THE CORPORATE GOVERNANCE REVIEW

Tenth Edition

Editor
Willem J L Calkoen

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Willem J L Calkoen

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I am proud to present this new edition of *The Corporate Governance Review* to you.

In this 10th edition, we can see that corporate governance is becoming a more vital and all-encompassing topic with each year that passes. We all realise that the modern corporation is one of the most ingenious concepts ever devised. Our lives are dominated by corporations. We eat and breathe through them, we travel with them, we are entertained by them, most of us work for them. Most corporations aim to add value to society, and they very often do. There is increasing emphasis on this. Some, however, are exploiting, polluting, poisoning and impoverishing us. A lot depends on the commitment, direction and aims of a corporation’s founders, shareholders, boards and management, and employees. Do they show commitment to all stakeholders and to long-term shareholders, or mainly to short-term shareholders? There are many variations on the structure of corporations and boards within each country and between countries. All will agree that much depends on the personalities and commitment of the persons of influence in the corporation.

We see that everyone wants to be involved in better corporate governance: parliaments, governments, the European Commission, the US Securities and Exchange Commission (SEC), the Organisation for Economic Co-operation and Development (OECD), the UN’s Ruggie reports, the media, supervising national banks, more and more shareholder activists, proxy advisory firms, the Business Roundtable and all stakeholders. The business world is getting more complex and overregulated, and there are more black swans, while good strategies can quite quickly become outdated. Most directors are working very diligently. Nevertheless, there have been failures in some sectors and trust must be regained. How can directors do all their increasingly complex work and communicate with all the parties mentioned above?

What should executive directors know? What should non-executive directors know? What systems should they set up for better enterprise risk management? How can chairs create a balance against imperial CEOs? Can lead or senior directors create sufficient balance? Should most non-executive directors understand the business? How much time should they spend on their function? How independent must they be? Is diversity actively being pursued? Is the remuneration policy defendable? What are the stewardship responsibilities of shareholders? What are the pros and cons of shareholder rights plans and takeover defences?

Governments, the European Commission and the SEC are all pressing for more formal inflexible legislative acts, especially in the area of remuneration. Acts set minimum standards, while codes of best practice set aspirational standards. We see a large influence on norms by codes and influential investor groups.

More international investors, the Business Roundtable, voting advisory associations and shareholder activists want to be involved in dialogue with boards about strategy, succession and income. Indeed, far-sighted boards have ‘selected engagements’ with stewardship...
shareholders to create trust. What more can they do to show all stakeholders that they are improving their enterprises other than through setting a better tone from the top? Should they put big signs on their buildings emphasising integrity, stewardship and respect?

Interest in corporate governance has been increasing since 1992, when shareholder activists forced out the CEO at General Motors and the first corporate governance code – the Cadbury Code – was written. The OECD produced a model code, and many countries produced national versions along the lines of the Cadbury comply or explain model. This has generally led to more transparency, accountability, fairness and responsibility. However, there have been instances where CEOs have gradually amassed too much power, or companies have not developed new strategies and have incurred bad results – and sometimes even failure. More are failing since the global financial crisis than before, hence the increased outside interest in legislation, further supervision and new corporate governance codes for boards, and stewardship codes for shareholders and shareholder activists. The European Commission is developing regulation for this area as well. Recently, we see that governments want to involve themselves in defending national companies against takeovers by foreign enterprises. We also see a strong movement of green investors, which often is well appreciated by directors. There is a move to corporate citizenship. The Business Roundtable with about 180 signatories has confirmed to embrace stakeholder corporate governance.

This all implies that executive and non-executive directors should work harder and more as a team on long-term policy, strategy, entrepreneurship and investment in R&D. More money is lost through lax or poor directorship than through mistakes. On the other hand, corporate risk management with new risks entering such a digitalised world and cybercrime is an essential part of directors’ responsibilities, as is the tone from the top. How can directors do their important work well without being petrified of attacks from shareholders, regulations and the press?

Each country has its own measures; however, the chapters of this book also show a convergence. Understanding differences leads to harmony. The concept underlying the book is that of a one-volume text containing a series of reasonably short, but sufficiently detailed, jurisdictional overviews that permit convenient comparisons, where a quick first look at key issues would be helpful to general counsel and their clients.

My aim as editor has been to achieve a high quality of content so that The Corporate Governance Review will be seen as an essential reference work in our field. To meet the all-important content quality objective, it was a condition sine qua non to attract as contributors colleagues who are among the recognised leaders in the field of corporate governance law from each jurisdiction.

I thank all the contributors who helped with this project. I hope that this book will give the reader food for thought; you always learn about your own law and best practice by reading about the laws and practices of others. Further editions of this work will obviously benefit from the thoughts and suggestions of our readers. We will be extremely grateful to receive comments and proposals on how we might improve the next edition.

Willem J L Calkoen
NautaDutilh
Rotterdam
March 2020
Chapter 1

AUSTRALIA

Jeremy Blackshaw, Kate Koidl, Bart Oude-Vrielink and Lucy Wang

I OVERVIEW OF GOVERNANCE REGIME

In Australia, listed companies are subject to a corporate governance regime comprising various legislative instruments and regulatory guidelines including the Corporations Act 2001 (Cth) (Corporations Act), the Listing Rules of the Australian Securities Exchange (ASX), the Market Integrity Rules (Securities Markets) 2017 (Market Integrity Rules) of the Australian Securities and Investments Commission (ASIC), the ASX Corporate Governance Principles and Recommendations (CGPR) (4th Edition), the accounting standards of the Australian Accounting Standards Board (AASB) and ASIC’s regulatory guides.

The Corporations Act regulates, among other things, the corporate governance duties and standards of behaviour for both private and public, listed and non-listed companies. It also applies to both local companies and foreign companies that are registered in Australia. As the principal piece of legislation in this area, the Corporations Act provides a roadmap for company officers and directors. It features a comprehensive regime of mandatory provisions that attract penalties for contravention and optional replaceable rules that can be excluded, modified or replaced by an alternative provision in a company’s constitution.

The ASX, Australia’s primary securities exchange and one of the world’s top 10 listed exchange groups by value,2 has many overarching objectives, including:

- supervising compliance by listed entities with the Listing Rules and enforcing any contraventions of these rules;
- highlighting the importance of sound corporate governance values to ASX-listed entities in Australia; and
- educating retail investors, who lack a sophisticated understanding of the companies they are considering for investment opportunities.

The Listing Rules serve many purposes and govern terms around admission to the official list, disclosure and general behaviour. Contraventions of the Listing Rules can be enforced against listed entities pursuant to various provisions of the Corporations Act.

ASIC is empowered by Pt 7.2A of the Corporations Act to create the Market Integrity Rules, which govern domestic licensed financial markets and participants in those markets.

Established in August 2002, the ASX Corporate Governance Council (Council) operates as a hub for various stakeholders to share insights on topical corporate governance issues. The Council was responsible for developing the CGPR, the first edition of which was

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1 Jeremy Blackshaw, Kate Koidl and Bart Oude-Vrielink are partners and Lucy Wang is a lawyer at MinterEllison.

Australia

published in 2003. The Council has just recently released the fourth edition of the CGPR, which will apply to ASX-listed entities for financial years commencing from 1 January 2020 onwards. This revision was prompted by growing concerns over trust, values and culture in the corporate sphere.

Listed entities must take an ‘if not, why not’ approach to the CGPR. This simply means that, although the board of a listed entity is entitled to not adopt certain recommendations that it considers are inappropriate in the circumstances, it must explain its reasons for forming this view.3

Although the AASB operates under the Australian Securities and Investments Commission Act 2001 (Cth), the accounting standards developed by the AASB are enabled by the Corporations Act. The preparation and disclosure of financial statements serve a very important purpose by ensuring the accountability of a company’s management.

i ASX
The ASX is responsible for ensuring compliance by listed entities with the Listing Rules and the ASX Settlement Operating Rules (Operating Rules). It has certain limited powers, including suspension, delisting, ordering rectification and referral of matters and investigations to ASIC.

The ASX’s powers to investigate are curtailed in many respects as it is compelled by the Corporations Act to defer to the authority of ASIC in regard to various issues, such as investigation of breaches of the Corporations Act. Nevertheless, the ASX and ASIC often work together to ensure that listed entities are subject to an appropriate degree of supervision.

ii ASIC
As the chief corporate regulator, ASIC serves a variety of different and important functions, including:

a identifying breaches of the Market Integrity Rules;
b overseeing financial markets, participants of these markets and trading on domestic licensed financial markets such as the ASX;
c enforcing compliance with corporate governance standards and punishing breaches of conduct obligations; and
d administering and governing the administration of the Corporations Act.

For breaches of the Market Integrity Rules, ASIC maintains accountability through enforceable undertakings and infringement notices.

iii Australian Prudential Regulatory Authority
As Australia’s independent prudential authority in the banking, insurance and superannuation industries, the Australian Prudential Regulatory Authority (APRA) creates prudential standards on risk management, corporate governance and financial security, for participants in these markets.

In the event of a potential breach of prudential standards, APRA generally seeks to achieve compliance through cooperation and negotiation with a company’s directors and

3 ASX Corporate Governance Council, Corporate Governance Principles and Recommendations (ASX Corporate Governance Council, 4th ed, 2019).
management. However, APRA does possess enforcement powers, which it will exercise if a company or its officers resist efforts from APRA to reach a mutually beneficial solution by cooperation.

### Australian Competition and Consumer Commission

The Australian Competition and Consumer Commission (ACCC) is the regulator of federal laws relating to competition, fair trading and consumer protection and it is responsible for enforcing various sections of the Competition and Consumer Act 2010 (Cth), such as those relating to consumer protection, product safety, industry codes and anti-competitive corporate practices.

#### Recent developments

ASIC established the Close and Continuous Monitoring (CCM) Program in October 2018, which involves the placement of ASIC employees in significant financial services institutions, currently AMP, Australia and New Zealand Banking Group, Commonwealth Bank of Australia (CBA), National Australia Bank and Westpac Banking Corporation, to undertake surveillance. These ASIC employees are tasked with reviewing the non-financial risk practices of banking staff, especially those in positions of leadership and seniority. Since launching the CCM Program in October 2018, ASIC has:

- interviewed more than 300 banking employees;
- placed ASIC employees in banking institutions for the majority of business days; and
- undertaken reviews of thousands of documents.⁴

ASIC also established the Corporate Governance Taskforce, which undertook a thorough review of the specific corporate governance practices engaged in by Australia’s largest listed entities. The Corporate Governance Taskforce restricted its focus to seven of Australia’s largest ASX-listed financial institutions and was primarily interested in asking two questions:

- How was the discretion of management exercised in regard to the issue of remuneration?
- How did company officers navigate risk?

Unlike the CCM Program, the Corporate Governance Taskforce was largely a passive exercise. However, it did express some interest in practical changes, such as encouraging officers to change:

- how they treated investors and consumers;
- their disclosure habits, particularly in regard to the timing and clarity of their disclosures;
- how and when they take accountability for their actions; and
- how they engage in other corporate governance measures.

#### General trends

The relative stability of the corporate governance regime in Australia has been disrupted by two relatively recent events: the APRA inquiry into the CBA and the Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry (Banking Royal Commission). The final CBA report produced by APRA was published on 1 May 2018 and the Banking Royal Commission commenced at the start of 2018. Andrew Clarke, Professor at

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the College of Law and Justice, described this period of time in 2018 as ‘the perfect corporate storm’. These events produced a heightened awareness of corporate culture and increased public scrutiny of the alleged dishonesty and ‘hubris’ which was said to be widespread in large financial services institutions.

The Hon. Kenneth Hayne AC QC was appointed as Commissioner to oversee the Banking Royal Commission. The Commissioner released his interim report on 28 September 2018 and his final report on 1 February 2019 (Final Report). Three key themes arose from Commissioner Hayne’s pronouncements following the release of the findings from the Banking Royal Commission:

a. the law must be clear so that businesses understand their legal obligations (i.e. substantive amendments to the law to simplify it);
b. businesses must obey the law and foster a culture that drives compliance; and
c. regulators must enforce the law and act on contraventions, asking themselves ‘why not litigate’ rather than ‘why litigate’.

Further, APRA’s report identified four damaging cultural practices, which were then prevalent in the CBA:

a. entrenched complacency;
b. a reactive rather than proactive approach to risks;
c. an insular culture and an inability to learn from past mistakes; and
d. preoccupation with obtaining consensus.

II CORPORATE LEADERSHIP

In his Final Report, Commissioner Hayne noted: ‘Culture, governance and remuneration march together. Improvements in one area will reinforce improvements in others; inaction in one area will undermine progress in others.’ The following organisations have published best practice principles:

a. the Australian Council of Superannuation Investors (ACSI);
b. the Council;
c. the Australian Institute of Company Directors (AICD); and
d. the Investor Group on Climate Change.

6 Ibid 603.
7 Ibid.
10 Australian Institute of Company Directors, ‘Find out more about who we are and what we do’, Australian Institute of Company Directors (Web Page) <https://aicd.companydirectors.com.au/about>.
Board structure and practices

Public companies are required to have a minimum of three directors (with at least two residing in Australia). In Australia, the board is structured as a single tier with one chair and executive and non-executive directors.

For listed entities, compliance with the CGPR constitutes a reporting requirement. The CGPR recommends, among other things, that listed companies establish board charters, diversity policies, performance evaluations (for the board, committees, directors and senior executives) and separate board committees. Gender diversity is also a key recommendation, with listed entities included in the S&P/ASX300 Index expressly required to have a target of no less than 30 per cent of directors of each gender holding board positions. ASX200 companies achieved this objective in December 2019.

Board and chair

The board must ensure that proper accountability systems and mechanisms are in place and that shareholders are kept informed in accordance with the entity’s continuous disclosure obligations. The chair’s role is to ensure that appropriate board structures and procedures are in place. The general view in Australia is that the roles of CEO and chair should remain separate.

The board should comprise a majority of independent non-executive directors and must maintain oversight of the CEO and senior management.

Delegation

Subject to the company’s constitution, directors may delegate their powers and are responsible for a delegate’s exercise of power unless he or she reasonably believes after proper inquiry that the delegate will comply with the director’s duties and is reliable and competent.

In circumstances where a market announcement was ‘a key statement in relation to a highly significant restructure’ and where management has brought the matter to the board, none of the directors are entitled to ‘abdicate responsibility by delegating his or her duty to a fellow director’. In this regard, non-executive directors also cannot avoid liability by pleading reliance on management or expert advisers.

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11 Corporations Act 2001 (Cth) Section 201A.
12 ASX Listing Rules (as at 22 January 2020) r 4.10.3.
14 ibid, Recommendation 1.5.
15 ibid, Recommendations 1.6 and 1.7.
16 ibid, Recommendations 2.1, 4.1, 7.1 and 8.1.
17 ibid, Recommendation 1.5.
20 ibid, Recommendation 2.4.
21 Corporations Act 2001 (Cth) Section 198D.
There is a core, irreducible requirement for directors to take all reasonable steps to be in a position to guide and monitor the company.23

Board committees perform a critical role in determining matters where executive directors are faced with a conflict of interest24 and assist directors to obtain the information required to discharge their duties, including to challenge information or senior management, or both. As noted in the Final Report, ‘[t]he task of the board is overall superintendence of the company, not its day-to-day management.’25 It is a requirement for listed entities to have nomination,26 audit,27 risk28 and remuneration committees.29

During takeover transactions, committees should only comprise directors not associated with the counterparty to the takeover and the establishment of an independent takeover committee may be required.30

iv Remuneration

It is expected that listed entities will remunerate fairly and responsibly.31 ACSI notes that non-executive directors should generally only be remunerated by way of reasonable fixed fees, and should not include variable remuneration (which may include short-term (i.e. annual payment in cash or securities) and long-term (i.e. options or securities-based) incentives) which may be more appropriate for executive directors.32

For listed companies, remuneration reports are required to be adopted by shareholders at every AGM.33 Voting on the resolutions to the report and the operation of the ‘two strikes’ rule is a mechanism for shareholders to hold the board accountable for excessive remuneration where more than 25 per cent of the votes cast by shareholders at the AGM are against remuneration reports in consecutive years.34 If this occurs, shareholders must then be asked to vote on a spill motion. Shareholders can also use this mechanism to express dissatisfaction with other governance and performance issues.

23 Australian Securities and Investments Commission (ASIC) v Healey (2011) 196 FCR 291.
33 Corporations Act 2001 (Cth) Section 300A.
34 Corporations Act 2001 (Cth) Section 250U.
v Directors

In Australia, there are federal and state laws that impose liability on directors and senior managers for corporate breaches of laws other than the Corporations Act, including environmental, health and workplace safety laws and securities and competition laws. Directors must:

a. exercise their powers and discharge their duties with a reasonable degree of care and diligence;\(^\text{35}\)
b. act in good faith in the best interests of the company or for a proper purpose;\(^\text{36}\)
c. not misuse their position or improperly use information obtained from their position as director to obtain an advantage for themselves or a third party or to cause detriment to the company;\(^\text{37}\) and
d. prevent the company from trading while insolvent.\(^\text{38}\)

Companies often create a conflicts of interest policy as a ‘best-practice defence’.\(^\text{39}\) Directors’ duties must be observed carefully, as the consequences of breaching duties can be severe. There are legal protections available to directors in certain circumstances, including:

a. the business judgement rule: when directors are making a ‘business judgement’ and in doing so:
   • are acting in good faith and for a proper purpose;
   • do not have a material personal interest in the matter;
   • inform themselves to the extent they reasonably believe to be appropriate; and
   • rationally believe that the judgement is in the best interests of the company;

b. directors will meet the requirement of exercising due care and diligence both under the Corporations Act and the common law; and

c. reliance on information and advice: directors are entitled to rely on information or professional or expert advice from an employee, professional adviser or expert, another director or officer, or a board committee, provided the reliance was made in good faith, and after the director has made an independent assessment of the information or advice.

The purpose of the business judgement rule is to recognise that directors are expected to take advantage of business opportunities and engage in responsible risk taking. In practice, the rule has fallen short of this goal as it has not alleviated directors’ concerns about liability. The ability to rely on information and advice has been diluted by courts postulating ‘core irreducible duties’ in certain areas. The Centro case requires directors to personally be financially literate and to understand the AASB accounting standards.

Other protections such as constitutional indemnities and insurances including directors and officers liability insurance are also commonly relied on in Australia. Additional duties may arise for directors of responsible entities, directors of life companies,\(^\text{40}\) superannuation

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\(^{35}\) Corporations Act 2001 (Cth) Sections 180 (in the case of a listed company) and 601FD(1)(b) (in the case of a listed trust).

\(^{36}\) Corporations Act 2001 (Cth) Section 181.

\(^{37}\) Corporations Act 2001 (Cth) Sections 182 and 183.

\(^{38}\) Corporations Act 2001 (Cth) Section 588G.

\(^{39}\) James Dunn, ‘Managing conflicts of interest’ (1 August 2017) Company Director Magazine.

