in the decision making process. Other measures include regulating the affairs of the board with disclosure requirements i.e. codifying the duties of directors and appointment of independent directors prescribed classes of public companies.

This group of Jurisdictions with a positive law evolvement in the protection of minorities, includes also: **Italy**, where in view of the dominance of company groups in related party transactions, it has developed special rules and jurisprudence, and where the monitoring of courts on the management of listed companies has increased; **Japan**, where courts tend to consider necessity of protecting minority shareholders. Stock exchanges also recently tightened the regulations for said protection in abusive issuance of shares in the market, and increase the requirements to have independent directors, who are supposed to work for the interest of minority shareholders; **Latvia**, where under the Commercial Law, minority shareholders, provided some requirements are met, are entitled to request the management board the filing of a suit against founders, council, the auditor or the management board itself on behalf of the company; if the board fails to file the suit after one month after the request, the minority shareholder is entitled to directly file the suit; **Sweden**, where one important change, is the incorporation of the “Leo-law”, which sets forth that in a new issue of shares, transfer of shares, warrants or convertible instruments or certain types of loans directed to a member of the board of directors, the managing director, employees of the committing company or those closely related to the persons just referred to, a qualified majority of 90%, both of the votes cast and the shares represented at the general meeting, is required to be valid; and in companies listed on an authorized marketplace, the annual general meeting shall adopt resolutions regarding compensation to the management; and **Lithuania**, where after amendments to local laws, minorities have broader rights to apply to courts, claiming that a specific decision made by the majority violates their rights, and thereby they can contest its validity and provided certain requirements are met, request payment of

damages. Also minorities can file there preventive claims in court requesting to ban future majority decisions which could cause damage to the Lithuanian company.

In the case of **Germany**, although there are ways for minority shareholders to defend themselves against majority shareholders and corporate mismanagement, as the right to request information or require a special audit, as well as to appoint and revoke management staff and challenge unlawful shareholders meetings resolutions, they are moderately efficient at best, and in most cases, minority shareholders cannot avoid harmful actions or resolutions, with the sole exception of LLC, in which a minority shareholder may judicially require the dissolution of the company in case of profound quarrels between the shareholders as ultima ratio.

As to **Iran**, no specific procedure has been predicted for internal control of power of major shareholders, although the appointed inspectors may play a crucial role for observing the acts of management. On the other hand, there seems that the law of **Spain** has not in reality evolved in a way that increases the protection of minority shareholders.

1.4 Is the legal dimension the prevalent one in the Corporate Governance (CG) atmosphere, or is the firm's level CG the common manner to protect minorities?

For all National Reports the legal dimension is the prevalent manner to protect minority shareholders. However, at the firm's level, several defensive mechanisms can be applied on the basis of shareholders agreements and of by-laws as well.

It is interesting to mention as to this matter, that in the case of **Iran**, the legal dimension prevails mainly because shareholders agreements are not a common

procedure in corporate law for guarding rights of minor shareholders; nevertheless, through collective voting, the minor shareholders in said Jurisdiction, could put all their voting shares together to be granted to one person, and accordingly, it could be likely for the minor shareholders to nominate a representative in the Board. In **Latvia**, although Corporate Governance rules on the firm's level would be a better and more suitable tool for protecting the interests of the minority shareholders, this tool is largely underestimated by local companies, thus, the Corporate Governance rules provided by law currently remain the common tool for protecting the minority shareholders. As in the case of **Lithuania**, it is important to bear in mind that there is no voluntary Good Corporate Governance code, either proposed or accepted by the corporate community.

1.5 What is the role of ownership concentration in the protection of the minority?

Ownership concentration does not play a protective role in favor of the minority shareholders, according to the relevant content of the National Reports, in consequence, minorities are forced in many cases, to be in a vulnerable situation, as in the case of dividend distributions, as asserted by Reporter of **Brazil**. In the case of **Lithuania** for example, ownership concentration is a leading shareholders structure.

In some Jurisdictions however, controlling shareholders have certain responsibility towards the company and other shareholders; in **Japan** for example, said responsibility is not admitted by its courts. In the case of **Italy**, high ownership concentration and limited contestability of control, are key features of listed firms; that trend in Italy is however, slightly decreasing.