\(^{40}\) Australian Securities and Investments Commission (ASIC) v Hellicar (2012) 247 CLR 345.
trustees and authorised deposit taking institutions (ADIs). In addition to these duties, the Listing Rules impose continuous disclosure obligations. A company’s obligation to continuously disclose market sensitive information is considered by the ASX to be critical to the market staying informed. Accordingly, directors should give due consideration to the company’s communications strategy and market announcements or otherwise risk personal liability. This is reflected by the breach of directors’ duties found by the High Court of Australia in the case of *James Hardie Industries Limited*.41

The role of an audit committee is to assist the board to discharge its duties in respect of the entity’s financial performance, reporting and management.42 The *Centro* case raised the bar; directors must apply their own minds to, and review carefully, the financial statements and directors’ report.43 Directors must ensure that the CEO and CFO provide a declaration stating that financial records have been properly maintained and that the financial statements give a true and fair view and comply with accounting standards.44

vi Appointment, nomination, term of office and succession

The CGPR stipulate a detailed process for the nomination and election of directors to the board of a listed entity. Candidates must have the requisite skills, capacity and experience to ensure that their duties can be discharged and that they can provide effective leadership to act in the best interests of the company. Nomination committees should be formed to provide recommendations to the board based on objective criteria, such as the CGPR.45

Generally, a company’s constitution outlines the appointment process for directors. However, Listing Rule 14.4 provides that a director of a listed company must not hold the position of director without re-election past the third AGM following their appointment or three years after their appointment.46 While some bodies call for annual re-election of directors,47 staggered board re-election is commonly adopted in Australia. If a director serves a period of 10 years or more, the director’s independence may need to be considered.48

Ongoing board succession processes ensure that board composition reflects an appropriate balance of skill, experience and subject matter expertise. This is often overseen by the nomination committee.49

41 *Australian Securities and Investments Commission (ASIC) v Healey* (2011) 196 FCR 291.
43 *Australian Securities and Investments Commission (ASIC) v Healey* (2011) 196 FCR 291.
46 ASX Listing Rules (as at 22 January 2020) r 14.4.
III DISCLOSURE

Public companies are subject to a range of periodic reporting and continuous disclosure obligations, as well as disclosure rules for specific one-off events, mandated by the Corporations Act and Listing Rules. Circumstances in which the disclosure of information is mandated under the Corporations Act and Listing Rules include the following:

a periodic financial reporting;
b specific disclosures with respect to changes to fundraising, corporate control transactions and other changes to a company’s capital structure; and
c timely or continuous disclosure of price sensitive information in relation to a company’s securities.\(^{50}\)

In particular, persons who, together with their associates, have relevant interests in voting shares representing 5 per cent or more of the votes in a listed company must disclose details of their relevant interest. If a person’s relevant interest changes to below 5 per cent he or she ceases to have a substantial holding. If he or she makes a takeover bid, disclosure must also be made.\(^{51}\)

The Corporations Act also requires a director of a listed public company to provide the ASX with details of his or her relevant interests in any securities of the company or a related body corporate within 14 days of his or her appointment (other than reappointment at the same meeting), the company’s listing and any change in the director’s interests.\(^{52}\) A listed entity must provide the same information to the ASX within five business days of these events, and when a director ceases to be a director.\(^{53}\)

These disclosure obligations are supported by prohibitions on market misconduct, including insider trading, misleading and deceptive conduct, and other forms of market manipulation. In addition, shareholders are entitled to particular information when a general meeting is convened for certain purposes (e.g. to obtain shareholder approval for a related party transaction).

Listed companies are required to satisfy half-yearly and annual financial reporting obligations, each requiring preparation and lodgement of the following reports:\(^{54}\)

a a financial report, comprising audited financial statements and notes to those statements, prepared in accordance with Australian accounting standards;
b a directors’ report, which must include, amongst a range of other things, specific commentary regarding the company’s operations and business, as well as a remuneration report detailing the remuneration of directors and key management personnel; and
c an auditor’s report, obtained from the company’s independent auditor.

\(^{50}\) Mark Blair and Ian Ramsay, ‘Mandatory Corporate Disclosure Rules and Securities Regulation’ in Gordon Walker, Brent Fisse and Ian Ramsay (eds), Securities Regulation in Australia and New Zealand (LBC Information Services, 2nd ed, 1998) 55, 55-56.

\(^{51}\) Corporations Act 2001 (Cth) pt 6A.1.

\(^{52}\) Corporations Act 2001 (Cth) ss 205F, 205G, 300(11) and (12).

\(^{53}\) ASX Listing Rules (as at 22 January 2020) r 3.19A.

\(^{54}\) Corporations Act 2001 (Cth) ch 2M.
This information is typically provided in the form of an annual report, which listed companies must provide to shareholders each financial year by the earlier of 21 days before the company’s AGM (where the reports must be laid before the meeting) or four months after the end of the financial year.

According to guidance recently published by ASIC and the AASB with respect to effective disclosure, the focus of regulators and the market on climate-related financial risk disclosures is expected to heighten in the 2020 financial year. This follows the introduction of legislation requiring companies with a minimum annual turnover of A$100 million to report on the risks of modern slavery and actions taken to address such risks within their supply chains and operations.

Complementing periodic reporting, the continuous disclosure regime imposed by the Listing Rules requires a listed entity to immediately disclose to the ASX, once an entity becomes aware of ‘any information concerning it that a reasonable person would expect to have a material effect on the price or value of the entity’s securities’ – commonly referred to as ‘price sensitive’ or ‘material information’. The Listing Rules contain the following exception to the continuous disclosure obligation where one or more of the following five situations applies:

- it would be a breach of a law to disclose the information;
- the information concerns an incomplete proposal or negotiation;
- the information comprises matters of supposition or is insufficiently definite to warrant disclosure;
- the information is generated for the internal management purposes of the entity; or
- the information is confidential and the ASX has not formed the view that the information has ceased to be confidential; and
- a reasonable person would not expect the information to be disclosed.

The continuous disclosure obligation is reinforced under the Corporations Act, which prescribes an offence for a listed company that fails to comply with its continuous disclosure obligations where the information in question is both market sensitive and ‘not generally available’. To assist with satisfying its continuous disclosure obligations, a listed company will usually adopt a continuous disclosure policy, as encouraged by the CGPR.

Recent years have seen significantly increased shareholder class action activity for breach of continuous disclosure obligations, particularly in cases of downgrades to earnings forecasts previously disclosed by companies or reflecting market consensus.

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57 ASX Listing Rules (as at 22 January 2020) r 3.1.

58 ASX Listing Rules (as at 22 January 2020) r 3.1A.

IV CORPORATE RESPONSIBILITY

The year 2019 brought unprecedented change to the landscape of Australian corporate responsibility in the wake of the Banking Royal Commission, the introduction of laws and regulations that impact the internal culture and values of an organisation, and heightened public scrutiny on corporate ethics.

In response to this, Australian boards have had to adapt and adopt significant internal changes to promote proper corporate responsibility.

i Embedding the appropriate culture

Traditionally, legislation and standards regulated Australian companies’ behaviour and external transactions. In 2019 Australian law makers and regulators increasingly sought to regulate the ‘interior’ of Australian organisations by seeking to impact organisational culture, values and intentions. In addition to requirements to publicly report environmental and social risks in their business, including climate risks and modern slavery practices, companies are also now subject to comprehensive whistleblowing protection legislation as a further safeguard for corporate ethics.

To address this evolving legislative environment and to meet rising community expectations of corporate behaviour, boards must continually assess organisational culture. Corporate responsibility is as much about policing conduct as it is facilitating a culture of ethical behaviour and decision-making. Reporting to boards must be as comprehensive as possible in relation to organisational conduct and culture.

Boards should encourage a culture that positively impacts on the interests of multiple stakeholders, including customers, employees, regulators and the community. Metrics should not be confined to financial targets; both qualitative and quantitative data sources need to be accessed to provide a holistic picture of the organisation’s impact on all stakeholders.

Boards must seek views from all organisational levels. Management behaviour must mirror the ‘tone at the top’, created by the board, for consistency of values and intentions throughout the organisation.

To operate effectively, Australian companies are recommended as often as reasonably possible to:

a assess their culture and governance;

b identify any problems with that culture and governance;

60 ‘A social licence: the future of business’, Transforming business with MinterEllison: ideas and challenges that are shaping our future (MinterEllison, 19 August 2019).

61 Modern Slavery Act 2018 (Cth); Treasury Laws Amendment (Enhancing Whistleblower Projections) Act 2019 (Cth).


c deal with those problems; and

d determine whether any changes made have been effective.

ii Listed entities

Entities listed on the ASX should instil and continually reinforce a culture across the organisation of acting lawfully, ethically and responsibly. The ASX encourages boards to approve the organisation’s statement of values and to hold senior executives accountable for imparting those values across the organisation. Listed entities are also recommended to have and disclose a code of conduct for directors, senior executives and employees and ensure that the board or a committee of the board is informed of any material breaches of that code.

ASX-listed entities must report against these recommendations and, to the extent that they have not adopted or implemented any recommendation, they must provide a detailed explanation as to the reasons that they have not.

While these recommendations and obligations apply only to listed entities, it has a cascading effect on corporate Australia and reflects the ASX’s view of the critical relationship that ethical and responsible culture has to good governance.

iii Management and reporting of non-financial risk

Heightened focus on corporate responsibility brings a commensurate need to properly address broad categories of risk. Historically, companies have focused on risks that directly affect financial performance, deprioritising other categories and sources of risk including legal noncompliance, dishonest and misleading conduct, and unfair customer treatment.

Boards need to increase attention to managing these ‘non-financial’ risks. This often requires an uplift in capability, frameworks and supporting systems.

In particular, Australian stakeholders, including institutional investors, credit ratings agencies and prudential regulators, now regard climate change as a significant economic and financial risk over both the long- and shorter-term. Such risks arise not only from the physical or ecological impacts of climate change, but associated economic transition risks and litigation exposures from both regulators and private parties. The recent bushfire crisis over the Australian summer has emphasised the reality of climate change risk in Australia. Proper reporting on these risks for listed entities has become a major focus of Australian corporate regulators.

65 Ibid, Recommendation 3.1.
66 Ibid, Recommendation 3.2.
67 ASX Listing Rules (as at 22 January 2020) r 4.7.
69 Ibid.
70 See, eg, ASIC’s update to ASIC Regulatory Guide 247 (Effective disclosure in an operating and financial review) to incorporate the types of climate change risk developed by the G20 Financial Stability Board’s Taskforce on Climate Related Financial Disclosures.
iv Remuneration and incentives

Australian companies must align the remuneration of their officers and employees to encourage the management of non-financial risks and to promote a compliance culture within the organisation. As noted in the Final Report, culture, governance and remuneration reinforce each other, for better or worse.

v Corporate responsibility and directors’ duties

It is accepted in Australia that the duty upon directors to discharge their powers and duties in good faith in the best interests of the corporation is not confined solely to the pursuit of maximising short-term financial returns for shareholders. On the basis that the interests of all stakeholders associated with the corporation converge in the longer term, boards are expected to focus on achieving long-term financial advantage. A company is more likely to obtain long-term financial advantage ‘if the entity conducts its business according to proper standards, treats its employees well and seeks to provide financial results to shareholders that, in the long run, are better than other investments of broadly similar risk’.

V SHAREHOLDERS

i Shareholder rights and powers

The Corporations Act grants powers to shareholders of listed companies to influence a board in a number of ways, particularly by granting shareholders the power to call or require the calling of shareholders meetings and propose members’ resolutions.

In most instances, the shares held in Australian listed companies are all of the same share class (usually ordinary class shares) and generally the only difference between shareholders is the number of shares held. Therefore, the powers and rights of each shareholder largely derive from the number of shares held.

The right of shareholders to require or call meetings is enshrined in sections 249D and 249F of the Corporations Act. Shareholders who hold at least 5 per cent of the votes that may be cast at the general meeting can request the directors of a company to call and hold a general meeting of shareholders. The Corporations Act imposes a number of requirements on the form of this request. Directors must call the meeting within 21 days of the request being given to the company and the meeting must be held no later than two months after the request is given to the company. Additionally, shareholders who hold at least 5 per cent of the votes that may be cast at a general meeting may directly call and arrange to hold a general meeting. As shareholder activism gains favour in Australia, use of this right to call a meeting by shareholders is becoming more prevalent.

Shareholders with at least 5 per cent of the votes that may be cast on the resolution or at least 100 members who are entitled to vote at a general meeting may also give a company

72 Corporations Act 2001 (Cth) s 181(1).
73 The Hon Justice Kenneth Hayne AC QC, Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry (Final Report, February 2019) 403.
74 ibid.
75 Corporations Act 2001 (Cth) Section 249D.
76 Corporations Act 2001 (Cth) Section 249F.
notice of a resolution that they propose to move at a general meeting.\textsuperscript{77} The Corporations Act sets out various requirements relating to the form of notice and to whom the notice must be directed. If a company has been given notice of a resolution under section 249N of the Corporations Act, the resolution is to be considered at the next general meeting that occurs more than two months after the notice is given.

Shareholders also have a variety of other rights and powers. In order to change or repeal its constitution, a company must pass a special resolution, which requires at least 75 per cent of the votes cast by shareholders at a general meeting to be in favour.\textsuperscript{78} Companies may also reduce their share capital by way of a share capital reduction or a share buy-back. A selective buy-back scheme, in which identical offers are not made to every shareholder, must first be permitted by a special resolution, which requires at least 75 per cent shareholder approval by votes cast.\textsuperscript{79} A selective reduction of capital must also be approved by a special resolution.\textsuperscript{80}

\section*{ii Shareholders' duties and responsibilities}

Shareholders are not subject to the duties outlined in the Australian corporate governance regulatory framework. Rather, shareholders, regardless of share class or number, may exercise certain rights and powers afforded to them by the Corporations Act, within the bounds of the company’s constitution. However, shareholders cannot act in an unfettered manner.

\section*{iii Shareholder activism}

In Australia, shareholder activism has evolved over the past decade from an occasional disruption to a real risk to be anticipated and managed by the board. Activist shareholders are typically institutional shareholders including superannuation funds, hedge funds, private equity investors and, increasingly, specialist activist funds (e.g., Manikay Partners’ intervention in the MYOB Group scheme of arrangement (2019)).

Australian shareholder activism can generally be classified under the following categories (or some combination thereof):

\begin{itemize}
\item[a] M&A activism – persuading the board to respond positively to a takeover proposal or other control transactions to spin-off divisions to unlock ‘hidden value’, divest of non-core businesses to eliminate a perceived ‘conglomerate discount’ or initiate a process to sell the company or put it into play;
\item[b] balance sheet or financial engineering activism – persuading the board to increase the gearing of the company to what is perceived to be a more optimal ratio, return excess capital to shareholders, reduce costs and focus on maximising return on invested capital; and
\item[c] governance activism – highlighting corporate governance lapses or invoking corporate governance ‘best practices’, sometimes this may be with a view to changing the composition of the board so that the new directors nominated by the activist can pursue M&A activism or balance sheet activism.
\end{itemize}

Shareholder activists may initially try to privately engage with boards to effect change. When this fails they may seek to take public action. Australia is a relatively friendly jurisdiction

\textsuperscript{77} Corporations Act 2001 (Cth) Section 249N.
\textsuperscript{78} Corporations Act 2001 (Cth) Section 136.
\textsuperscript{79} Corporations Act 2001 (Cth) Section 257D.
\textsuperscript{80} Corporations Act 2001 (Cth) Section 256B.
for shareholder activists due to a large number of shareholder protections enshrined in the Corporations Act and the risks and potential liabilities faced by directors. Some of the techniques that can be used by shareholder activists include:

- **Putting forward proposed shareholder resolutions** – shareholders of Australian listed companies who either alone or with other shareholders hold 5 per cent or more of the shares on issue can put forward shareholder resolutions for consideration at upcoming AGMs.

- **Calling an extraordinary general meeting to spill the board** – shareholders who meet the 5 per cent threshold described above can request the company to call a meeting to consider and vote on a board spill resolution. Alternatively, these shareholders may call and arrange to hold the meeting themselves, however, in this case they are responsible for the associated expenses.

- **Applying pressure in the lead up to voting a resolution by:**
  - buying further shares;
  - lobbying shareholders to vote in favour of (or against) a resolution;
  - applying to a court for an order to inspect company books and records; or
  - requesting access to details of proxy votes in advance of the meeting.

### iv Takeover defences

In Australia, change of control in public and listed companies is primarily affected by takeovers and schemes of arrangement. Schemes of arrangement are a court-based process which requires the support of the target company board to implement. Accordingly, the only practical way for a hostile bidder to obtain control of a public company is by way of a takeover bid.

In a takeover bid in Australia a target company has 14 days from when the bidder’s statement is sent to shareholders to send a target’s statement to shareholders. However, practically there may be more time to prepare a target’s statement as a bidder may take up to two months from a proposed off-market bid to send its bidder’s statement to shareholders.

In managing hostile takeovers, Australian boards can employ pre-emptive and reactive strategies.

- **Pre-emptive:**
  - monitoring the company’s share register;
  - maintaining current internal valuations so a board can objectively assess the merit of any takeover approach;
  - maintaining template market announcements, shareholder communications and target statements that can be quickly adapted and released; or
  - using convertible securities to create entrenched capital structure.

- **Reactive:**
  - persuading target company shareholders to reject the hostile bid;
  - persuading the hostile bidder to improve its offer price to a price at which the target’s board is prepared to recommend the offer to shareholders;
  - seeking a better offer from a third party, either by engaging with a ‘white knight’ competing bidder, or creating an auction for control between the two independent bidders; or
  - making an application to the Takeovers Panel, the primary forum for disputes relating to takeover bids in Australia until a bid period is ended. The Takeovers
Panel has broad powers, with its primary power to declare ‘unacceptable circumstances’ in the context of a takeover bid. Where the Takeovers Panel has made such a declaration it can make remedial orders to rectify the circumstances.

v Contact with shareholders
Shareholder communications are an integral part of the corporate governance framework in Australia as they not only enable boards and officers to gauge the shareholders but also provide a channel of communication with the broader shareholder base.

For public companies (listed or unlisted), these communications are typically facilitated through the forum of the AGM. Listed public companies are required under the CGPR to typically have an investor relations programme that is designed to facilitate effective two-way communication with the shareholders, involving scheduled and ad hoc interactions with institutional investors, retail investor groups, sell-side and buy-side analysts, proxy advisers and the financial media.81

VI OUTLOOK
The Banking Royal Commission and the APRA inquiry into the CBA has undoubtedly triggered a move towards greater regulation and more aggressive enforcement by regulators. The general public has become more wary of the potential for conflicts of interest to drive the wrong behaviours and create toxic cultures within many large financial services institutions.

ASIC has expressly adopted the ‘why not litigate’ approach that was recommended by Commissioner Hayne. The implementation of this trigger happy approach to litigation has produced significant changes in ASIC’s mentality and operation and arguably reduced levels of cooperation from businesses.82 Similar to the ACCC, ASIC has:

a demonstrated a deep lack of trust in big business, having watched the evidence unfold in the Banking Royal Commission – particularly in how big business was approaching its engagement with ASIC;

b embraced the explicit recommendations of the Banking Royal Commission to enforce the law and act on contraventions; and

c embraced collaboration with the government to give it the legislative powers and resources it believes is necessary to better do its job.

Through measures like the CCM Program and the Corporate Governance Taskforce, ASIC developed greater insight into the relationship between corporate values and misbehaviour by directors and officers. The connection between culture and corporate governance is often spoken about, but rarely understood.

Legislation in Australia has evolved so that it now regularly includes broad prohibitions and provides very specific and limited exceptions. This has been seen to result in an arms race between legislators and advisers seeking to find methods for creative avoidance. This has resulted in Australia’s current legal landscape – many areas of business are governed by arguably impenetrable or overly inclusive legislation that clearly imposes significant costs of compliance and additional risks on business. Given voluminous and arguably overbearing

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legislation, the lack of trust in business now seemingly entrenched in regulators (and
the community), regulators’ newfound or validated aggression and their desire to work
with government to toughen up the regulatory regime for business, you have a powerful
combination of factors to be considered by companies conducting business in Australia.

Commentators have begun questioning whether non-executive directors in fact need
to become executives to discharge their duties. For the foreseeable future, it is highly likely
Australian regulators will be aggressive, not just in their approach to enforcement but also in
their approach to government regulation.
Chapter 2

AUSTRIA

Martin Abram and Clemens Ph Schindler

I OVERVIEW OF GOVERNANCE REGIME

Austrian listed companies are incorporated in the form of a joint-stock corporation (JSC) or – less frequently – a European company, the Societas Europaea (SE). The most relevant sources of law for listed companies are:

a. the Stock Corporation Act or the Societas Europaea Act and the SE Regulation, which set forth the organisational framework for the company;

b. the Stock Exchange Act, which regulates disclosure obligations, as well as the rules on insider trading, market manipulation and directors’ dealings;

c. the Takeover Act, which sets forth the framework for public takeover bids;

d. the Commercial Code, which contains the applicable Austrian accounting rules;

e. the Accounting Control Act, which is aimed at ensuring that financial and other information published by listed companies complies with national and international accounting standards;

f. the (non-binding) Corporate Governance Code, which contains best practice rules and recommendations for listed companies; and

g. regulations and circulars by the Austrian Financial Market Authority.

As regards the Corporate Governance Code, it is principally non-binding and only applies to listed JSCs or SEs that have committed themselves to complying with the Corporate Governance Code; however, such a commitment is a prerequisite for entry to the prime market of the Vienna Stock Exchange.

Listed companies are subject to the supervision of the Financial Market Authority (in particular regarding insider trading, market manipulation and directors’ dealings), the Takeover Commission (regarding takeover bids) and the Austrian Financial Reporting Audit Panel (for audits pursuant to the Accounting Control Act, unless the audits are made by the Financial Market Authority).

1 Martin Abram and Clemens Ph Schindler are partners at Schindler Rechtsanwälte GmbH.
II CORPORATE LEADERSHIP

Most Austrian-based listed companies have a two-tier board structure (consisting of a management board and a supervisory board), even though the two-tier structure is only mandatory for JSCs – SEs may choose between a one-tier or two-tier structure. As there are only a few companies that have opted for a one-tier structure, the following overview will focus only on the two-tier structure.

i Board structure and practices

Management board

Role

The management board is responsible for managing the operations of the company, taking into account (as the Stock Corporation Act provides) the interests of the shareholders and the employees, and the public good. In performing its function, the management board is not subject to instructions by the supervisory board or the shareholders; however, certain decisions (such as the determination of business principles and the establishment or closure of business lines or production branches) and transactions (such as the sale or acquisition of shares or real estate, the granting and taking up of loans exceeding certain thresholds, investment above certain thresholds) are subject to the consent of the supervisory board. These consent requirements are based on the Stock Corporation Act, but can (and typically are) made more specific or be expanded in the rules of procedure for the management board or – less frequently for listed companies – in the articles of association. Certain transactions and decisions (e.g., acquisition of treasury stock, issuance of new shares or bonds, mergers, spin-offs or dissolution) require the prior consent of the shareholders’ meeting. Further, the management board may decide, or be required (see Section V.i), to ask the shareholders’ meeting for instructions on or approval of certain transactions.

Composition

According to the law, the management board can have one or more members. For certain regulated businesses (such as financial institutions or insurance companies), at least two members need to be appointed. In practice, listed JSCs have more than two members.

As a general rule, any two management board members together can represent the company, except if the articles of association allow for single signing authority and the appointment resolution bestows such single signing authority on a board member.

The signing authority of each board member is published in the Companies Register; in business dealings, third parties can rely on this information in the Companies Register (if acting in good faith), even if the management board members fail to comply with internal restrictions on their representation powers.

Chairperson

If two or more management board members are appointed, the supervisory board typically also appoints the CEO of the company as the chairperson of the management board. In the event of a tied vote, the chairperson has the deciding vote, except if the articles of association provide for otherwise. In addition to the specific tasks delegated to him or her by (typically) the by-laws, the chairperson of the management board also is responsible for the preparation, convocation and documentation of the meetings of the management board. However, the chairperson is not entitled to give instructions to the other board members.
Delegation of tasks and committees

Even though the Stock Corporation Act provides that the operations of a JSC are managed by the members of the management board collectively, it is customary (and recommended by the Corporate Governance Code) that the various members of the management board have specific areas of responsibility (i.e., they would each be responsible for certain departments). This allocation is established either in the articles of association or the by-laws of the management board (which are adopted by the supervisory board) or by the management board itself. Even when certain management tasks are allocated exclusively to certain management board members, the other management board members are still responsible for proper supervision of the due performance of these tasks. Certain tasks cannot be delegated to individual board members (such as decisions on the fundamental business policy of the company or the convocation of general meetings where the company’s equity is equal to or lower than its stated capital). It is not customary for the management board to establish committees. It has to be noted that the allocation of tasks among the members of the management board does not dispense the management board members from keeping themselves informed of (and obtaining information about) developments and activities in areas allocated to other management board members or from acting if they perceive any deficits.

Supervisory board

Role

The supervisory board is tasked with the control and monitoring of the management board. In performing its functions, the supervisory board is not bound to instructions by the management board or the shareholders. The supervisory board can request reports of the management board and can inspect the books and records of the company. The supervisory board needs to hold a meeting at least every calendar quarter.

Composition

According to law, the supervisory board must have at least three and no more than 20 members elected or nominated by the shareholders. For listed companies, the Corporate Governance Code recommends a maximum of 10 supervisory board members elected or nominated by the shareholders.

Representation of the company

Neither the supervisory board nor any of its members are entitled to represent the company, except in connection with the conclusion, amendment or termination of directors’ agreements and legal proceedings of the company against the members of the management board. In such cases, the supervisory board is represented by its chairperson.

Chairperson

The supervisory board is required to elect from its members a chairperson and (at least one) vice chairperson. Even though this means that a representative delegated by the employees’ council could also be so elected, in practice these positions are predominately taken up by supervisory board members elected or nominated by the shareholders. Besides certain administrative duties (such as the convocation of the supervisory board meetings, the preparation of the agenda), the chairperson of the supervisory board also takes the chair
of the (annual or extraordinary) general meeting, is entitled to demand a report from the management board even without the support of other supervisory board members, and is required to sign certain applications of the company with the Companies Register.

**Delegation of tasks and committees**

The Stock Corporation Act allows for (and in one case mandates), and the Corporate Governance Code recommends, the establishment of committees of the supervisory board. Each committee established must have at least three members. For listed companies, the establishment of an audit committee is mandatory; in addition, the Corporate Governance Code recommends the creation of a nomination and compensation committee. The mandatory audit committee is basically responsible for the monitoring of the company’s accounting process, the internal control systems and the audit of the financial statements (and related documents), including the preparation for their approval. The audit committee is also tasked with proposing the auditor of the company to the general meeting and monitoring the independence of the appointed auditor. One member of the audit committee must be a person with special knowledge and practical experience in finance and accounting and reporting. If established, a remuneration and nomination committee is responsible for negotiating and approving directors’ agreements, determining general policies for the remuneration of the management board, and preparing nominations for the appointment of new management board members (including successor planning) as well as for the appointment of new supervisory board members.

**Remuneration of the management board**

The remuneration of the members of the management board is decided by the supervisory board (or the compensation committee, if any).

In determining the compensation for a management board member (which includes payments, bonuses, stock options or benefits in kind), several aspects have to be taken into account. The compensation should be appropriate both for the tasks allocated to the board member and the overall economic situation of the company. The compensation should include a fixed and variable component; as regards the criteria for the variable component, they should be chosen so as not to incentivise inappropriate risks, and should not exclusively be based on financial figures. If management board members receive stock options, the vesting period must not be less than three years, and vesting should be based on long-term, measurable and sustainable criteria. There should be contractual safeguards implemented in the directors’ agreements to claw back variable payments in the event a pay-out decision was based on obviously false data. Finally, a management board member should not be entitled to redundancy payments if his or her director’s agreement is terminated on important grounds; in addition, redundancy payments should in any case be no more than two years’ salary. The same principles also apply to senior management.

For listed companies, new rules on the remuneration of the management board were introduced in the legislation implementing the EU Shareholder Rights Directive. In particular, these rules require the formulation of a general remuneration policy, which has to be put to a (non-binding) vote of the general meeting every four years.

The remuneration of the management board has to be published both in the annual financial statements (on an aggregate basis) as well as in the annual remuneration report.
Remuneration of the supervisory board

The remuneration of the members of the supervisory board is either determined in the articles of association of the company or (more frequently) by a decision of the general meeting. Also, the remuneration for supervisory board members of listed companies must be included in the remuneration policy. Remuneration for supervisory board members in Austria is relatively low compared with other countries (although a certain recent trend to raise remuneration can be reported), and usually comprises a base remuneration (which is typically higher for the chairperson, vice chairperson and committee members) and a meeting fee (which will only be paid to members attending a meeting). The remuneration of each supervisory board member is published annually in the remuneration report of listed companies. While it is possible for supervisory board members to participate in stock option programmes, the Corporate Governance Code does not recommend such participation.

Board and company practice in takeovers

When faced with a takeover offer, the boards of the target company are bound by the objectivity principle set forth in the Takeover Act. This means that they are barred from taking any measures that would prevent the shareholders from taking a free and duly informed decision about the offer.

Both boards of a JSC are required to publish a reasoned statement regarding the offer, which is subject to a mandatory review by an independent expert. The statement has to contain, inter alia, an assessment of:

a. the consideration offered by the bidder;
b. the expected consequences of a successful takeover for the company, its employees (in particular the terms and conditions of employment and working conditions) and creditors;
c. the strategic goals pursued by the bidder; and
d. information on whether the members of the management board and the supervisory board recommend shareholders to accept the offer.

If such a recommendation is deemed by the boards to be inappropriate, they are obliged to state arguments both for and against the acceptance of the offer.

Directors

Management board

Appointment

Members of the management board are appointed by the supervisory board for a period of up to five years. It is possible (and customary) to renew an appointment, with the renewed term again being subject to the five-year limit. According to the Corporate Governance Code, the supervisory board is required to define profiles for the respective management board members and an appointment procedure as a basis for the appointment decision. Since 1 January 2018, supervisory boards of listed companies and unlisted companies with more than 1,000 employees have to have at least 30 per cent female members (subject to certain
exceptions). Supervisory board members may not be appointed management board members of the same company; for certain regulated industries, candidates for the management board need to fulfil additional criteria or pass a fit and proper test before they can be appointed.

**Dismissal**

Members of the management board can be dismissed by the supervisory board before the end of a term only on important grounds, in particular, if a board member has materially breached his or her duties, if the board member is unable to properly carry out his or her duties (both for health reasons or lack of required skills or knowledge) or if the shareholders adopt a vote of no-confidence (except if the vote was adopted for obviously inappropriate reasons).

**Duties**

As a general matter, the members of the management board of an Austrian company owe to the company (not the shareholders or any other constituents) the following duties:

\( a \) the duty of care, requiring members to exercise the level of care of a proper and diligent person in similar circumstances (which includes an obligation to be reasonably informed about areas allocated to other board members and articulate any concerns they may have);

\( b \) the duty of loyalty, requiring members to act in the best interest of the corporation (taking into account the interest of its shareholders and employees as well as the public good) and not in their own interest;

\( c \) the duty of confidentiality; and

\( d \) a duty not to compete.

**Liability**

Wilful or negligent failure to comply with these duties results in the personal liability of the responsible board members, unless the general meeting has lawfully approved a measure resulting in damage. As regards the duty of care, not every decision or transaction that results in a loss for the company is automatically deemed a breach. Based on the business judgement rule, which was recently included in statutory law, management board members are allowed to assume risks provided that those risks are not outside normal business practice or inappropriate given the economic situation of the company. A JSC may waive or settle its damages claims with an affirmative shareholder vote of 80 per cent after five years, or even before that with an affirmative vote of all shareholders.

**Conflicts of interest**

As a general rule, management board members shall take their decisions without being influenced by their own interests or the interests of controlling shareholders. If a management board member has a material personal interest in transactions of the company (or its subsidiaries) or other conflicts of interest, he or she has to inform the supervisory board and the other management board members without delay. Any transactions of the company with a management board member (or its related persons or entities) need to be on arm’s-length terms, have to meet industry standards and have to be approved by the supervisory board. For other conflicts of interest not involving such transactions, the management board member should not participate in any discussions of the management board concerning the topic,
and should be excluded from any information flow in this respect. There are also statutory provisions and recommendations in place aimed at preventing (or limiting) potential conflicts of interest: The aforementioned non-compete duty prohibits management board members from operating other businesses, becoming supervisory board members in non-affiliated companies, becoming general partners of (entrepreneurial) partnerships or engaging in business transactions in the company’s field of business, except – in each case – with the consent of the supervisory board. The Corporate Governance Code also recommends that management board members should not sit on more than four (or chair more than two) supervisory boards of non-affiliated companies, even with the supervisory board’s approval. The Corporate Governance Code also recommends implementing similar restrictions for senior management. Finally, management board members are prohibited from becoming supervisory board members of the same company for a period of two years following the end of their term on the management board, unless they were nominated by shareholders holding more than 25 per cent of the total voting rights of the company.

Conflicts of interest may also arise in connection with any dealings by a management board member (or its related persons or entities) in the stock of the company (director’s dealings). In this respect, management board members are required to report such trades to the Financial Market Authority within five banking days; the Financial Market Authority maintains a publicly accessible database for the reported trades. Additionally, listed companies are required to issue internal compliance guidelines that deal with the handling of, and the monitoring of access to, potential insider information. These internal compliance guidelines and their implementation are monitored by the Financial Market Authority.

**Supervisory board**

**Appointment**

Members of the supervisory board are elected by the shareholders’ meeting, usually at an annual general meeting; the articles of association can also bestow nomination rights to shareholders (for up to one-third of the total number of supervisory board members). Supervisory board members are elected for a limited term, which has to expire – by law – at the latest with the completion of the fifth annual general meeting after their election. Re-elections are permissible. No term limitations are mandated for nominated supervisory board members. The Stock Corporation Act provides that shareholders should consider the following aspects when electing supervisory board members:

- the professional and personal qualifications of the candidates;
- whether the composition of the supervisory board (and the respective professional qualifications of its members) adequately accounts for the structure and business of the company; and
- diversity, appropriate age structure and internationality as well as the appropriate representation of women on the supervisory board.

Persons already holding multiple supervisory board positions (i.e., 10 positions in non-listed companies or eight positions in listed companies (with positions as chairperson counting as double), or a combination thereof) may not run for further supervisory board positions in listed companies. In addition, persons holding managerial functions in the JSC or any of its affiliated companies may not be elected to the supervisory board.

The employees’ council (if established) of a listed JSC is entitled to delegate employee representatives to the supervisory board. For every two supervisory board members elected or
nominated by the shareholders, the employees’ council can delegate one representative. If the number of supervisory board members elected or nominated by the shareholders is uneven, the number of representatives to be delegated by the employees’ council is calculated based on the next highest even number (e.g., if there are seven supervisory board members elected or nominated by the shareholders, the employees’ council can delegate four representatives).

**Dismissal**
Members of the supervisory board can be removed from office during their term of appointment by a shareholders’ resolution that requires a 75 per cent majority of the votes cast, unless the articles of association provide otherwise. Members of the supervisory board delegated by the employees’ council can be recalled at any time by the employees’ council.

**Duties**
Members of the supervisory board are in principle subject to the same duties as members of the management board, which are scaled down to reflect that fact that the supervisory board members are mainly tasked with the monitoring and review of the conduct of the management board. One exception is that supervisory board members are not explicitly prohibited from competing with the company. Any actual competition will, however, always be scrutinised under the duty of loyalty to the company.

**Liability**
The liability standards applicable to management board members also apply to supervisory board members.

**Conflicts of interest**
In principle, the provisions regarding conflicts of interest of management board members also apply to supervisory board members, except that supervisory board members are not subject to a statutory non-compete obligation. In this respect, the Corporate Governance Code recommends supervisory board members not to assume functions on the boards of competing companies. As a precautionary measure, candidates running for a position on a supervisory board have to present to the general meeting information on all positions they hold and all other circumstances that could give rise to potential conflicts of interest. Supervisory board members are also subject to the same directors’ dealing requirements as members of the management board, and are typically also covered by the internal compliance guidelines of the company.

**III DISCLOSURE**
Listed companies are required to prepare (consolidated) annual financial statements and half-yearly financial reports. In most cases, listed companies also prepare quarterly reports. The financial statements and reports have to be prepared in accordance with IFRS. In addition, listed companies also have to prepare stand-alone annual reports in accordance with Austrian GAAP.

The annual financial statements need to be audited by an independent auditor or auditing firm appointed by the general meeting based on a recommendation of the audit
committee. Any auditor or auditing firm proposed as the annual auditor has to provide a statement to the general meeting confirming that neither of the statutory exclusion reasons apply, and disclosing its business dealings with the company during the past business year.

Listed companies also have to publish a corporate governance report together with the annual financial statements. Besides certain information on the organisation, composition and remuneration of the boards of the company, and on the measures to promote appropriate representation of women on the management board, the supervisory board and in executive positions, the report in particular has to include a corporate governance statement. This statement has to include information whether – and if so, in what form – the company deviates from any comply or explain rules of the Corporate Governance Code.

Additionally, listed companies and their directors are subject to various disclosure requirements under the Stock Exchange Act, such as publication of directors’ dealings and ad hoc disclosure. Ad hoc disclosure is aimed at preventing insider trading, and requires listed companies to publish without undue delay any non-public information relating to the issuer that could have a material impact on the market price of the securities of the company. Shareholders of listed companies are faced with a statutory obligation to notify the company, the Stock Exchange and the Financial Market Authority if their shareholdings (whether direct or indirect) exceed certain thresholds (starting at 4 per cent, unless the articles of association lower the threshold to 3 per cent). Finally, the Beneficial Owner Register Act, requires listed and non-listed companies to maintain a register of its ultimate beneficial owners, and report the identity of its ultimate beneficial owners electronically to a newly established corporate service portal overseen by the Federal Ministry of Finance. This register is accessible for:

a. public authorities;

b. credit and financial institutions, attorneys, auditors, tax advisers, as well as certain other professionals for the purpose of performing know your customer checks; and

c. any other person or entity that can prove a legitimate interest in connection with the prevention of money laundering or terrorist financing;

Since January 2020, also the general public can obtain extracts containing select information from the register. Starting in November 2020, the documents required for the identification and verification of beneficial owners can be submitted by professional representatives on behalf of their clients to the portal as a ‘compliance package’ on a voluntary basis. These materials can then be used by obligated parties for the fulfilment of due diligence obligations.

IV CORPORATE RESPONSIBILITY

Corporate responsibility and compliance have become important topics in recent years, in particular in connection with corruption scandals and highly publicised criminal proceedings against management board members regarding anticompetitive practices. As a consequence, listed companies have introduced compliance codes and installed compliance officers. These compliance codes materially influence the daily corporate life and usually emphasise the tone from the top principle. Many companies have also established whistle-blowing hotlines. Since the entry into force of the EU General Data Protection Regulation and the implementing legislation in May 2018, the establishment of such hotline no longer requires the consent of the Data Protection Authority; however, its implementation and operation require the conclusion of a shop agreement with the employees’ council.
V SHAREHOLDERS

i Shareholder rights and powers

Shares in JSCs have – except for limited exceptions provided by law – equal rights (i.e., equal voting, dividend and information rights). The Stock Corporation Act expressly prohibits golden shares (i.e., shares with multiple or disproportionately higher voting rights). However, it is permissible for the articles of association to introduce maximum voting rights or staggered voting rights. In addition, a JSC may issue non-voting preferred shares based on a shareholder resolution, whereas the nominal amount of such non-voting shares may not exceed one-third of the aggregate stated capital of the JSC.

Shareholders in listed companies have no direct influence on the management board and are not permitted to issue instructions or otherwise direct the management board. Their influence is limited to certain reserved decisions, which fall into the following three categories:

a certain decisions (such as changes in the articles of association, appointment of supervisory board members, appropriation of distributable profit, acquisition of treasury stock, issuance of new shares or bonds, mergers, spin-offs or dissolution) require a shareholder resolution by operation of law;

b the management board or the supervisory board may put certain decisions to the shareholders if no agreement can be reached among the boards; and

c there is an obligation to put certain fundamental business decisions to a vote by the shareholders; this requirement is not based on a statutory obligation, but on a doctrine developed by the German Supreme Court, which was also followed by the Austrian Supreme Court.