In connection with this matter, in **Germany**, minority shareholders may not be

restricted in competing with the company in case they have no extraordinary influence on the company, but majority shareholders also could be allowed to compete, if the competition existed beforehand, and this fact was known to all the shareholders.

Also in Germany, minority shareholders of a LLC are entitled to a minimum dividend if the company is part of a profit and loss pooling agreement with the majority shareholder. In a listed stock corporation, shareholders are entitled to claim a minimum dividend of four per cent of the share capital. There are not provisions to guarantee a minimum dividend for minority shareholders of partnerships.

1.6 Is benchmarking used as a mechanism for minorities to select the country or firm better suited to risk profile and protection from rights deprivation?

Benchmarking, as a systematic structured process that provides with evaluation of methods and best market practices, as well as with the valuation and projection of the future performance of a company, can be used in **Brazil**, as a criterion for choosing a company for small shareholders.

The response to this question on benchmarking, is quite interesting because the majority of European Jurisdictions answered that such mechanism is not used by shareholders for said purpose, as in the case of **Germany, Italy, Spain and Sweden**; whereas in **Brazil** as above mentioned, **Iran** in the case of public joint stock companies, **India, Hungary and Latvia** –as European exceptions-, benchmarking is a common practice and used as an instrument to consider various aspects for the ease of doing business in a country, i.e., legal and regulatory framework, protection of investors rights, legal enforceability of contracts, tax impact, due process and rule of law.

In **Japan**, benchmarking is not generally used, but it is expected there that professional investors such as hedge funds who buy minority stakes of companies, consider how minority shareholders are protected under the laws and in practice in investing in certain firm or country.

Useful to comment in connection with this matter of benchmarking, that in **Latvia** minority shareholders (investors) tries to implement the best aspects of their home jurisdictions and convince their partners to incorporate them into the bylaws. It is worth mentioning that in Latvia, the choice between companies may also be difficult, considering existing shareholders' agreements are not publically available, therefore, interested parties should carry out due diligence before entering the company.

1.7 Is the formation of group dynamics among dispersed shareholders working in your country?

The formation of said groups dynamics is generally not working in **Japan**; it is incipient in the cases of **Brazil** and **India**; whereas it works in other Jurisdictions such as **Lithuania, Iran** and **Sweden**, where the Swedish Shareholders' Association works at defending small shareholders' rights, keeping track of matters concerning individual stock ownership and provides the minority shareholders with important information and education.

In **Italy**, formation of group dynamics among dispersed shareholders can work rarely at listed company level; indeed –asserts the Italian Reporter- these dynamics can be implemented in closely based companies by virtue of shareholders agreements, in terms of exercise of voting rights on certain strategic or material decisions both at board and shareholder meetings levels.

Minority shareholders in **Latvia** are forming groups within the companies based on interests on a case-by-case basis, however, it cannot be stated with certainty whether the formation of said groups may work in a long term perspective; the efficiency - says the Latvian Reporter- of such formation is conditional on the amount of shares they can represent collectively in order to influence at least some decisions (according to the required thresholds).

1.8 What is the role of market liquidity in the minority shareholders exit option?

For Jurisdictions such as **Latvia, Spain** and **Sweden**, market liquidity plays no role in general as to the minority exit option. In the case of **Spain**, because in the event that the rest of shareholders does not acquire the minority shareholding, then the company itself shall acquire the shares of the minority that is willing to leave. In **Sweden**, there have been no signs of market liquidity being a problem, although it is said by Reporter that perhaps the amount of buy-out processes would increase with better liquidity of the market. As to **Latvia**, it becomes relevant only where the shareholder has not exercised the voluntary option and has been expelled, in which case, the company is obligated to sell the shares on the market, and disburse to the shareholder, 80% of the price received from the buyer of shares. In regard with **Lithuania**, the law does not provide automatic appraisal rights in the form of buyout of dissenting shareholders; however, the courts may order a buyout, but in this regard only few cases of this kind have been heard so far in practice.