Other rights of the shareholders include the right to demand a convocation of a shareholders’ meeting and the right to put certain matters on the agenda of a convened meeting (which requires the requesting shareholders to hold at least 5 per cent of the stated capital, unless the articles of association provide for a lower threshold) and the right to demand a special audit of the company (which requires the requesting shareholders to hold at least 10 per cent of the stated capital). All shareholders are entitled to request information on all items on the agenda in a shareholders’ meeting, and are furthermore entitled to request that any of their statements (and the responses thereto) are recorded verbatim in the meeting minutes.

Dissenting shareholders are entitled to object to resolutions passed at a shareholders’ meeting and can (if an objection was made) file for annulment or rescission of a resolution with the competent court in limited circumstances.

ii Shareholders’ duties and responsibilities

Shareholders of a JSC (both controlling and minority) are subject to a fiduciary duty requiring them not to directly cause harm to the company in the exercise of their shareholder right. Shareholders’ resolutions breaching fiduciary duties may be contested and may give rise to damages claims against the JSC and its shareholders. Shareholders breaching this fiduciary duty may also be subject to damages claims by the company.

There are no specific duties for institutional investors above the general duties applicable to all shareholders. There is also no code of best practice for shareholders of Austrian listed companies.
iii Shareholder activism
Shareholder activism has traditionally not played an important role in Austria (unlike Germany). More recently, Austrian activist shareholders as well as the Austrian Shareholder Association have taken a more active role in representing free float shareholders.

Proxy battles do occur, but not very frequently. The most recent example was an (initially unsuccessful) proxy battle at the general meeting of Conwert SE, where minority shareholders tried to have two candidates elected to the board. This attempt was initially thwarted as the chair of the meeting decided to suspend the voting rights of certain shareholders owing to alleged violations of the Takeover Act, which led to the election of two candidates proposed by the board. The minority shareholders then initiated legal proceedings aiming at the annulment of this election. Ultimately, the minority shareholders prevailed, as Conwert decided not to continue its objection against the legal proceedings.

As previously mentioned, shareholders in Austrian listed companies have no direct say as regards the remuneration of the directors, with the exception of stock option or transfer schemes, the introduction of which requires a vote of the shareholders. Since June 2019, shareholders also get the opportunity to vote on the general remuneration policy of listed companies; however, such vote is only a recommendation and non-binding.

iv Takeover defences
Listed companies have several options to implement general takeover defences prior to the launch of a hostile takeover bid, such as including provisions in the articles of association limiting the maximum voting rights per shareholder, introducing transfer restrictions (to the extent possible) as well as the staggered appointment of supervisory board members. The shareholders’ meeting can, however, also decide to install a provision in the articles of association that provides for the non-applicability of such defence provisions upon the formal announcement of a takeover bid. Furthermore, the articles of association can also provide for a reduction of the threshold for mandatory offers to less than 30 per cent, which can also act as a deterrent.

If a hostile takeover is expected, but not yet announced, additional measures can be employed, such as capital increases, purchase of treasury stock and reorganisations. The Takeover Act limits potential defence measures by the corporate bodies of listed companies once the listed company becomes aware of a hostile takeover bid. From this point on, the corporate bodies may only take measures aimed at preventing the success of the hostile takeover bid with the prior approval of the shareholders’ meeting (except for the search of a white knight). However, any defence actions by corporate bodies have to be in line with the standard duty of care applicable to them; otherwise they can be held liable for any damage incurred.

v Contact with shareholders
Under Austrian law, listed companies are in general required to treat all shareholders in an equal manner. Therefore, as a matter of principle, any direct communication with shareholders is a sensitive matter and is only possible if an objective justification exists. Such an objective justification may exist, for example, if a listed company intends to acquire a business owned by one of its shareholders. In such cases, it is standard market practice to insist on a comprehensive secrecy agreement (which sometimes includes standstill covenants). In such cases, listed companies typically impose internal restrictions so that only a limited
number of persons (usually the management board, selected senior managers) have access to such information. If the transaction requires the consent of the supervisory board, the matter is sometimes delegated to a committee of the supervisory board to ensure confidentiality.

Selective meetings with individual shareholders usually take place during corporate roadshows or capital market days. Additionally, several Austrian listed companies do schedule investors’ calls, typically around the publication of financial information by the company. To avoid allegations of unequal treatment of shareholders, the presentations given during such events and recordings of investor calls are made publicly available on the website of the company.

Recent legislative changes introduced in the implementation of the EU Shareholder Rights Directive will make it easier for listed companies to get information on their shareholders as, from September 2020 on, intermediaries such as banks and brokers will be obliged to inform a listed company about the identity of shareholders holding more than 0.5 per cent of the shares or voting rights.

VI OUTLOOK

On a general level, it has to be noted that business decisions of the management boards of listed companies continue to be scrutinised more and more under criminal law aspects. Judgments of the Austrian Supreme Court have resulted in a high degree of uncertainty about whether certain business decisions could constitute fraud or embezzlement, and further clarifications by the courts would be welcome. On the other hand, the inclusion of the business judgement rule gives management boards more robust grounds for defence.
I OVERVIEW OF GOVERNANCE REGIME

Belgian corporate governance practices for listed companies have been partially codified in the new Belgian Code on Companies and Associations (BCCA) and the Royal Decree of 29 April 2019 implementing the Code on Companies and Associations. The BCCA contains mandatory provisions on, for example, the establishment of an audit and risk committee and a remuneration committee, requirements with respect to the determination and disclosure of executive remuneration, requirements for independent directors and the issuance of a corporate governance statement. Compliance with these mandatory provisions is ensured, for the most part, by the listed company’s auditor and the Financial Services and Markets Authority (FSMA). For existing companies, associations and foundations, the BCCA is applicable since 1 January 2020. The articles of association of existing legal entities must be brought into line with the BCCA no later than 1 January 2024.

In addition, other financial and ad hoc disclosure requirements for listed companies are laid down in the Royal Decree of 14 November 2007 on the obligations of issuers whose financial instruments are admitted for trading on a regulated market. Listed companies must also disclose the transparency notices they receive from their shareholders pursuant to the Act of 2 May 2007 and the Royal Decree of 14 February 2008.

The other main source of guidance with respect to corporate governance for Belgian listed companies is the Corporate Governance Code 2020 (2020 Code), published on 5 May 2019. The 2020 Code is an initiative of the non-governmental Corporate Governance Committee, composed of representatives from bodies such as the FSMA (formerly the CBFA), the Federation of Belgian Enterprises, Euronext Brussels, the Belgian Institute of Chartered Accountants and the Central Economic Council. The FSMA monitors compliance by listed companies with the comply or explain principle applicable under the 2020 Code. The 2020 Code applies to companies incorporated in Belgium whose shares are admitted to trading on a regulated market (i.e., listed companies) as defined by the BCCA.

By Royal Decree of 12 May 2019, the 2020 Code was named the mandatorily applicable corporate governance code for certain listed Belgian companies, more specifically those whose shares are listed on a regulated market (in Belgium or another member state of the European Economic Area (EEA)) or whose shares are traded on a multilateral trading facility (MTF)
(i.e., in Belgium, mainly the Vrije Markt/Marché Libre and Alternext), provided they have other securities listed on a regulated market (e.g., in Belgium, Euronext Brussels or the market for derivatives of Euronext Brussels). The BCCA obliges such companies to adhere to the provisions of the 2020 Code or to explain in their corporate governance statement, which forms part of the annual report, why they have not done so, assuming, of course, that the provisions in question are not of mandatory application. This means that listed companies are not required by law to comply with the 2020 Code, but they are required to explain why they have not done so. In addition, compliance is highly recommended since it gives credibility and authority to listed companies. Non-compliance can adversely affect public opinion about a company.

The Belgian corporate governance rules have thus evolved over the past few years from soft law (the Lippens Code and the 2009 Code) to hard law (BCCA), and the process is ongoing. The 2020 Code is a thorough review of the 2009 Code, incorporating numerous regulatory changes, both on European and Belgian level. European legislation is often the driving force behind Belgian legislative proposals.

This chapter, however, focuses only on the corporate governance rules applicable to listed companies.

II CORPORATE LEADERSHIP

i Board structure and practices

In Belgium, listed companies usually take the form of a limited company (NV/SA). Companies with other corporate forms can be listed if their shares are freely transferable.

The basic governance structure of an NV/SA is a one-tier model, whereby the board of directors holds all powers except those specifically reserved by law or the articles of association to the general meeting of shareholders. Limitations on the powers of the board of directors set out in the articles of association are not enforceable against third parties and have internal effect only. The board of directors should be composed of at least three directors (or two if there are only two shareholders in the company and the articles of association so provide).

The BCCA allows the board of directors to delegate the daily management of the company, and the external representation of the company in that respect, to another person, who may also be a director. Limitations on the powers of the daily manager, either set out in the articles of association or adopted by the board of directors, are not enforceable against third parties and have internal effect only. This person is generally known as the CEO, managing director or general manager. The board of directors still has authority to take decisions with respect to the delegated powers.

The BCCA allows companies to adopt a two-tier governance model if their articles of association provide for this possibility. This model already existed under the old BCC where the board of directors delegated (some of) its powers to a management committee, except those reserved to it by law and general corporate policy.

3 Publieke Veilingen/Ventes Publiques, Trading Facility and Easynext, organised by Euronext Brussels, and MTS Belgium, MTS Denmark and MTS Finland, organised by MTS Associated Markets SA, are also MTFs but are rarely used.

4 Since most listed companies in Belgium take the form of an NV/SA, the governance structures of other corporate forms are not discussed in this chapter.
Under the new regime, however, the intention has been to create a more clearly delineated two-tier system using two newly introduced legal bodies: a management board and a supervisory board.

The supervisory board is responsible for general policy, overall strategy and supervision of the management board. It holds the same powers that would otherwise be held by the board of directors within the one-tier model, provided these powers are reserved to it pursuant to the BCCA. The supervisory board has at least three members, who reach decisions collegially. Its members are nominated and dismissed by the general assembly.

The management board exercises all management powers, provided these have not been reserved to the supervisory board in accordance with the BCCA. Similar to the supervisory board, the management board is a collegial body consisting of a minimum of three members. Their nomination and dismissal is controlled by the supervisory board.

The aim of the two-tier model is to entrust exclusive powers to the aforementioned bodies through the articles of association and the law. This duality is further highlighted by prohibiting overlapping membership. The CEO, for instance, cannot be a member of the supervisory board, let alone vote in it. Very few listed companies have adopted a two-tier governance model.

The BCCA has also introduced the possibility of a sole director model. This means that there is no longer a collegial body at board level. Instead, all powers are held by one single director, which can be a natural or a legal person. For listed companies, however, only an NV/SA with a collegiate board is eligible to be a sole director.5

The most common governance model in listed companies is the one-tier model, whereby the board of directors delegates daily management to the CEO, who is assisted by a number of executive managers (who may or may not be directors), for example, the chief operating officer, the chief financial officer or the chief legal officer. Together, they constitute the company’s executive management. The powers of the executive managers, other than the CEO, to represent the company for the purposes of certain acts, derive from a special authorisation granted by the board of directors or the CEO.

In addition to representation by the CEO (for matters of daily management) and other executive managers (within the limits of their specific powers), the company can also be represented externally by a majority of its directors acting jointly, or by a person appointed to this end in the articles of association (often two directors acting jointly, the chair, the CEO, etc.). The company will be bound by any acts taken or obligations incurred by these individuals, even if the internal decision was not taken by the correct corporate organ (unless the counterparty acted in bad faith). Quantitative limitations (e.g., representation for transactions with a value of up to €100,000) on the external representation powers of the CEO or the persons appointed in the articles of association to represent the company are not enforceable against third parties and have internal effect only.

In the above model, the board of directors still has all powers to manage the company, but daily management is mostly handled by executive management. The board of directors, in actuality, mainly supervises the management of the company. The 2020 Code indicates that the board of directors is responsible for determining the company’s values and strategy, its risk appetite and key policies. As a guideline, the board of directors should ensure that the necessary leadership and human and financial resources are available for the company to meet its objectives. In translating values and strategies into key policies, the board should

5 See: Article 7:101 Section 1 par. 3.BCCA.
pay attention to corporate social responsibility, gender diversity and diversity in general. In addition to general corporate policy, the board of directors should at least, in the context of its supervisory role:

a review the performance of executive management and the realisation of the company’s strategy;

b approve the framework of internal control and risk management proposed by the executive management and review the implementation of this framework;

c take all necessary measures to ensure the integrity and timely disclosure of the company’s financial statements and other material financial and non-financial information in accordance with applicable law;

d ensure that the company presents an integrated view of the company’s performance in its annual report and that it contains sufficient information on issues of societal concern and the relevant environmental and social indicators;

e ensure that there is a process in place for monitoring the company’s compliance with laws and other regulations, as well as for the application of internal guidelines relating thereto; and

f approve a code of conduct (or several activity-specific codes of conduct), setting out the expectations for the company’s leadership and employees in terms of responsible and ethical behaviour. The board should monitor compliance with such code of conduct at least on an annual basis.

The 2020 Code states that the board of directors should take decisions in close consultation with the CEO regarding the structure of executive management and should determine the powers and duties of the executive managers. A mention to this effect should be included in the terms of reference of the board and of executive management. The board should ensure that executive management is able to perform its responsibilities and duties. In view of the company’s values, risk appetite and key policies, executive management should have sufficient latitude to propose and implement corporate strategy. Executive management should, at least:

a be entrusted with the running of the company;

b put internal controls in place (i.e., systems to identify, assess, manage and monitor financial and other risks) without prejudice to the board’s supervisory role that are based on a framework approved by the board of directors;

c present to the board complete, timely, reliable and accurate financial statements, in accordance with the applicable accounting standards and company policies;

d prepare the company’s required disclosure of the financial statements and other material financial and non-financial information;

e present the board with a balanced and understandable assessment of the company’s financial situation;

f provide the board of directors with all information necessary in a timely fashion for the board of directors to carry out its duties; and

g be responsible and accountable to the board for the discharge of its responsibilities.

The 2020 Code states that the board of directors should be composed of both non-executive directors, who do not participate in the company’s daily activities, and executive directors, who belong to executive management and thus participate in the company’s daily activities. The majority of the board should be made up of non-executive directors, at least three of whom are independent based on the criteria set out in Clause 3.5 of the 2020 Code. In
Article 7:87, the BCCA limits its own definition of independent to not having a relationship with the company or an ‘important’ shareholder that would jeopardise independence. The board’s composition should ensure that decisions are taken in the company’s interest and should reflect gender diversity and diversity in general, as well as complementary skills, experience and knowledge. No individual or group of directors should dominate the board’s decision-making process, and no individual should wield excessive decision-making powers.

In January 2011, the Corporate Governance Committee, which issued the 2020 Code, issued an additional recommendation providing that within seven years, at least 30 per cent of board members should be women.

Article 7:86 of the BCCA stipulates that at least one-third (rounded to the nearest whole number) of the board of directors of companies whose securities are listed on a regulated market should be of a different gender to the other members. If the required number of directors of the less-represented gender is not met, the next appointed director should be of that gender. If not, the appointment shall be deemed null and void. The same holds true if an appointment would cause the number of directors of the other gender to drop below the required minimum.

For companies whose securities are admitted to trading on a regulated market for the first time, the requirement should be met as from the first day of the sixth financial year after the admission.6

If the required quota is not met, a board that meets the quota should be composed at the next general meeting. Otherwise, any financial or other benefit to which the directors are entitled by virtue of their office shall be suspended. These benefits will be reintroduced once the board meets the gender diversity requirement.

The 2020 Code assigns a clear role to the chairperson of the board of directors. The chair and the CEO should not be the same person, and there should be a clear division between duties related to the running of the board (chair) and the management of the company’s business (CEO). This division of responsibilities should be clearly established, set out in writing and ratified by the board. The chair should cultivate a close relationship with the CEO, providing support and advice while fully respecting the CEO’s executive responsibilities. As a guideline, the chair should stimulate effective interaction between the board and executive management. The chair is responsible for leading the board of directors and can be entrusted by the board with specific responsibilities. The chair should take the necessary measures to foster a climate of trust within the board, contribute to open discussion, allow constructive dissent and ensure support for the board’s decisions. Once decisions are taken, all board members should be supportive of their execution. The chair7 determines the agenda for board meetings, after consultation with the CEO and the company secretary, and ensures that procedures relating to preparations for board meetings, deliberations, the adoption of resolutions and the implementation of decisions are properly followed. The chair, or as the case may be the chair and the CEO, is responsible for ensuring that the directors receive accurate, timely and clear information before the meetings and, where necessary, between meetings. All directors should receive the same information.

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6 Applicable as from the first day of the first financial year starting after 14 September 2011.
7 In a two-tier structure, the chair of the supervisory board and the CEO should set the agenda of their respective board meetings, in consultation with the company secretary.
The BCCA obliges companies whose shares are listed on a regulated market to set up a remuneration committee composed of non-executive directors, a majority of whom should be independent. The members of the remuneration committee must possess the requisite level of expertise in the area of remuneration policy. The chair of the board of directors or another non-executive director should head the remuneration committee. The remuneration committee should meet at least twice a year and whenever it deems necessary to carry out its duties. The remuneration committee should report regularly to the board of directors on the exercise of its duties. The CEO should attend meetings of the remuneration committee when the committee is discussing the remuneration of executive management. The remuneration committee should submit proposals to the board of directors on the company’s remuneration policy and on the individual remuneration of directors and executive managers and, where appropriate, on proposals to be submitted by the board of directors to the general meeting of shareholders (i.e., proposals on the remuneration of directors). The remuneration committee also prepares the remuneration report that forms part of the annual report and provides explanations on this report at the annual general meeting of shareholders.

The 2020 Code provides for practically the same requirements with respect to the remuneration committee. The 2020 Code further specifies, however, that the remuneration committee should have at least three members should advise the board on the adoption of a remuneration policy. In addition to a remuneration committee, the BCCA obliges companies whose securities are listed on a regulated market to set up an audit and risk committee composed of non-executive directors. At least one member should be independent, and at least one member of the committee must possess the requisite level of expertise in the area of accountancy and audits. The audit and risk committee should report regularly to the board of directors on the exercise of its duties and in any case when the board draws up the annual accounts, consolidated annual accounts and short-form financial statement (intended for publication). The audit and risk committee should:

a. monitor the financial reporting process;
b. monitor the effectiveness of the company’s internal control and risk management systems;

8 There is an exception for small listed companies that meet the criteria set out in Article 7:100 Section 4 BCCA. In that case, no remuneration committee need be set up. Rather, the board of directors will perform the duties of the remuneration committee and should have at least one independent member. If the chairperson of the board is an executive director, he or she cannot chair board meetings when the board is acting as the remuneration committee. There is also an exception for public undertakings for collective investment with variable capital, within the meaning 3, 5° of the Act of 3 August 2012 on institutions for collective investments that meet the conditions of Directive 2009/65/EC and for companies whose business is the issuance of asset-backed securities, as defined in Article 2(5) of Commission Regulation (EC) No. 809/2004.

9 In accordance with the requirements set out in Clause 3.5 of the 2020 Code and Article 7:87 BCAA.

10 There is an exception for small listed companies that meet the criteria set out in Article 7:99 Section 3 BCCA. In that case, no audit committee need be set up. Rather, the board of directors will perform the tasks of the audit committee and should have at least one independent member. If the chairperson of the board is an executive director, he or she cannot chair board meetings at which the board is acting as the audit committee. There is also an exception for public undertakings for collective investment with variable capital, within the meaning 3, 5° of the Act of 3 August 2012 on institutions for collective investments that meet the conditions of Directive 2009/65/EC, and for companies whose business is the issuance of asset-backed securities, as defined in Article 2(5) of Commission Regulation (EC) No. 809/2004.