On the other hand, market liquidity does play a role as to that exit option, in the cases of: **Brazil**, where liquidity occurs in the event that the type of share integrates the representative general index of securities portfolio admitted to trading in the

securities market of Brazil or abroad; **Hungary**, where it is an essential element, since it secures that minorities have not only the exit option, but the payment of the shareholding at a fair market value, within reasonable time; **India** , in cases of public listed companies, although contractual exit options -i.e., secondary sale- are provided to minority investors to ensure protection to unlisted and private companies; **Italy** - for listed and unlisted companies-, in that Jurisdiction there are some tools available for the exit option, due to market liquidity effects. Whereas in the case of **Iran**, the playing of said role depends on the scope of business, i.e., in banking the market is a liquid one and thus, entrance and exit are easily conducted, but in huge construction companies, the risk of illiquidity is higher and subject to non-transparency.

1.9 Have legal reforms in your country given tools to majority to use compliance as an instrument to somehow “legalize” minority expropriation?

In six of the Jurisdictions, the legal reforms undertaken thereby have not given said tools to majority as a means for minority expropriation: **Brazil, Germany, Hungary, India, Iran** and **Spain**. The opposite happens in the cases of **Japan** and **Italy**, where in the latter for example, Italian Law no.116 (2014) entitles companies to amend their articles of association, in order to allow the grant of up to two votes per share to shareholders who have held their shares continuously for at least two years (“loyalty shares”), depriving minority institutional investors of their right to vote with the same weight of controlling shareholders. In **Latvia**, when dealing with listed companies, the laws give majorities several tools therefor.

As to this issue, very interesting to mention is the case of **Sweden**, where the relevant part of Act of Public Takeover-Bids on the Stock Market, states that when someone achieves a stockholding representing at least 30% of the votes in a listed company, the obligation to leave a public takeover-bid arises. This is not minority expropriation

in the true sense of the word according with the Reporter with whom we agree thereupon, but the result may very well be the same. As to **Lithuania**, despite of reforms, so far the protection of minority shareholders is more evident according to the Reporter, at theoretical level, but not effective enough in practice.

II. LOOKING FORWARD

2.1 What is the way to avoid *minority shareholders* from suffering mayor shocks, -if applicable in your country- due to restrictive visions as to minority rights, without falling into abuses of minority rights? Is it possible to harmonize both given the circumstances?

As to this issue which implies a paradox, there are five approaches: one represented by **Iran**, affirming that there is no way to avoid that minorities suffer major shocks, since there are no regulations to protect them, and the market control has no fundamental role in regard with dominance of governmental companies.

Another group, formed by **India** and **Sweden**, underline the harmonization issue, sharing the idea that it is possible to reach a fine balance between the two needs, through the decision of Swedish legislation of giving a minority that holds at least 10%, a somehow wide minority protection, and through the present Indian statutory framework that tries to maintain said harmony by appropriate checks and balances, courts playing a very important role in this matter.

Whereas, **Italy**, **Japan**, **Lithuania** and **Hungary** state that the ways to avoid minorities from suffering major shocks are: in Hungary, active shareholder engagement in the course of the company business since the lack of it is one of the

main factors behind the abuses seen in practice; protective content of the by-laws, and agreements among shareholders stating for example, provisions on how to select management, veto rights, exit options and information disclosure rights, ability to file claims in the cases of Italy, Japan and Lithuania. The Reporter of Lithuania states that laws concerning transparency and the relative power of minorities in the event of takeovers threat are crucial for that purpose.

The fourth approach is that of **Brazil**, emphasizing the abuse element: the Brazilian Corporate law indicates the acts of the controlling shareholders that are considered abuse of power and that generates personal accountability; and key to mention that the Brazilian courts have admitted that the Consumer Code is applicable to matters of minority shareholders, given their vulnerability.

The fifth approach with regard to this crucial matter is that of **Spain** who addresses the issue by asserting that all shareholders' conduct, regardless of their portion at company capital, must be guided by principles of fairness and good faith. Nevertheless, certain rights granted to minority shareholders under Spanish law run the risk of being used in an opportunistic manner which could gravely compromise the interest of the company and the normal operation of corporate bodies.

The Spanish Reporter further argues that in order to harmonize a greater protection of minority shareholders with the safeguard of the interest of the company as a whole, it would be useful to have more *interim* measures available, under which the Spanish court could evaluate the urgency by adopting certain decisions (i.e. the financial necessities of the company in light of the failure to adopt capital increases or structural transformations).

2.2 Is minority shareholders activism taking place in your country, and to

what extent ?

Half of the Jurisdictions that expressly answered this question, states that shareholders activism is taking place to an important extent, being the case of **Italy** with regard to listed companies, **India**, **Sweden** and **Brazil**; the other half including **Japan**, affirms that it is taking place, but not very often and to a limited extent, either because activism is ineffective as in the case of **Latvia**, where negotiation with the majority is the best way for minorities to have influence in the business; or because it is rather a new phenomenon, as in the case of **Spain**, or because it depends on the internal culture of each company, as in **Iran**. In **Lithuania** said activism is not that common.

2.3 What is the trend in your country for the protection of minority shareholders?

In almost all Jurisdictions the trend is to improve significantly and make more efficient the protection of minority shareholders, as in **Hungary**, where provisions on minority shareholding in effect become more consequent and transparent; as in **Sweden** where the expected changes in listed companies are –among others, stricter legislation regarding transactions to related parties and the time limit on declaration of acquisitions of shares is expected to be prolonged; **as in Germany**, where the trend seems to be a high level of protection in listed stock corporations, but a limited one for other types of companies; as in **India**, where there are notable provisions towards upholding minority rights, such as wider powers to minorities in respect of mergers, acquisitions and amalgamation processes, and in respect of appointment of independent directors on the board, protecting minority; as in **Brazil**, where there are reports of minority shareholders who sought the courts to charge the losses in the value of the shares of Petrobras by accusation of corruption.

In **Italy** the trend is also to improve the protection, mostly in case of listed companies, and especially in terms of rules of transparency of the decision-making processes of boards and disclosure of the membership of a corporate group, and their mechanisms of enforcement, all of which results in a very promising trend. As to **Japan**, the tendency is to have more regulation to protect minorities, because governments and stock market operators of that Jurisdiction, felt the necessity to protect them against abusive use of laws. In the case of **Latvia**, Reporter points out that the State has strived to adopt and implement almost every reasonable legal measure aimed to protect minorities, but according to Latvian scholars, a major gap in the legal framework is a statutory exit option, since currently, a shareholder has no possibility to leave the company, transfer its shares to the entity itself, and receive a just compensation.

On the other hand, **Iran** and **Spain** seem to have basically a common trend: it is difficult to point out what the main tendency is regarding protection of minority shareholding. In Iran, referral to public courts would be considered as the final solution. In Spain despite that tendency, the Supreme Court ruled in favor of the minority shareholders, denying the validity of certain transactions carried out by the majority that pursued the divesting of some key elements to another company of the same group. In **Lithuania** says the Reporter, the number of cases regarding violations to minority rights from the side of majority shareholders is increasing, and in most cases the minority shareholders are rather passive.

2.4 What is the impact of the Sarbanes-Oxley Act (SOX) in your country, as a canon to regulate domestic capital markets and CG?

Before addressing this issue, let us point out some of the key points of SOX:

- I. Public company oversight board.
- II. Auditor independence.
- III. Corporate responsibility.
- IV. Enhanced financial disclosures.
- V. Analyst of conflict of interest.
- VI. Commission resources and authority.
- VII. Studies and reports.
- VIII. Corporate and criminal fault accountability.
- IX. White-collar crime penalty enhancements.
- X. Corporate tax returns.

As to this matter, in most of the Jurisdictions, SOX either has no impact or has a limited one; that is the case of **Germany**, because SOX does not constitute a particular protection of minorities; **India**, because the requirements of said Act have been in place under Indian laws; **Iran**, because it does not affect directly her laws, and the issues regarding CG are still unfamiliar thereto; **Italy**, because it is not applicable to her companies; **Brazil**, because SOX is mandatory solely for companies that are present in the international market, and because some rules thereof have been already under her laws; **Latvia**, because SOX is only applicable to companies interested in being listed in the USA, and because the majority of its rules already existed or were implemented later into the applicable laws; and **Lithuania**, where SOX-type regulation is not enacted, however similar concepts are being discussed, according with the Reporter.

Whereas the Reporter from **Hungary** states an interesting experience: that SOX imposes heavy regulatory and financial costs and compliance burdens to small start-

up companies, preventing many of them from funding the high levels of administrative costs of being public companies; on the other hand, the Reporter points out that the European Union was just as determined as the USA to increase investor protection and prevent corporate scandals through the EuroSox, that is equivalent to SOX.