11 In accordance with the requirements set out in Clause 3.5 of the 2020 Code and Article 7:87 BCAA.
monitor the internal audit (if any) and its effectiveness;

monitor the audit of the annual and consolidated accounts, including the follow-up of any questions and recommendations by the statutory auditor; and

review and monitor the independence of the statutory auditor, in particular with respect to the provision of additional services to the company.

The statutory auditor should report to the audit and risk committee on key matters arising from the audit of the annual accounts, in particular on material deficiencies in the internal control of the financial reporting process. The statutory auditor shall confirm to the audit and risk committee annually, in writing, its independence from the company, inform the audit committee on an annual basis of any additional services provided to the company, and examine, together with the audit committee, the risks to its independence and the safeguards to be implemented to minimise these risks. The audit committee should make a proposal on the appointment or reappointment of the statutory auditor or external auditor, which should be placed on the agenda of the general meeting.

The audit and risk committee meets whenever it deems it necessary to perform its duties properly and at least four times a year. The audit and risk committee reports regularly to the board of directors on the performance of its duties, and in any case when the board of directors prepares the annual accounts, the consolidated annual accounts and, where appropriate, the abbreviated financial statements intended for publication.

The audit and risk committee should review the specific arrangements for raising concerns – in confidence – about possible improprieties in financial reporting or other matters. The audit committee should agree on arrangements whereby staff may inform the chair of the audit committee directly. If deemed necessary, arrangements should be made for the proportionate and independent investigation of such matters and for the appropriate follow-up actions.

The 2008 financial crisis led to an animated debate on the (at times excessive) remuneration of directors and executive managers of Belgian companies. In an attempt to rein in the remuneration of directors and executive managers, several new provisions were adopted in 2010 and codified in the BCC and subsequently the BCCA.
As a general rule, the general meeting of shareholders has exclusive power to determine the remuneration of directors. The board of directors, in turn, determines the remuneration of executive management, unless the company’s articles of association provide otherwise. In listed companies, the articles of association sometimes provide that the shareholders’ general meeting determines the overall remuneration for the board of directors as a whole, while the board itself decides how to distribute this total amount among its members.

The BCCA stipulates that the remuneration of individual directors and executive managers shall be determined further to a proposal by the remuneration committee. The remuneration committee should also submit proposals on the company’s remuneration policy, which must be explained in the remuneration report that forms part of the board’s annual report. The general meeting of shareholders need not approve the remuneration policy per se in accordance with the BCCA, but does have the power to vote on the remuneration report in which the remuneration policy is described. There are no consequences, however, if the general meeting rejects the remuneration report. The remuneration report should also be provided to the works council or, in the absence thereof, the employee representatives on the committee for prevention and protection at work or, if there is no such committee, the trade union representatives.

If an executive manager receives variable remuneration (i.e., remuneration linked to performance), the criteria used to determine the remuneration should be set out in the contractual or other provisions governing the company’s relationship with the manager, and payment can only take place if these criteria have been met within the specified time period. If this is not the case, the executive’s variable remuneration cannot be taken into account to determine his or her severance package.

If the variable remuneration of an executive manager of a listed company makes up more than one-quarter of his or her annual remuneration, at least 25 per cent of the variable remuneration should be based on previously established and objectively verifiable performance criteria measured over a period of at least two years, and at least another 25 per cent should be based on previously established and objectively verifiable performance criteria measured over a period of at least three years, unless the articles of association provide otherwise or the general meeting of shareholders expressly consents to deviate from this rule.

Unless the articles of association provide otherwise or the general meeting of shareholders expressly agrees, shares shall only be finally acquired, and share options or any other rights to acquire shares shall only be exercisable, by a director or executive manager of a listed company after a holding period of at least three years is satisfied.

The general meeting of shareholders should also approve in advance any severance package agreed by the company with an executive manager if the severance pay amounts to more than 12 months’ remuneration, as well as any variable remuneration granted to an independent or non-executive director. If the severance package represents more than 18 months’ remuneration, a reasoned opinion from the remuneration committee is also required. Any such contractual provision that has not been approved by the general meeting.

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12 The Code 2020 provides that the remuneration policy should be submitted for approval to the shareholders’ meeting.
13 This rule applies to any agreements entered into or renewed as from 3 May 2010.
14 For non-executive dependent directors, this rule applies to any agreements entered into or renewed after 3 December 2011.
shall be deemed null and void. The proposal should also be notified to the works council or, if there is none, the employee representatives on the committee for prevention and protection at work or, in the absence thereof, the union representatives.

The aforementioned provisions of the BCCA are supplemented by the 2020 Code principles and best practices with regard to the level and structure of executive remuneration. The board should adopt a remuneration policy based on the advice of the remuneration committee in order to achieve the following objectives:

a. to attract, reward and retain the necessary talent;
b. to promote the achievement of strategic objectives in accordance with the company’s risk appetite and behavioural norms; and
c. to promote sustainable value creation.

The board needs to ensure that the remuneration policy is consistent with the overall remuneration framework of the company. The board can decide to submit the policy to the general shareholders’ meeting for approval ('comply or explain' principle of the 2020 Code). When a significant proportion of the votes have been cast against the remuneration policy, the company should take the necessary steps to address the concerns of those who vote against it, and consider adapting the policy.

Further to a special recommendation of the remuneration committee, the severance package can amount to 18 months’ fixed and variable remuneration. In any case, the severance package should not take into account variable remuneration or exceed 12 months’ fixed remuneration if the departing CEO or executive manager did not meet the agreed performance criteria. The 2009 Code also adds that the prior approval of the general meeting of shareholders is required for schemes that provide for the remuneration of executive managers with shares, options or any other right to acquire shares.

The 2020 Code further provides that the remuneration of non-executive directors should take into account not only their role as ordinary board members but also any specific positions they may hold, such as chair of the board, or chair or member of a board committee, as well as their resulting responsibilities and commitments in terms of time, and that non-executive directors should not be entitled to performance-based remuneration such as bonuses, long-term stock-based incentive schemes, or fringe or pension benefits. The 2020 Code also stipulates that non-executives board members should receive part of their remuneration in the form of shares in the company. These should be held until at least one year after the non-executive board member leaves the board and at least three years after the moment of award. However, no stock options should be granted to non-executive board members.

With regards to executive board members’ remuneration, the remuneration policy should describe the different components of and determine an appropriate balance between fixed and variable remuneration, and cash and deferred remuneration. The variable remuneration for the executive director should be structured to link reward to overall corporate and individual performance, and to align the interests of the executives with the sustainable value-creation objectives of the company. When the company awards short-term variable remuneration to the executive management, this remuneration should be subject to a cap.

Since the financial crisis, remuneration schemes for executives (such as stock options and incentive compensation) were deemed to be overly focused on short-term results. These additional requirements concerning the remuneration policy are a result of the 2020 Code’s broader emphasis on sustainable value creation and long-term growth.
ii Directors

The 2020 Code indicates that both executive and non-executive directors, regardless of whether the latter are independent or not, should exercise independence of judgement in their decisions. Directors should make sure they receive detailed and accurate information and should study this information carefully so as to acquire and maintain a clear understanding of the key issues relevant to the company’s business. They should seek clarification whenever they deem it necessary to do so.

Non-executive directors should be made aware of the extent of their duties at the time of their appointment, in particular the time commitment involved. They should not consider taking on more than five directorships in listed companies. Changes to commitments and the assumption of new commitments outside the company should be reported to the chairperson of the board as they arise.

Pursuant to the BCCA, a director can be either a natural person or a legal entity. In the latter case, a permanent representative should be appointed from among the entity’s shareholders, directors, members of executive management or personnel who is solely responsible for performing this office in the name and on behalf of the legal entity. The representative shall be liable for the performance of this office as if he or she had been appointed in his or her own name, notwithstanding the joint liability of the legal entity that is represented. The directors of autonomous governmental companies, public institutions and any legal entities over which the state exerts direct or indirect influence must be natural persons if they are remunerated for the directorship. Any payment to a legal entity, acting as director, in this case will be deemed null and void. A listed company that falls into any of the aforementioned categories (e.g., Proximus Group NV) must ensure that its remunerated directors are natural persons.

Directors cannot use the information obtained in their capacity as directors for purposes other than the exercise of their functions. They have an obligation to treat confidential information received in their capacity as directors with care.

Each board member should place the company’s interests above their own. The board members have a duty to look after the interests of all shareholders on an equivalent basis. Each board member should act according to the principles of reasonableness and fairness. Board members should inform the board of any conflict of interests that could in their opinion affect their capacity of judgement. In particular, at the beginning of each board meeting, board members should declare whether they have any conflicts of interests regarding the items on the agenda. When a board member takes a decision, he or she should disregard their personal interests. They should not use business opportunities intended for the company for their own benefit.

In the possible case of a conflict of interests, the board should, under the lead of its chair, decide which procedure it will follow to protect the interests of the company and all its shareholders. In the next annual report, the board should explain why they chose

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15 Holding directly or indirectly a majority of the share capital or voting rights, or having the power to appoint a majority of the members of the governing or executive body or to appoint a person entrusted with governmental supervision including by means of a contract.

16 Act of 19 December 2012 on the remuneration of employees and office holders in institutions of public utility, autonomous governmental companies and legal entities over which the state exerts, directly or indirectly, a preponderant influence, published in the Belgian State Gazette on 28 January 2013, entered into force on 1 August 2013.
this procedure. However, where there is a substantial conflict of interests, the board should carefully consider communicating as soon as possible on the procedure followed, the most important considerations and the conclusions. This disclosure should be effected through two different documents: the Corporate Governance Charter, posted on the company’s website, and the Corporate Governance Statement, a specific section of the annual report. The BCCA indicates a specific procedure to be followed when directors have a pecuniary conflict of interest with the company. In listed companies, a director with a conflict of interest of a financial nature cannot participate in the deliberations or vote on the decision in question.

The board should also take all necessary and useful measures to ensure effective and efficient execution of the Belgian rules on market abuse. It should draw up a set of rules (the dealing code) regulating transactions (and the disclosure thereof) in shares of the company or in derivatives or other financial instruments linked to shares carried out for their own account by directors or other persons with managerial authority.

Directors can be held liable for shortcomings in the performance of their official duties in accordance with the applicable statutory provisions. For a violation of the law or the company’s articles of association, directors can be held jointly and severally liable (unless they were not personally involved in the violation and brought it to the attention of the company’s shareholders at the first general meeting after becoming aware of it). In addition, directors can be held liable in a number of specific circumstances (e.g., in the event of bankruptcy, a conflict of interest or tax liability).

Although the term of office of a director in an NV/SA cannot exceed six years by law, the 2020 Code advises setting the maximum term of directors at four years. The 2020 Code indicates that the board of directors should establish nomination procedures and selection criteria for its members, including specific rules for executive and non-executive directors where appropriate. The nomination committee should lead the nomination process and recommend suitable candidates to the board. The board should then make appointment proposals or re-appointment proposals to the general shareholders’ meeting. For any new appointment to the board, the skills, knowledge and experience of existing board members and those needed on the board should be evaluated and, in the light of that assessment, a description of the role and skills, experience and knowledge should be prepared. For a director to qualify as independent, a number of criteria should be met.\(^\text{17}\)

### III DISCLOSURE

Companies whose securities are listed on a regulated market\(^\text{18}\) must publish annually and biannually\(^\text{19}\) a financial report. These listed companies are also obliged to publish ad hoc information if the information in question can be considered inside information. The annual financial report must contain:

\(\begin{align*}
\text{a} & \quad \text{the annual accounts and consolidated annual accounts;} \\
\text{b} & \quad \text{the board’s annual report (including the BCCA’s requirements, such as the corporate governance statement and remuneration report);} 
\end{align*}\)

\(^{17}\) Clause 3.5 of the 2020 Code and article 7:87 BCAA.

\(^{18}\) Some of the provisions also apply to companies whose securities or shares are listed on certain MTFs.

\(^{19}\) The latter is applicable to companies whose shares or debt instruments are listed.
a number of specific items that could have consequences in the event of a takeover\textsuperscript{20} (e.g., shareholder agreements or limitations on the transferability of shares and securities); the statutory auditor’s report; and a declaration by the issuer on the faithful nature of the accounts and report.

If the issuer decides to publish a communication between the end of the financial year and the publication of the annual financial report, this communication should meet certain criteria. The biannual financial report should contain interim financial statements and an interim report, information on external control and a declaration by the issuer regarding the faithful nature of the statements and report.

Listed companies are subject to other disclosure requirements with respect to any changes in the conditions, rights and guarantees linked to their securities, special reports of the board of directors and draft amendments to the articles of association. Listed companies should also disclose the transparency notices they receive from their shareholders in accordance with the Act of 2 May 2007 and the Royal Decree of 14 February 2008.

In addition to the disclosures set out above, the 2020 Code indicates that the company should draw up a corporate governance charter describing the main aspects of its corporate governance policy, such as its governance structure, the terms of reference of the board and its committees as well as other important topics. It should contain the minimum information set out in the 2020 Code. The charter should be updated as often as necessary to reflect the company’s corporate governance at all times. It should be made available on the company’s website and should specify the date of its most recent update.

The corporate governance charter should include at least:
\begin{itemize}
\item \textit{a} a description of the company’s governance structure and the terms of reference of its board of directors;
\item \textit{b} the policy established by the board for transactions and other contractual relationships between the company, including related companies, and board members and executive managers, to the extent not covered by the statutory provisions on conflicts of interest;
\item \textit{c} the measures taken by the company to comply with the Belgian rules on market abuse;
\item \textit{d} the terms of reference of each board committee;
\item \textit{e} the terms of reference of executive management;
\item \textit{f} the identity of major shareholders, with a description of their voting rights and special control rights, and, if they act in concert, a description of the key elements of existing shareholders’ agreements;
\item \textit{g} any other direct and indirect relationships between the company and its major shareholders; and
\item \textit{h} a statement that the company has adopted the 2020 Code as its reference code.
\end{itemize}

The board of directors should also include a corporate governance statement in its annual report, describing all relevant corporate governance events that have taken place in the past year. This statement should be included in a specific section of the annual report and should contain the minimum information set out in the 2020 Code. If the company has not complied fully with one or more provisions of the Code, it should explain its reasons for not doing so in its corporate governance statement (the comply or explain principle). The BCCA has made a corporate governance statement mandatory.

\textsuperscript{20} Act of 1 April 2007 on public takeover bids.
Pursuant to the BCCA, the following items should be disclosed in the corporate governance statement in the company’s annual report:21

a. a statement that the company has adopted the 2020 Code as its reference code and the place where the 2020 Code can be consulted, as well as relevant information on the corporate governance practices applicable in addition to the 2020 Code and the place where these can be consulted;

b. if the company does not fully comply with the 2020 Code, an indication of the provisions of the 2020 Code that were not complied with during the year and an explanation for the non-compliance;

c. a description of the main features of the company’s internal control and risk management systems in relation to financial reporting;

d. the shareholder structure on the closing date of the financial year as it appears from the notifications the company received;

e. the holders of securities to whom special control rights have been granted and a description of these rights;

f. any limitations on voting rights provided for by law or the company’s articles;

g. the rules for the appointment of directors and amendments to the company’s articles of association;

h. the powers of the board of directors, specifically the possibility to issue or purchase own shares;

i. a description of the composition and running of the board of directors and its committees. The 2009 Code adds that this description should include at least:
   • a list of all board members, indicating which are independent;
   • information on any directors who have ceased to meet the requirements for independence;
   • an activity report on board and board committee meetings, indicating the number of board committees;
   • information on meetings and the individual attendance records of directors;
   • a list of all members of board committees;
   • if applicable, an explanation as to why the appointment of the former CEO as chair is in the best interests of the company; and
   • a list of all members of executive management; and

j. an overview of the efforts taken to ensure that at least one-third of the members of the board of directors are of a different gender than the other members.

The BCCA indicates that the corporate governance statement should also include a remuneration report, prepared by the board of directors further to a proposal of the remuneration committee.

The following information should be disclosed in the remuneration report pursuant to the BCCA:

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21 These requirements are applicable to companies whose shares are listed on a regulated market. The requirements under (a), (b) and (i) are also applicable to companies whose securities, other than shares, are listed on a regulated market when their shares are listed on an MTF. The requirement set out under (c) is also applicable to companies whose securities are listed on a regulated market.
a description of the company’s internal procedure to develop a remuneration policy for directors and executive managers and set the level of individual remuneration for directors and executive managers;
b the remuneration policy for directors and executive managers containing at least the following items of information:
• the principles on which remuneration is based, including the relationship between remuneration and performance;
• the importance of the various components of remuneration;
• the characteristics of performance-based bonuses in the form of shares, share options or other rights to acquire shares; and
• information on the remuneration policy for the next two years. Furthermore, any significant changes to the remuneration policy since the end of the financial year should be expressly mentioned;
c the individual remuneration and other benefits granted directly or indirectly by the company, or another company that falls within the same scope of consolidation, to non-executive directors;
d the remuneration granted to executive managers who are also directors, but in that case only the remuneration received in their capacity as directors. It is unclear whether this information should be disclosed on an individual or collective basis;
e if the executive managers receive variable remuneration linked to the performance of the company, a company that falls within the same scope of consolidation as the company or a business unit of the company or their own performance, the criteria used to evaluate the achievement of the specified goals, the evaluation period and a description of the methods applied to verify whether the performance criteria are met. This information should be disclosed in such a way as to prevent the disclosure of confidential information about the company’s strategy;
f the remuneration and other benefits granted directly or indirectly to the CEO by the company or a company that falls within the same scope of consolidation, indicating:
• base remuneration;
• variable remuneration: for all incentives, the form in which the variable remuneration is paid;
• pension benefits: the amounts paid or the value of services provided during the financial year, per pension scheme, with an explanation of the applicable pension schemes; and
• other components of remuneration, such as the cost or monetary value of insurance coverage and fringe benefits, with an explanation of the details of the main components. Moreover, any significant changes to the remuneration policy since the end of the financial year should be expressly mentioned;
g on a collective basis, the remuneration and other benefits granted directly or indirectly to other members of executive management (excluding the CEO) by the company or a company that falls within the same scope of consolidation, with a breakdown between:
• base remuneration;

The term CEO can refer here to the main representative of the executive directors, the chairperson of the management committee, the main representative of ‘other leaders’ or the main representative of the persons entrusted with daily management of the company.
• variable remuneration: for all incentives, the form in which the variable remuneration is paid;
• pension benefits: the amounts paid or the value of the services granted during the financial year, per pension scheme, with an explanation of the applicable pension schemes; and
• other components of remuneration, such as the cost or monetary value of insurance coverage and fringe benefits, with an explanation of the details of the main components. In addition, any significant changes to the remuneration policy since the end of the financial year should be expressly mentioned;

\[ \text{for each executive manager (including the CEO):}\]
• the number and key features of shares, share options or any other rights to acquire shares granted, exercised or expired during the financial year;
• the provisions on severance pay; and
• whether the company has the right to recover any variable remuneration granted on the basis of incorrect financial data;

\[ \text{if an executive manager (including the CEO) leaves the company, the decision of the board of directors, further to a proposal of the remuneration committee, on whether the person is eligible to receive a severance package and the method used to calculate the severance pay.}\]

IV CORPORATE RESPONSIBILITY

The Belgian corporate governance rules do not specifically cover corporate responsibility, with the exception of Article 7:86 BCCA, which provides that at least one-third (rounded to the nearest whole number) of the board members of companies whose securities are listed on a regulated market should be of a different gender. The 2020 Code moreover mentions that the composition of the board should be determined so as to gather sufficient expertise in the company's areas of activity as well as sufficient diversity of skills, background, age and gender.

The 2020 Code is characterised by a stronger emphasis on sustainable value creation. This involves an explicit focus on the long term, on responsible behaviour at all levels of the company and on the permanent consideration of the legitimate interests of stakeholders. More explicit expectations are also formulated in terms of diversity, talent development and succession planning, and in relation to the company's annual reporting on non-financial matters.

Unlike financial institutions, which have specific rules on compliance policies and risk management, there are currently only a limited number of rules on compliance and risk management for listed companies. The main provision in the 2020 Code is that an independent internal audit function should be established, with resources and skills adapted to the company's nature, size and complexity, and that if the company does not have such a position, the need for one should be reviewed at least annually. The effectiveness of the internal control and risk management systems set up by executive management should be monitored by the audit committee at least once a year, with a view to ensuring that the main risks (including those relating to fraud and compliance with existing legislation and regulations) are properly identified, managed and disclosed in accordance with the procedures approved by the board.

The 2020 Code further indicates that the audit and risk committee should review the specific arrangements for raising concerns – in confidence – about possible improprieties.
in financial reporting or other matters. The audit and risk committee should agree on arrangements whereby staff may inform the chair of the audit committee directly. If deemed necessary, arrangements should be made for the proportionate and independent investigation of such matters, appropriate follow-up actions and schemes whereby staff can inform the chairperson of the audit committee directly. It should be noted that the rules on personal data protection should of course be respected when establishing a whistle-blowing scheme.

On 18 December 2014, the Institute of Internal Auditors Belgium and the Institute of Company Auditors, together with the Belgian Association of Listed Companies, issued further practical guidelines for an effective relationship between the audit committee, the internal auditor and the external auditor. These guidelines are supported by the Corporate Governance Committee.

V SHAREHOLDERS

i Shareholder rights and powers

The basic rule is that each share of the same value carries one vote. If the shares do not have the same value or if there is no value mentioned, the shares carry voting rights in proportion to the capital they represent, with the share with the lowest value carrying one vote. Fractions of votes are not taken into account.23

The BCCA introduces a new multiple voting rights regime. For listed companies, this regime is restricted and only offers the possibility for the issuance loyalty shares with double voting rights (i.e., maximum 2 votes per share). The BCCA utilises an ‘opt-in’ system for companies wishing to avail themselves of the loyalty share regime. One vote per share remains the default system.

It requires a change to the company’s articles of association, which needs to be approved by a two-thirds majority in the general assembly. Notably, this threshold is lower than the majority required for any other type of change to the articles of association.

The regime applies only to shares that have been registered in the name of the same shareholder for a continuous period of at least two years. The two-year period starts on the day on which the registered shares are registered, even if that registration took place before the statutory provision introducing the double voting right was adopted and before the company was listed. Every share that is converted into a dematerialised share or whose ownership is transferred loses double voting rights.

However, the transfer of shares as a result of succession, liquidation of matrimonial property regime or transfer, for pecuniary interest or free of charge, to the benefit of a beneficiary does not result in the loss of the double voting right and does not interrupt the required two-year period. The same applies in the event of transfer of shares between companies that have been controlled by the same shareholder (‘intragroup transfers’), or in the case of joint control, by the same shareholders, natural or legal persons, or between one of these companies and these controlling shareholders. Controlling shareholders often have the right to appoint a majority of the company’s directors, so that they de facto influence the management of the company.

Any powers not granted by law or the company’s articles of association to the general meeting of shareholders are reserved to the board of directors. A number of decisions are

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23 Except as mentioned in Article 7:155 BCCA.
reserved by law to the general meeting and cannot be delegated\(^{24}\) to the board of directors, such as approval of the annual accounts and discharge of the directors and statutory auditor, the final appointment of directors and the statutory auditor, the initiation of claims by the company against the directors, dissolution of the company, or a merger or a division. In 2010, a number of decisions relating to the remuneration of executive managers and directors were also made subject to the approval of the general meeting.

In general, a validly adopted decision of the general meeting of shareholders is, by law, binding on dissenting shareholders or shareholders who did not attend the meeting. Any party that can prove standing, including a shareholder, may, however, seek to invalidate a decision of the general meeting on account of:

a. a formal irregularity, provided this irregularity could have influenced the decision;

b. a violation of the procedural rules of the general meeting or the passage of a resolution on an item that was not on the agenda, provided there is fraudulent intent;

c. an ultra vires act or abuse of power;

d. the exercise of suspended voting rights, if this influenced the adoption of the decision; or

e. any other reason set out in the BCCA.

In addition, dispute resolution procedures are available to shareholders pursuant to which they can be obliged to sell their shares or purchase the shares of other shareholders in the event of a serious conflict among them (Articles 2:60 to 2:69 BCCA, or the involuntary dissolution of the company can be requested as a last resort (Article 7:230 BCCA).

One or more shareholders who, individually or collectively, hold 10 per cent of the share capital can also request the board of directors and the statutory auditor to call a general meeting. It is generally accepted that these shareholders also have the possibility to determine the agenda for the meeting. In accordance with Article 7:130 of the BCCA, shareholders holding at least 3 per cent of the share capital of a listed company have the right to submit proposals regarding items on the agenda and propose resolutions (this does not apply to meetings held on second call: i.e., meetings called because the required quorum was not met at the first meeting).

Shareholders also have the right to ask the directors (and the statutory auditor) questions during general meetings or in writing before the meeting (to be answered at the meeting). The directors or the statutory auditor, as the case may be, have a duty to answer these questions. There is, however, an exception to this rule: directors and the statutory auditor can refuse to answer a question if doing so would cause harm to the business of the company or violate their or the company's duty of confidentiality. Questions should relate to items on the agenda or to a report prepared by the board of directors or the statutory auditor. Questions on the same topic may be consolidated and answered together.

One or more shareholders owning at least 95 per cent of the securities to which voting rights are attached can initiate a squeeze-out to obtain 100 per cent of all voting securities or securities that allow their holders to acquire voting securities.

\(^{24}\) It is generally accepted that, in certain cases, some powers can be delegated.
ii Shareholders’ duties and responsibilities

The 2020 Code stipulates that, in companies with one or more controlling shareholders, the board should endeavour to have the controlling shareholders make considered use of their position and respect the rights and interests of minority shareholders. The board should encourage the controlling shareholders to respect the 2020 Code. In addition, it is recommended to enter into a relationship agreement with the majority shareholders.

The 2020 Code also specifically mentions some best practices with regards to institutional investors. Namely that the company should discuss with institutional investors the implementation of their policy on the exercise of institutional investors’ voting rights in the relevant financial year and ask institutional investors and their voting agencies for explanations on their voting behaviour.

Furthermore, the board should encourage shareholders, and in particular, institutional investors, to communicate their evaluation of the company’s corporate governance prior to the general shareholders’ meetings and at least through participation in the general shareholders’ meeting. The general rule of law that minority shareholders can seek to invalidate a resolution of the general meeting on the grounds of abuse of majority still applies, of course. Such a request must be made within six months of the time the resolution became enforceable against the shareholder or was notified to the shareholder. Pursuant to this principle, a resolution can be invalidated if the voting rights were not exercised in the company’s interest or the voter abused his or her rights, meaning the voting rights were exercised in an obviously unreasonable manner.

iii Shareholder activism

The general meeting of shareholders normally determines the remuneration of directors, but not of executive managers (except for the approval of severance pay in certain cases), so it does not have a complete say on pay. The general meeting of shareholders has the power to vote separately on the remuneration report in which the remuneration policy is described, but there are no legal consequences if it rejects the report.

If one or more shareholders do not agree with the board’s management of the company, there is judicial relief available to them.

The BCCA does not contain express rules on the invalidation of resolutions by the governing body (i.e., the board of directors); however, based on general rules of law, the courts tend to accept that resolutions of the board of directors can be declared null and void at the request of any interested party (including a shareholder).

In general, the grounds for invalidating resolutions of the board of directors are the following:

- a violation of the convocation formalities or procedural requirements for the meeting;
- b violation of rules of law or the articles of association (e.g., an ultra vires act);
- c resolutions that are obviously in violation of the company’s interests; and
- d resolutions adopted fraudulently.

Directors can be held liable, in accordance with the BCCA, for shortcomings in their management of the company, breach of rules of law or the articles of association and, in certain cases, violation of their general duty of care (the relevant standard is how a reasonably prudent director would have acted under the same circumstances). The general meeting of shareholders has the power to initiate proceedings on behalf of the company against one or more directors on the above-mentioned grounds. Such a decision should be approved by a
majority of votes cast. No action can be taken if the general meeting has already discharged the directors. There is also a possibility for minority shareholders to initiate the same proceedings on behalf of the company if they represent at least 1 per cent of the voting securities or hold at least €1.25 million of the company’s capital on the day the general meeting voted to discharge the directors. Minority shareholders that validly approved the discharge cannot bring such proceedings.

At the request of one or more shareholders holding at least 1 per cent of the total voting rights or securities that represent at least €1.25 million of the company’s capital, the court may also appoint, if there are indications that the interests of the company are seriously jeopardised or could be jeopardised, one or more experts to verify the company’s books and accounts and the actions of its corporate bodies.

In certain cases, one or more shareholders can also request the appointment of a temporary administrator to manage the company in lieu of the board of directors.

The BCCA provides for the possibility to solicit proxies for certain shareholder meetings. This solicitation should, however, comply with the requirements of the BCCA.25 A public solicitation of proxies (i.e., when advertisements or intermediaries are used or if more than 50 shareholders are targeted) should be approved by the FSMA and a number of requirements should be met.26 Proxy solicitation is mostly done by associations that defend (minority) shareholders’ rights.

Several associations that defend (minority) shareholders have campaigned to involve as many shareholders as possible in certain proceedings (e.g., the Fortis case in 2008, the case against the National Bank of Belgium in 2010, the Lernout & Hauspie case, the Madoff case and the Lehman Brothers case).

Pursuant to the Act of 28 March 2014,27 class actions are now possible in Belgium. However, certain limitations apply. A class action may only be brought against a company, by a consumer, and for breach of a contractual obligations or a specific law. Thus, shareholders who would like to introduce a claim against (current or former) directors cannot bring a class action under Belgian law. Therefore, only investors that take part in the proceedings against a company have the right to claim damages.

iv  Takeover defences

In general, the following measures can be taken by the target company to frustrate a takeover bid:

a Capital increase with the issuance of new shares: in principle, only the general meeting of shareholders is entitled to increase the company’s share capital, unless the board of directors has been authorised to do so (pursuant to the BCCA). However, such an authorisation is not valid in the context of a takeover bid, during which the board, in principle, cannot increase the share capital by means of a contribution in kind or in cash with the cancellation or restriction of the shareholders’ pre-emptive right. The general meeting may, however, authorise the board of directors to increase the share capital during the offer period by means of a contribution in kind or in cash with cancellation or restriction of the shareholders’ pre-emptive right, provided:

- the board has been specifically authorised to do so within the past three years;

25 Article 7:144 BCCA.
26 Article 7:145 BCCA.
27 Act of 28 March 2014 on class actions, Belgian State Gazette, 29 April 2014.
Belgium

- the newly issued shares are fully paid up;
- the number of new shares does not exceed 10 per cent of the number of existing shares; and
- the subscription price is at least equal to the offer price.

**b** Acquisition of own shares by the company: in principle, the general meeting of shareholders must authorise the acquisition of own shares by the company unless the board of directors has been authorised to do so (pursuant to the BCCA). However, such an authorisation is not valid during a takeover bid, as from the time the company is notified of the bid by the FSMA. As an exception to this rule, the board may acquire own shares to avoid serious, imminent harm to the company, provided the articles of association so allow (for a maximum period of three years). In this case, other conditions governing the acquisition of own shares also apply.

**c** Poison pill: in general, certain advance measures are available to protect companies against potential takeover bids. However, pursuant to Article 7:151 of the BCCA, only the general meeting of shareholders (thus not the board) can grant rights to third parties liable to affect the company's assets or give rise to a debt or obligation on behalf of the company, when the exercise of the rights depends on the launch of a takeover bid or a change in control. To be valid, the resolution to this effect should be filed with the clerk's office (of the competent court) prior to the FSMA's notification of the bid to the company. During the offer period, only the target company's (general meeting of) shareholders can take decisions or execute transactions that could have a significant impact on the composition of the company's assets or liabilities or enter into transactions without effective compensation. Such decisions and transactions cannot, in any case, be made subject to the outcome of the bid. Decisions that have been sufficiently implemented prior to receipt of the FSMA's notification can be further executed by the board; however, the FSMA and the bidder should be immediately notified of any such decisions, which should also be made public.

**d** Issuance of convertible bonds or subscription rights (warrants): these instruments may be issued by the general meeting of shareholders and may, for example, be convertible or exercisable upon the launch of a takeover bid. It is also possible to create a pyramidal ownership structure or issue share certificates.

As a general rule, in keeping with the Takeover Directive, the target company's board of directors must act in the company's interest. It may, therefore, seek out an alternative bidder (or white knight). Belgian law specifically provides that the target company need not inform the FSMA of the fact that it is searching for an alternative bidder (while it should inform the bidder and the FSMA of any decision in relation to the issuance of shares or that is liable to frustrate the bid).

Belgium has opted out of the provisions of the Takeover Directive aimed at restricting the use of defensive measures by the board of directors. Nevertheless, companies with their registered office in Belgium whose shares are (at least partially) listed on a regulated market may voluntarily include such restrictions in their articles of association (i.e., opt in).

In this regard, a company may provide in its articles of association that:

- during the offer period, the board of directors (or the body to whom the relevant powers have been delegated) may not take any action (other than seeking alternative bids) liable to result in frustration of the bid without the prior consent of the general meeting of shareholders;
any decisions taken prior to the offer period that are not yet fully implemented and that could frustrate the bid can only be further implemented with the prior consent of the general meeting of shareholders (except for those taken in the ordinary course of business);

c restrictions on share transfers expressed in the articles of association or a shareholders’ agreement shall not apply to the bidder during the acceptance period or after the bid if the bidder holds at least 75 per cent of the target’s share capital;

d restrictions on voting rights expressed in either the articles of association or a shareholders’ agreement shall not apply at a general meeting held during the offer period for the purpose of adopting measures to frustrate the bid or after the offer if, as a result of the offer, the bidder holds at least 75 per cent of the target’s capital; and

e provisions of the articles allowing a shareholder to appoint or remove a director shall not apply at the first general meeting called by the bidder after the offer, provided the bidder holds at least 75 per cent of the target’s capital as a result of its bid.

If the rights set out in (c) to (e) cannot be exercised, reasonable compensation should be paid to their holders.

The company may also stipulate in its articles of association that such provisions shall only apply to the extent the bidder or the company controlling the bidder is subject to the same restrictions on the application of defensive measures (the reciprocity rule).

The use of staggered boards as a takeover defence is not relevant in Belgium, as a director of a public limited company can always be removed at will by the general meeting of shareholders.

v Contact with shareholders

The basic rule is that the company should treat all similarly situated shareholders equally.

The Royal Decree of 24 November 2007 regulates periodic (annual and semi-annual) and occasional information (i.e., inside information) to be disclosed by listed companies, in addition to the mandatory disclosures set out in the BCCA (e.g., annual accounts and annual reports). Periodic information should be disclosed quickly and on a non-discriminatory basis so that it can reach as many people as possible, and disclosure should take place, insofar as possible, simultaneously in Belgium and other member states of the EEA. The company should use media that are expected to ensure disclosure in all member states of the EEA. Any inside information should be disclosed as simultaneously as possible to all categories of investors in the member states where the company has requested or agreed to trade its financial instruments on a regulated market.

The 2020 Code stipulates that the board should ensure an effective dialogue with shareholders and potential shareholders through appropriate investor relation programmes, in order to achieve a better understanding of their objectives and concerns. Feedback of such dialogue should be given to the board, on at least an annual basis. Individual meetings with institutional investors are also encouraged to receive explanations on their voting behaviour. It is indeed common practice for companies to hold individual meetings with their controlling

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shareholders, institutional shareholders, or both. However, the information disclosed in these meetings should be information that is already public or that is made public at the same time, to avoid the unequal treatment of shareholders.

Each director has a duty to keep information about the company confidential unless required to disclose it pursuant to a statutory or ethical duty. This duty also extends to companies’ shareholders. Some scholars argue, however, that directors representing a controlling shareholder can consult with that shareholder on decisions to be taken by the board of directors and the position the director will adopt in future deliberations, unless the board of directors specifically decides otherwise. This does not mean that the directors can inform the person they represent of information he or she can then use for his or her own purposes (e.g., to determine whether to sell or purchase shares).

In addition to this general duty of confidentiality, it is also forbidden for anyone in possession of inside information (e.g., directors) to, inter alia, disclose such information to anyone else except in the normal course of business or in the performance of his or her professional duties.

The general rule is that inside information should be immediately disclosed. However, a company can decide, at its own risk, to postpone the disclosure of inside information if the disclosure could harm the company’s legitimate interests, provided that the delay in disclosure does not mislead the public and confidentiality can be guaranteed. If inside information is disclosed in the normal exercise of the discloser’s profession, function or work, the information should simultaneously be made public unless the person to whom the inside information is disclosed is bound by a duty of confidentiality (e.g., the printer or the communications department). If the disclosure of inside information is postponed, the company should take the necessary measures to, inter alia, bar access to this information to all persons who do not need it to exercise their functions.

Based on the foregoing, in our opinion, directors cannot disclose inside information to a shareholder further to a confidentiality agreement. The only exception to this rule is if a third party or a shareholder requests information from the company to determine, for example, the appropriateness of making a public offer, in which case the board of directors can grant access to the information in question if it enters into a confidentiality agreement that includes a standstill clause (i.e., no transactions in the company’s shares until the information has been made public) and provided disclosure is in the company’s interest.

VI OUTLOOK

Belgian law has been subject to important changes over the past year. In addition, the Shareholders Rights Directive II has not yet been implemented in Belgian law. SRD II will have an additional material impact on the governance of listed companies.
I OVERVIEW OF GOVERNANCE REGIME

The corporate governance regime applicable to Brazilian listed companies is basically established by the Brazilian Corporation Law, the rulings issued by the Brazilian Securities Commission (CVM) and the listing rules issued by the Brazilian Stock Exchange (B3) to each of its listing segments.

Among the Law and rules mentioned above, it is important to highlight that CVM enacted a ruling in June 2017 – Ruling No. 586 – establishing the obligation for listed companies to disclose, on an annual basis, ‘Brazilian Corporate Governance Code: Listed Companies Information’, whereby companies shall indicate, in relation to each recommendation of the Corporate Governance Code, whether the company was compliant, and if not, provide an explanation for the non-compliance (i.e., a comply or explain approach). The Corporate Governance Code for listed companies was elaborated by GT Interagentes (the Interagents Working Group, which comprises 11 of the most important agencies concerned with the Brazilian capital markets) and issued on 16 November 2016.

Of the B3 listing segments, the Novo Mercado has the highest standards of corporate governance rules, followed by Level 2 and Level 1. There is also the BOVESPA MAIS, an organised over-the-counter market managed by B3 and created as a way for small and medium-sized companies to access the capital markets. It falls under the authority of CVM, a federal independent agency reporting to the Ministry of Finance that supervises and enforces listed companies’ compliance with the Corporation Law and the rules issued by CVM. This enforcement can result in the imposition of fines and restrictions on companies and their administrators.

B3 is responsible for supervising compliance with its listing rules and has the authority to impose on companies and their administrators contractual fines and other sanctions, such as suspension and exclusion from trading in shares in the B3 environment.

Most Brazilian listed companies do not have widely held stock, but in the past years there has been a trend for CVM to stimulate the participation of minority shareholders.