In Japan, Spain and Sweden, SOX has a substantial impact, because for example in the case of Sweden, it is the basis to her Corporate Governance Code.

2.5 Do you think it advisable to rescue the concept of “Popular Capitalism”, as defined in the fifties by the great jurist Joaquin Garrigues in view of the present circumstances regarding status of minorities?

In the cases of **Italy and Japan**, it is considered very advisable: the former to the extent that minority shareholders would have a real protection, and also in terms of participation and voice in the decision making process; the latter because “Popular Capitalism” is defined as a theory or system based on the idea that everyone has the opportunity to own property and shares. **Indian** Reporter considers it advisable, but given the current statutory framework, the need to rescue said concept, may not be necessary, since such framework provides for adequate safeguards to protect interests of minorities and corporate governance standards. **Latvian** Reporter although implicitly thinks it advisable, affirms that it is unlikely that such concept could be implemented in Latvia in the foreseeable future, by virtue of the rather low level of statutory and firm’s current framework.

On the other hand, in the case of **Spain** it is not considered advisable, given the current circumstances as to this matter in said Jurisdiction. **Swedish** Jurisdiction does

not express an opinion thereon, in view of the nature of the concept at debate: a political one.

2.6 What should be the role of minorities as to the flaws of executive pay packages that reflect structural problems in underlying governance agreements, as pointed out by Lucian Bebchuk, Harvard Law Professor?

As to this matter, in the case of **Japan** it is mentioned a very interesting experience: Japanese managers do not normally receive a large amount of pay packages to motivate managers to take risks and work hard for the growth of the businesses. **Indian** Reporter states that Board accountability would significantly improve if minority shareholders played a vigilant role by questioning the majority and the Board on their acts and policies.

Important to mention that **Italy** at the end of 2010, introduced for listed companies, a regulation requiring companies to publish a remuneration report and to submit a policy thereon to a mandatory non-binding shareholder vote –the so called Say on Pay system (SOP).

Spanish Reporter says on this issue, that often corporate Boards set up payments guided exclusively by the shareholders' interests, and that in said context, the salary of the managing directors has been subject to strong public criticism. In **Sweden**, the Companies Act and the Corporate Governance Code demand for disclosure of remuneration. **Brazilian** Reporter addresses this issue by stating that if management does not comply with good practices, it should be liable therefor.

Hungarian Reporter points out a crucial fact as to this issue raised by professor Bebchuk from Harvard: compensation agreements are always the focal point of the relationship between shareholders and management, and dispersed shareholder ownership has less incentive to monitor management and to invest effort in reducing managerial opportunism than large outside shareholders.

Whereas the **Lithuanian** Reporter mentions as to this matter, that shareholders in large publicly traded companies, lack the power to intervene and change existing arrangements, and that in view thereof, management might have an excessive tendency to reject attractive opportunities to merge, sell or dissolve, because termination would end its control over the independent company. These answers are sufficient to initiate a good debate on this very relevant corporate matter.

III. PRECEDENT CASES

As to this matter, we kindly suggest that you review each one of the National Reports to grasp the interesting judicial trend regarding the defense and protection of the minority shareholders.

We can summarize the content of the reported precedents by saying that most of them are protective of minority shareholders, although in an very interesting Indian case (Cadbury India Ltd.), the Court forced the company to issue a fresh valuation of its stock, at a 50% increase in the initial offer it had made a few years earlier to buy back its shares from minority shareholders, due to objections raised by them, but also reprimanded the minority and declined to entertain their requests for conducting repeated valuations so as to obtain an even higher share price, thereby upholding the

overall commercial interests of the company, whilst providing minority shareholders with adequate consideration for their forced exit from the company.

In connection with the crucial issue raised in point 2.1 of this General Report, we can affirm that this precedent from India proves that harmonization of ideals is possible.

Maybe that could be the conclusion of this General Report, but we submit it to debate, because Law is and has always been -just remember the great Greek and Roman thinkers and jurists- a matter of a fascinating dialectical enterprise undertaken by lawyers and jurists who in their tasks seek fairness and justice. Thanks to all.

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