1 Marcelo Viveiros de Moura is a partner and Marcos Saldanha Proença is a counsel at Pinheiro Neto Advogados.
2 Federal Law No. 6,404, of 15 December 1976, as amended.
3 B3 SA – Brasil, Bolsa, Balcão is the current corporate denomination of the Brazilian Stock Exchange, which was formerly denominated BM&FBOVESPA SA – Bolsa de Valores, Mercadorias e Futuros until 10 May 2017.
4 The Brazilian Corporate Governance Code: Listed Companies Information must be disclosed within seven months of the end of each fiscal year.
in the governance of companies through the creation of a mechanism that enables all the shareholders to send their votes electronically prior to any shareholders’ meeting. In 2017, implementation of this mechanism was only mandatory for the main companies listed on B3; however, as from 2018 it became mandatory for all companies.

CVM has also enacted rules in recent years to improve the quality and amount of information that a listed company must disclose to its investors, including Ruling No. 480, published at the end of 2009, which created the reference form, a document containing very detailed information about the company that must be updated at least once a year; and Ruling No. 481 (published simultaneously with Ruling No. 480), which sets forth the mandatory information that must be disclosed by listed companies on an ordinary basis and prior to each shareholders’ meeting. Both these rules have already been adjusted to incorporate improvements that CVM considered necessary.

Furthermore, B3 launched the State-Owned Enterprise Governance Programme in September 2015 in response to the scandals and political use of state-owned companies by the government that were mainly revealed by Operation Car Wash, as from 2014. The Programme aims to restore investor confidence in state-owned companies (which are significant elements of the Brazilian capital markets) by enhancing the corporate governance rules of these companies in the following ways:

- through more clear disclosure of the company’s objectives;
- through the creation of mechanisms to remove administrators who divert company activities from the stated objective;
- through the establishment of detailed nomination criteria encompassing the qualifications and expertise of the administrators; and
- through the commitment of the public controlling shareholder to comply with corporate governance best practice.

As a result of the progressive reduction of the Brazilian basic interest rate that started in October 2016, when it was reduced from 14.25 per cent to 14 per cent, per year, and reached its lowest rate in the history in December 2019 (i.e., 4.5 per cent, per year), there has been a trend of investors who used to invest in fixed income products migrating to equity investments, in order not to reduce the return of their investments. Therefore, in 2019 an increase of the Brazilian capital markets transactions was verified, with five new companies being listed in addition to 37 follow-on offers.

The expectation is to have much more capital markets transactions in 2020 and, therefore, corporate governance should be a key element for those companies that will be trying to raise funds at the capital markets.

II CORPORATE LEADERSHIP

i Board structure and practices

Brazilian listed companies are managed by a board of directors and by an executive office. Brazilian companies can also install a fiscal board, which does not have the nature of a managerial body but rather of a supervisory body.
**Board of directors**

The board of directors is a decision-making body with authority to:

a. establish the company's business policy in general;
b. elect and dismiss officers;
c. set the duties and monitor the day-to-day managerial actions of officers;
d. express an opinion on any matters to be submitted to the shareholders; and
e. approve the implementation by the executive office of specific matters prescribed by law or under the company by-laws.

The authority of the board of directors established by the Corporation Law cannot be delegated to other bodies.

The Corporation Law sets out that the board of directors shall be composed of at least three members, who are not required to be Brazilian residents.

In the case of the companies currently listed on the Novo Mercado, considering the changes approved in its Listing Rules in 2017, they must observe the following rules:

- until the ordinary shareholders’ meeting that shall approve the financial statements related to the fiscal year 2020, the board must be composed of at least five members, and at least 20 per cent of the members must be considered to be independent; and
- as from the ordinary shareholders’ meeting that shall approve the financial statements related to the fiscal year of 2020, the board must be composed of at least three members, and at least two or 20 per cent of the members, whichever is greater, must be considered to be independent.

Companies that became listed on the Novo Mercado as from 2 January 2018 shall apply the rule provided in item (b) above, as from its listing.

In the case of the companies currently listed in the Level 2 segment, the board must be composed of at least five members and at least 20 per cent of the members must be considered to be independent.

The requirements for appointment to occupy a position on a board of directors are established in the Corporation Law. Generally, a director must be someone with an unblemished reputation who has not been convicted in an administrative or judicial procedure in relation to corporate crimes or irregularities.

The board of directors can create specific committees (e.g., compensation, related-party transactions and audit) to assist it in the management of the company. For the companies currently listed in the Novo Mercado segment, it will be mandatory to install an audit committee, statutory or not, as from the ordinary shareholders’ meeting that shall approve the financial statements related to the fiscal year 2020.

Listed companies must rotate their independent auditor every five years and must wait at least three years before rehiring the same auditor. However, if the listed company has installed a statutory audit committee, rotation can occur every 10 years instead of five.

In the event of a tender offer for the acquisition of the control of a listed company (Takeover TO), in principle, the board of directors of the listed companies is not under an obligation to make a statement as to whether or not it agrees with the terms and conditions of the Takeover TO.

If, however, the board of directors decides to make a statement on the Takeover TO, the statement must be disclosed to the market and must address such issues as provision of information on all aspects necessary to allow an informed decision by the investor, especially
with regard to the price being offered; and any material changes in the company’s financial condition since the date of the most recent financial statements or quarterly reports disclosed to the market.

In the case of companies listed on the Novo Mercado and Level 2 listing segments, the board of directors is required to prepare and disclose a reasoned opinion on the Takeover TO – in favour or against it – and to address the following topics:

a. the suitability of and opportunities presented by the Takeover TO;

b. the impact of the Takeover TO on the interests of the company;

c. the offeror’s stated strategic plans for the company; and

d. any other point of consideration the board may deem relevant.

Executive board

The executive board shall be composed of at least two officers. The officers of Brazilian listed companies can be elected and removed at any time by the board of directors.

Up to one-third of the board members may be elected for executive board positions held concurrently. Pursuant to the rules of the Novo Mercado, Level 2 and Level 1 listing segments, the offices of chair of the board of directors and CEO cannot be held by the same individual. However, the holding of these positions concurrently is allowed on an exceptional basis:

a. in the case of the companies listed in the Level 2 and Level 1 listing segments, for a maximum period of three years from the date that the company’s shares start to be traded on the special listing segment; and

b. in the case of the companies listed in the Novo Mercado listing segment, in the case of vacancy for a maximum period of one year, within such period the company shall disclose the accumulation of positions owing to vacancy not later than the business day following its occurrence, and disclose within 60 days of the vacancy the measures taken to end the accumulation of positions.

Among other duties, the executive board represents the company in dealings with third parties. The by-laws may establish that certain managerial decisions should be taken in executive board meetings only.

The by-laws will establish the number of officers permitted, the manner of their replacement, their term of office, and the assignments and powers of each officer. Officers will perform their duties separately, according to their assignments and powers, but in keeping with the other officers, and will not be held liable for any obligations assumed on behalf of the company as regards routine acts necessary for the company’s management.

If the by-laws are silent or there is no resolution adopted by the board of directors prescribing the officers’ duties, any officer may represent the company and take the actions necessary for its routine operations.

Compensation of the members of the board of directors and executive board

The shareholders’ meeting shall prescribe the aggregate or individual compensation of the members of the board of directors and executive board, including benefits of any kind and representation allowances, taking into consideration their responsibilities, the time devoted to their duties, their skills and professional standing, and the market value of their services. If
the shareholders’ meeting approves the aggregate compensation to be paid to the company’s directors and officers, it will fall under the authority of the board of directors to approve the allocation of the compensation between the company’s directors and officers.

If the company’s by-laws set forth a compulsory dividend equal to or above 25 per cent of the net profits, it may establish a share in the company’s profits to the benefit of the company’s directors and officers, provided that the total amount thereof does not exceed the annual compensation of the directors and officers, or one-tenth of the profits, whichever is the lower. Nevertheless, directors and officers shall only be entitled to a share in the profits in a financial year for which the compulsory dividend is paid to the shareholders.

Detailed information on the compensation paid to the company’s directors and officers, including, but not limited to, the breakdown of the compensation (e.g., fixed and variable compensation), and the minimum, lowest and average compensation paid, must be disclosed in the company’s reference form. In addition, the companies listed in the Novo Mercado segment must have and disclose their compensation policies.

**Fiscal board**

The fiscal board is a supervisory body responsible for supervising the company’s directors and officers and providing information in this respect to the shareholders.

The fiscal board is a compulsory body, but need not operate on a standing basis. A non-permanent fiscal board must be instated upon the request of shareholders representing at least 10 per cent of the voting stock or 5 per cent of the non-voting stock.

The fiscal board is composed of three to five members and a like number of alternates. The conditions for election and impairment of fiscal board members (who must be Brazilian residents) are prescribed by law.

The fiscal board has the authority to, among other things:

- monitor the actions of the company’s officers and directors and verify their compliance with their legal and statutory duties;
- review and give an opinion on the board of directors’ annual report;
- review and give an opinion on proposals of the management to the shareholders’ meeting relating to changes in capital, the issuance of debentures or warrants, investment plans or capital budgets, dividend distributions and certain corporate reorganisations;
- report any error, fraud or criminal act, and suggest measures useful to the company to any officer or member of another administrative body, and, if these fail to take any necessary steps, to act to protect the corporation’s interest and report to the shareholders’ meeting;
- review the balance sheet and other financial statements periodically prepared by the company; and
- examine the financial statements for the fiscal year and give an opinion about them.

The fiscal board’s authorities can be neither delegated nor attributed to any other body of the company.
Directors

The board of directors is a decision-making body of the company but the daily routine of administration of the company shall fall to the executive board. All the members of the board of directors, including the outside or independent members, must receive in advance of the meetings of the board of directors information about the matters that will be discussed and put to the vote.

Brazilian legislation does not expressly state that the directors have the right to visit the company’s facilities and its subsidiaries, or that the directors should have free access to the lower management of the company. However, considering that among the duties provided for the board of directors in the Corporation Law, it is established that the board of directors shall ‘supervise the performance of the officers, examine the books and records of the company at any time, request information on contracts signed or about to be signed, and take all other necessary action’, it is expected that the directors shall have free access to the company, its subsidiaries and its lower management.

Pursuant to the Corporation Law, the directors have the following duties and obligations:

a. a duty of diligence, employing the same care and diligence that every diligent and honest person employs in his or her own business;

b. to act within the scope of their duties without misuse of power, refraining from the performance of gratuitous or non-authorised acts and from the receipt of personal advantage by reason of the performance of their duties;

c. even if elected by a certain group or class of shareholders, they have the same duty to the company as everyone else, and must not, even in the defence of the interests of those who elected them, fail to fulfil these duties;

d. a duty of loyalty;

e. to act without conflict of interest, not intervening in any transaction where they have an interest conflicting with that of the company; and

f. a duty of information.

Directors shall not be held personally liable for the obligations assumed on behalf of the company as a result of a regular act of management. However, directors shall be held liable in civil lawsuits for losses that they cause owing to acts of negligence or fraudulent intent and in violation of the law or the company’s by-laws.

Note that the directors shall not be liable for unlawful acts performed by other directors, unless they are involved with these directors or they neglect to perceive them, or if, having knowledge of them, they fail to act to prevent their performance. However, directors are held jointly liable in the case of decisions taken by the board of directors.

In this particular, we note that each of its members is personally liable for any act of omission or negligence of the board of directors, and a dissident director shall express his or her disagreement regarding the resolutions taken through the clear and written register in the minutes of the meeting of the competent administration body, to release him or herself from any eventual civil liability. Any director who agrees with the performance of acts that violate the law or the company’s by-laws shall be held jointly liable for the losses resulting from said act.

The members of the board of directors are elected by the shareholders, who can dismiss them at any time. The shareholders representing at least one-tenth of the voting capital may
request that a multiple voting procedure be adopted to entitle each share to as many votes as there are board members, and to give each shareholder the right to vote cumulatively for only one candidate or to distribute his or her votes among several candidates.

The term of office of the directors must be defined in the by-laws, but cannot exceed three years, although re-election is permitted. In the case of companies listed in the Novo Mercado, Level 2, Level 1 and BOVESPA MAIS listing segments, the term of office cannot exceed two years, although again re-election is permitted.

The requirements for appointment to occupy a position on the board of directors are established in the Corporation Law. Generally speaking, a director must be someone with unblemished reputation, who has not been convicted in an administrative or judicial procedure in relation to corporate crimes or irregularities. Furthermore, unless waived in a shareholders’ meeting, individuals who hold positions in companies that may be regarded as market competitors of the company, or who have any interests that conflict with those of the company, cannot be elected as a board member.

As regards conflicts of interest, a director shall not take part in any corporate transaction in which he or she has an interest that conflicts with an interest of the company, or take part in the decisions made by the other directors on the matter. He or she shall disclose his or her disqualification to the other directors, and shall cause the nature and extent of his or her interest to be recorded in the minutes of the meeting of the board of directors.

Notwithstanding compliance with the conflict of interest provision, a director may only contract with the company at arm’s length. Any business contracted other than on an arm’s-length basis is voidable, and the director concerned shall be compelled to transfer to the company all benefits that he or she obtains through such business.

III DISCLOSURE

The Corporation Law has adopted the principle of full disclosure when it comes to acts or facts related to a company that may be considered relevant. The disclosure of material events is a duty of the company’s investor relations officer, who may be held personally liable for damage arising as a result of non-disclosure.

CVM Ruling No. 358/2002, which sets forth the general disclosure rules for listed companies, defines material event broadly as:

- any decision arising from a controlling shareholder, a general shareholders’ meeting or a management body of a publicly held corporation, or any other act or event of a policy, management, technical, business, economic or financial nature in connection with its business that could considerably influence the trading price of the securities issued by or related to the company;

- the decision by investors to buy, sell or keep those securities; and

- the decision by investors to exercise any rights they have as holders of securities issued by or related to the company.

The companies listed in the Novo Mercado segment are required to disclose their material facts in Portuguese and English, concurrently.

At the end of 2009, CVM enacted CVM Rulings Nos. 480/2009 and 481/2009, modifying, respectively, the rules regarding the disclosure of information by publicly held companies and the presentation of documents and information before meetings are held. The main change in disclosure issues was the introduction of the reference form, which basically
compiles corporate, contractual, financial or economic, governance and human resources information about the company. The reference form must be updated at least once a year, or in a shorter period upon the occurrence of certain events that demand an update of the information provided in the reference form.

As to financial reporting, listed companies must disclose their financial statements, together with the management report, the independent auditors’ report and the opinion of the fiscal board, if installed, at least one month in advance of the ordinary shareholders’ meeting.\(^6\)

Listed companies must also disclose the standard form of financial statements (DFP) within the first three months of the end of each fiscal year. The DFP is an electronic form created in CVM’s electronic system that must be completed using information obtained from the annual financial statement.

Listed companies shall also disclose, on a quarterly basis, the quarterly information form, which is also an electronic form and must be completed using the company’s quarterly financial information. It must contain the report of the special review issued by the independent auditor.

In addition to disclosing their financial statements in Portuguese, companies listed in the Level 2 listing segment must also disclose them in English.

Regarding one-on-one meetings, companies listed in the Novo Mercado must hold a public presentation on the information disclosed in their quarterly earnings results or financial statements within five business days of their release. Such public presentation may be conducted face-to-face or via teleconference, videoconference or any other means that enables stakeholders to participate remotely. On the other hand, the companies listed in the Level 2 and Level 1 listing segments are required to hold, at least once a year, a public meeting with analysts and other third parties to disclose information about their financial and economic situation, projects and expectations.

**IV CORPORATE RESPONSIBILITY**

Pursuant to the Corporation Law, all publicly held companies must prepare on an annual basis, within their financial statement, a value-added statement, which could be considered as the balance statement of the company’s ‘social account’. This statement provides information on the overall wealth produced by the company, on the allocation of resources to those areas of the company that contributed to the generation of that wealth (such as employees, financiers, shareholders, the government and others) and on the unallocated portion of that wealth. In addition, some companies seek certification from institutes such as the Ethos Institute, the Brazilian Institute of Social and Economic Analysis and the Global Reporting Initiative, but such certification is not mandatory for listed companies.

Another aspect of this social accounting is evidenced in the code published by the Brazilian Financial and Capital Markets Association (ANBIMA) regarding public offerings, which sets forth that companies must include in their reference form information on social responsibility and cultural incentives, and on any projects in those areas implemented by the company. Thus, although the ANBIMA code does not require their existence, if the company has any social responsibility policies in place, these should be disclosed in the reference form.

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\(^6\) The ordinary shareholders’ meeting must be held within the first four months of the end of each fiscal year.
Furthermore, a new anticorruption law has been in place since 29 January 2014, and this has introduced administrative and civil liability of legal entities for illicit acts committed in relation to local and foreign public officials. However, there is as yet no whistle-blowing legislation in force in Brazil.

V SHAREHOLDERS

i Shareholder rights and powers

Each common share shall have the right to one vote in shareholders’ meetings, and it is not possible to have shares with multiple voting rights. Brazilian companies can, however, issue preferred shares, which can be issued without voting rights (although companies listed in the Novo Mercado are required to issue only common shares).

In addition, the Corporation Law sets forth that it is possible to include in the company’s by-laws a provision restricting the number of votes by each shareholder. Nevertheless, the companies listed in the Novo Mercado and Level 2 listing segments are not permitted to include in their by-laws any provision restricting the number of votes of shareholders to a percentage below 5 per cent of the stock capital, except in a few cases provided in the listing rules.

In theory, shareholders should not have the ability to influence directors’ decision-making. In this regard, a specific article of the Corporation Law sets forth that a director shall use his or her powers to achieve the company objectives and to support its best interests, even if these interests are contrary to those of the shareholder, or a group of shareholders, who have elected or indicated him or her.

Nevertheless, the Corporation Law also contains a provision stating that the votes of directors can be bound by a shareholders’ agreement. Therefore, the Corporation Law recognises that the directors can receive instructions from the shareholders on how to vote in board meetings.

The shareholders’ meeting has exclusive authority to:

a amend the by-laws;
b elect or discharge the company’s senior management and fiscal board members;
c receive the annual accounts of the senior management and resolve on the financial statements presented by them;
d suspend the exercise of rights by a shareholder;
e resolve on the appraisal of assets contributed by any shareholder to the company’s capital;
f authorise the issuance of participation certificates;
g resolve on the transformation, merger, consolidation, spin-off, winding-up and liquidation of the company, elect and dismiss liquidators, and examine the liquidators’ accounts; and
h authorise the senior managers to admit bankruptcy of the company and to file for debt rehabilitation.

As for the rights of dissenting shareholders, certain fundamental changes in the company entitle the shareholders who have not voted in favour of the resolution to withdraw, by refund of their shares, under the circumstances below:
a in the case of the creation of preferred shares or an increase of an existing class without maintaining its ratio in relation to the other classes, and change of a preference, a privilege or a condition of redemption or amortisation conferred upon one or more classes of preferred shares, or creation of a new and more favoured class;
b the spin-off of the company only triggers the right to withdraw if it results in a change in the corporate purposes – except when the spun-off company is transferred to a corporation with a main line of business that coincides with the line of business of the spun-off company – a reduction in the mandatory dividend or participation in a group of corporations;
c the reduction of the compulsory dividend in any specific fiscal year, change of corporate purpose and insertion of an arbitration clause in the by-laws;
d the approval of the merger of shares entitles shareholders of both companies involved to withdraw; and
e a shareholder who has not voted in favour of the acquisition by the listed company of which he or she is a shareholder of the control of a business corporation is entitled to withdraw if the purchase price exceeds 1.5 times the greatest of:
• the average quotation of the shares on the stock exchange during the 90 days prior to the contracting date;
• the net value of each share or quota, the assets and liabilities having been valued at market prices (liquidation value); and
• the net profit of each share or quota, which may not exceed 15 times the annual net profit per share during the past two fiscal years, monetarily adjusted.

ii Shareholders’ duties and responsibilities

The controlling shareholder has the duty to use its controlling power to make the company accomplish its purpose and perform its social role, and shall have duties and responsibilities towards the other shareholders of the company, those who work for the company and the community in which it operates, the rights and interests of which the controlling shareholder must loyally respect and heed.

The controlling shareholder shall be liable for any damage caused by acts performed in abuse of its power. The Corporation Law lists some examples of what would be considered an abuse of power, which include, among others, the following:
a guiding a company towards an objective other than in accordance with its stated objects, or that is harmful to national interests, or induce it to favour another Brazilian or foreign concern to the detriment of the minority shareholders’ interests in the profits or assets of the company or of the Brazilian economy; and
b arranging for liquidation of a viable company or for the transformation, merger or division of a company to obtain, for itself or for a third party, any undue advantage to the detriment of the other shareholders, of those working for the company or of investors in the company.

There are no specific duties provided in Brazilian legislation for institutional investors, and there is no code of best practice for shareholders.
iii Shareholder activism

Shareholder activism is not well developed in Brazil. Recent years, however, have seen a growing amount of shareholder activism, especially by some fund managers, but shareholder activism is still not part of the culture of the Brazilian capital markets.

The Brazilian companies most exposed to shareholder activism are those that have issued American depository receipts in the US market. A good example would be Petrobras, the Brazilian oil and gas company, which faced securities class actions filed with the New York courts by US investors owing to losses stemming from money-laundering and corruption schemes that have become public in the past few years; Petrobras announced in January 2018 that it has signed an agreement to settle such class action in an amount of US$2.95 billion. Owing to this settlement, some minority shareholders have filed lawsuits in Brazil asking for a similar indemnification in Brazil, but it is unlikely that they will receive an indemnification from Petrobras in such amount, since the Brazilian legislation and judicial environment do not provide minority shareholders the ability to receive indemnifications in such proportion.

iv Takeover defences

Shareholder and voting rights plans, and similar measures

The Corporation Law and CVM Ruling No. 361 require as a condition for the effectiveness of the direct or indirect disposal of a controlling interest in a listed company that the acquirer make a mandatory public tender offer (tag-along TO) for the acquisition of all the voting shares that are not part of the controlling block.

The tag-along TO must ensure minority shareholders the receipt of at least 80 per cent of the value paid per voting share included in the controlling block. For companies listed on the Novo Mercado listing segment, the amount to be paid in the tag-along TO shall correspond to 100 per cent of the value paid per voting share included in the controlling block.

Another defence to be considered is the use of poison pills, which Brazilian legislation does not prevent companies from putting in place, and they are used in some listed companies. The typical Brazilian poison pill requires the acquirer of an equity interest above a given threshold to make a tender offer to all shareholders for a punitive price. The use of poison pills must, however, be established in the by-laws of the company. As a consequence, only the shareholders’ meeting, which has exclusive authority to amend the by-laws, is empowered to put poison pills in place.

CVM has already pronounced against provisions that penalise or prevent shareholders from voting against the exclusion of poison pills on a case-by-case basis in a definitive manner. Furthermore, the rules of Novo Mercado listing do not allow companies that want to trade their shares on the Novo Mercado to have poison pills in their by-laws.

v Contact with shareholders

Mandatory and best practice reporting to all shareholders

Companies must disclose to all of their shareholders, through their websites, as well as on the CVM and B3 websites, certain ordinary and extraordinary reports or information, such as the reference form, financial statements, minutes of the shareholders’ meetings and documents necessary for review by shareholders to be able to exercise their voting right in shareholders’ meetings.
It is common practice in listed companies to hold a conference call with investors right after the release of the annual or quarterly financial statement to discuss a company’s results. It is also usual for these companies to hold meetings or calls with analysts to discuss the company to enable the analysts to issue their reports on the company. In the case of the companies listed in the Novo Mercado segment, they must hold a public presentation on the information disclosed in their quarterly earnings results or financial statements within five business days of their release.

Whenever the company holds a meeting with a specific shareholder to discuss a material fact that has not been disclosed, it is usual to have this shareholder sign a non-disclosure agreement, and the shareholder would be subject to a blackout period during which it would be unable to trade in the company’s shares, until the material information is disclosed to the market.

Call notices for the shareholders’ meetings of publicly held companies must be published at least three times, with the first call notice being published, as a general rule, at least 15 days in advance.7

Publicly held companies are required to disclose on the same day as the first publication of the call notice the manual of the shareholders’ meeting, which contains detailed information about the matters to be discussed and the management proposal for each of the matters that will be voted on.

The supporting documentation for the ordinary shareholders’ meeting (e.g., financial statements, management report, independent auditor’s report and opinion of the fiscal board) must be disclosed to the shareholders 30 days in advance of the date of the meeting.

In 2015, CVM enacted a ruling on attendance and distance voting at shareholders’ meetings of publicly held companies, whereby shareholders would be able to present proposals of deliberations to be voted on, and to vote on the deliberations of the shareholders’ meeting, subject to certain requirements. Implementation of this proxy voting system was mandatory for the major companies listed on B3 as from 2017, and has been mandatory for all listed companies as from 2018.

VI OUTLOOK

We expect that the biggest trends in the next few years in Brazil will be the increase of number of IPOs and follow-ons, as a result of the migration of the Brazilian investors from the fixed income investments to equity investments, which will require the Brazilian companies to improve their corporate governance practices to stand out from the other companies that will be competing for raising funds through IPOs and follow-ons.

7 For some specific matters, the call notice must be published 30 days in advance.
I OVERVIEW OF GOVERNANCE REGIME

The main sources of law relating to governance practices of listed companies in Finland are the Companies Act and the Securities Markets Act. Both acts have recently undergone reforms and incorporate the most recent aspects of modern corporate governance. In addition, related regulations as well as guidelines, recommendations and rules issued by the competent authorities on both domestic and EU level, including the Finnish Financial Supervisory Authority (FIN-FSA), Helsinki Stock Exchange (operated by Nasdaq Helsinki Ltd) and the European Securities and Markets Authority (ESMA), are key regulatory sources in the Finnish governance regime. Requirements for corporate governance increasingly stem from EU level legislation, particularly the EU’s Second Shareholder Rights Directive (SHRD II), which was implemented in Finnish national legislation on 10 June 2019.

Furthermore, self-regulation plays an essential role, as do the articles of association and other company-specific rules of procedure, such as board and CEO work ordinances. Self-regulation norms can be found in the newly revised Finnish Corporate Governance Code (the Code) applied as of 1 January 2020 and in the Helsinki Takeover Code applied as of 1 January 2014, both issued by the Securities Market Association. The Code was amended to correspond to the requirements of SHRD II. The updates concerned particularly the provisions on reporting on remuneration, monitoring and assessing of related-party transactions, competence, expertise and duties of committees as well as assessing and reporting on the independence of board members.

1 Risto Ojantakanen and Ville Kivikoski are partners and Linda Pihonen is an associate at Itäinen & Ojantakanen Attorneys Ltd.


3 Finnish Securities Markets Act (746/2012, as amended).


II CORPORATE LEADERSHIP

i Board structure and practices

Pursuant to the Companies Act, the mandatory organs of a limited liability company are the general meeting and the board of directors. A supervisory board whose duties comprise the supervision of the company's administration and governance by the board of directors and the managing director may also be appointed. In practice, only a few listed companies have a supervisory board.

Legal responsibilities of the board

The board of directors is responsible for the overall administration of a company and the organisation of its operations, as well as for the arrangement of the control of the company accounts and finances. The board members and the managing director have a general duty to act with due care and in the best interest of the company.

In addition, the Companies Act contains several provisions by which the board of directors or its members are expressly entrusted with specific responsibilities, such as the ability to elect and dismiss the managing director, the obligation to draw up financial statements and the annual report as well as various other administrative obligations.

Decision-making

A quorum is constituted when more than half of the board members are present, unless a larger proportion is required in the articles of association. When the proportion is calculated, disqualified members are considered absent. The opinion of the majority shall constitute the decision of the board of directors. The articles of association may provide that decisions in the board shall, in order to be valid, be made by a qualified majority or unanimously. However, to our knowledge, listed companies very seldom use such qualifications. In the event of a tie, the chairman of the board of directors shall have the casting vote.

Committees

The board of directors may establish committees for the preparation of matters within its competence. The board, however, remains responsible for the duties assigned to the such committees. The Code describes the establishment and functions of an audit, remuneration and nomination committee. The board elects the members and the chairman of any such committee amongst its members. A committee shall consist of at least three members, all having the expertise and experience required for the duties of the committee in question.

Pursuant to the Code, a listed company shall establish an audit committee if the extent of the company's business requires that the preparation of matters pertaining to financial reporting and control be done in a more concentrated manner than by the board of directors.

If established, a nomination committee prepares matters pertaining to the election of the members of the board of directors. A remuneration committee, in turn, prepares the remuneration policy and may also be assigned to prepare the appointment of the managing director and the rest of the management team, as well as to assess and prepare their remuneration.

The board may also establish ad hoc committees to deal with matters of particular importance, such as a major acquisition or receipt of a takeover proposal.
Board and company practice in takeovers

Pursuant to the Securities Markets Act, both the party making a takeover bid and the target company listed in Helsinki Stock Exchange shall comply with the Helsinki Takeover Code, a recommendation issued by the Securities Market Association in order to promote good securities markets practice. Further regulations and guidelines concerning takeover bids have been set forth by FIN-FSA.

The board of directors of a target company plays an important role in public takeovers. The Securities Markets Act and the Helsinki Takeover Code impose certain obligations on the board of directors relating to such situations.

The board of directors has an obligation to seek the best possible outcome for the shareholders and actively evaluate and undertake the measures needed in order to achieve such objective. In a takeover bid situation, the interests of the shareholders require that the board of directors evaluate the bid and its consequences from various viewpoints and assess it also in light of other possible alternatives. The board of the target company may also seek competing bids subject to its own discretion.

Pursuant to the Securities Markets Act, the board of directors of a target company shall give a public statement containing well-founded assessment on the bid as well as a recommendation regarding whether or not the bid should be accepted. In any such recommendation, particular attention is to be paid to the valuation, the nature of the consideration and the overall feasibility of the takeover bid.

Remuneration

According to the Companies Act, the general meeting shall decide on the remuneration of the board of directors. The remuneration of the managing director shall be decided by the board. In a listed company, such decisions must be, save for certain exceptions, within the framework of a valid remuneration policy, which shall be presented to the general meeting at least every four years.

Based on the implementation of SHRD II, listed companies are obligated by the Securities Markets Act to disclose an annual remuneration report on the remuneration awarded to the company’s managers during the preceding financial year. Detailed rules concerning the remuneration report have been set forth in a decree of the Ministry of Finance6 and in the Code. The Code also recommends listed companies to provide aggregated information on their website on the remuneration of other members of its management team.

ii  Directors

Appointment, nomination and term of office

The general rule is that the annual general meeting elects all of the members of the board of directors, unless otherwise provided in the articles of association. If there are fewer than three board members, at least one deputy member shall be appointed. If the board has more than one member, the board shall elect a chairman amongst its members.

In a listed company, the term of a board member shall end with the conclusion of the ordinary general meeting following the election of the member. Other provisions on the term may be included in the articles of association. According to the Code, good corporate

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6 Decree of the Ministry of Finance on the content requirements and disposition of the remuneration policy and report of an issuer of shares (608/2019).
governance requires that the entire board of a listed company is elected annually at the annual general meeting. In addition, the general meeting may decide to establish a shareholders’ nomination board consisting of representatives of major shareholders for the purposes of preparing a proposal to the annual general meeting for the composition and remuneration of the board of directors.

**Competency and independence**

According to the Code, a board member must have the competence required by the position and, in general, the composition of the board shall reflect the requirements set by the company’s operations and development stage. Pursuant to the Companies Act, legal persons, minors, persons under guardianship, persons with restricted legal competency and bankrupts cannot be appointed as board members. Additionally, a person who has been prohibited by a court decision to conduct business cannot be appointed as board member during the period of validity of the prohibition. Further, according to the Companies Act, at least one member of the board must reside within the European Economic Area unless the company has been exempted from this requirement by the registration authority.

According to the Code, the majority of the board members must be independent of the company and at least two of such members must be independent of significant shareholders of the company. The board of directors has the responsibility to evaluate the independence of its members on a yearly basis.

**Liability of directors**

A member of the board of directors, a member of the supervisory board and the managing director shall be liable for the loss that he or she, in violation of the duty of care, other provisions of the Companies Act or the articles of association, has in office deliberately or negligently caused to the company. If the damage has not been caused in office, other compensation provisions, particularly the Tort Liability Act,7 may still apply.

**Conflicts of interest**

Pursuant to the Companies Act, a member of the board of directors is disqualified from the consideration of a matter that concerns a contract or other legal act between such board member and the company, or a contract between such member and a third party, if the member is expected to have a substantial interest in the matter and if the matter may contravene with the company’s interest.

As a result of the implementation of SHRD II, a board member of a listed company is also disqualified, with certain exceptions, from the consideration of a matter in the company’s or its subsidiary’s board, if the matter concerns a contract or other legal act that involves a party related to the board member, as defined in the international financial reporting standards (IFRS), and if the contract or act will not be made in the ordinary course of business or concluded on market terms. In a listed company, the managing director and members of the supervisory board (if appointed) are also bound by the above-mentioned rules of disqualification. Participation of a disqualified member in the decision-making process may lead to invalidity of the decision.

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7 Tort Liability Act (412/1974, as amended).
III DISCLOSURE

i General

Disclosure obligations and the management of insider information in listed companies are primarily regulated by the EU Market Abuse Regulation (MAR)⁸ and the Securities Markets Act. Further regulation has been set forth in the rules of Helsinki Stock Exchange and the regulations and guidelines of FIN-FSA and ESMA. Based on applicable disclosure obligations, listed companies are required to provide certain information to the market both on a periodic and an ongoing basis. Violation of or failure to follow the applicable disclosure obligations may result in administrative and criminal sanctions.

Periodic disclosure obligation

Listed companies shall publish financial statements, a management report and an auditor’s report annually. The financial statements shall be prepared in compliance with IFRS.

Further, listed companies are obligated to disclose an interim financial report for the first six months of their fiscal year without undue delay and not later than three months from the expiry of the reporting period. Quarterly financial reporting, however, is no longer mandatory although followed by many listed companies.

In addition, listed companies are required to annually disclose a corporate governance statement, either as a part of the annual management report or, as the Code suggests, as a separate report. Detailed rules concerning the periodic disclosure obligation, interim financial reports, the management report and the corporate governance report as well as remuneration policy and the remuneration report have been set forth by the Ministry of Finance.⁹ The Code also includes recommendations regarding the corporate governance and remuneration reports.

Continuous disclosure obligation

MAR requires issuers to inform the public as soon as possible of information of a precise nature that, if made public, would be likely to have a significant effect on the price of a security. However, pursuant to MAR, a company may, at its own responsibility, delay the disclosure of inside information provided that immediate disclosure is likely to prejudice the legitimate interests of the issuer, the delay is not likely to mislead the public and the issuer is able to ensure the confidentiality of the information in question. In this case an insider list shall be drawn up.

Other requirements and disclosure obligations

MAR requires listed companies to maintain a list of all the persons who have access to inside information and, upon request, provide the list to FIN-FSA. Recommendations concerning the management of insider lists have been set forth in the Code and in the guidelines for insiders of listed companies issued by Nasdaq Helsinki.

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⁹ Decree of the Ministry of Finance on issuer’s periodic disclosure obligation (1020/2012) and Decree of the Ministry of Finance on the content requirements and disposition of the remuneration policy and report of an issuer of shares (608/2019).
According to the Securities Markets Act, a shareholder of a listed company is obligated, with certain exceptions, to notify the company and FIN-FSA the total number of shares and voting rights held (flagging notification), when the proportion reaches, exceeds or falls below certain threshold limits (5, 10, 15, 20, 25, 30, 50, 2/3 and 90 per cent). Upon receipt of a flagging notification, the company must disclose the information of the notification to the public. MAR also requires persons with managerial responsibilities within a listed company, as well as persons closely associated with them, to promptly notify both the company and FIN-FSA of transactions conducted on their own account relating to the issuer’s securities.

Based on the implementation of SHRD II, listed companies are also required to disclose transactions that are material and concluded with a related party at latest when the company is bound by the transaction, provided that the transaction has not been entered into in the ordinary course of business or concluded on market terms.

Nasdaq First North Growth Market

Along with Helsinki Stock Exchange, Nasdaq Helsinki Ltd operates First North Finland Growth Market, the only multilateral trading facility in Finland that is an alternative stock exchange designed for small and growing companies. Companies listed on Nasdaq First North Growth Market are subjected to less extensive rules regarding, for instance, listing requirements, disclosure obligations and takeover situations. Further, First North Finland Growth Market listed companies are not obligated to prepare financial statements in accordance with IFRS nor are they required to comply with the Code.

IV CORPORATE RESPONSIBILITY

i Corporate social responsibility and wider society

The concept of corporate social responsibility has become more diverse and more important in recent decades and especially during the past few years, which in turn has made companies regard corporate responsibility not merely as a burden but as a strategic opportunity for a reform and a source of competitive advantage.

As social and environmental responsibility has become increasingly important in public speech, companies have started to pay more and more attention also to reputational risk aside from financial and operative risk. For instance, aggressive tax optimisation, poor working conditions in a factory of a foreign subcontractor or unclear information on the origin of raw materials may impose a significant reputational risk for a company. The increased demand for risk management has led to the use of numerous different certificates and standards and increased the importance of company policies and internal auditing. Correspondingly, consumers’ growing consciousness of the impact that production of goods has on local ecosystems and communities has increased the demand for transparent reporting.

Corporate social reporting has developed mainly on a voluntary basis. Although some general frames of reference have been developed for responsibility reporting, such as the Global Reporting Initiative, which is used by many Finnish companies, the quality of these reports has varied. Standards and instruments have also been developed to improve environmental management and social responsibility in companies, such as ISO 14000, ISO 26000 and the EU Eco-Management and Audit Scheme (EMAS).
Risk management

The board of directors is responsible for the organisation and effective oversight of risk management in the company. Recommendations regarding internal control and risk management for the board of directors in listed companies are set forth in the Code. The board shall ensure that the company has defined the operating principles for internal control and that the company monitors its functioning. In addition, companies shall report in the corporate governance statement the operating principles for internal control, the risk management principles relating to financial reporting processes and the main principles applied in internal audit.

Diversity

Along with diversity in experience, education and nationality, one element of diverse composition of a board of directors is to have balanced gender representation on it. According to the Code, companies must report at least the objectives relating to both genders being represented on the company’s board of directors, the means to achieve these objectives and an account of the progress in achieving them.

In 2019, women’s share of board seats was 29 per cent (being 18 per cent in 2011) in companies listed on Helsinki Stock Exchange, and nearly every company had a female member on the board of directors. Further, 9 per cent of listed companies had a woman as a managing director. These numbers have been reached solely through self-regulation and increasing initiative in commerce and industry.

V SHAREHOLDERS

Shareholder rights and powers

The main rules governing shareholders’ rights are set out in the Companies Act. Shareholders exercise their decision-making power at the general meeting. The annual general meeting must be held once a year within six months of the end of the financial period. Extraordinary general meetings must be convened when requested by the board of directors, the auditor, the supervisory board or shareholders holding at least 10 per cent of the total number of shares.

Each shareholder has the right to attend a general meeting. The same applies to the holders of non-voting shares unless otherwise provided in the articles of association.

Matters to be brought to the general meeting

The general meeting shall make decisions on matters that fall within its competence by virtue of the Companies Act. Matters to be decided by the general meeting include, among other things, amending the articles of association, distribution of funds, issuance, acquisition and cancellation of shares as well as any decision on corporate restructuring under the Restructuring of Enterprises Act (47/1993, as amended).

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10 Ibid.
In addition, a shareholder has, regardless of its ownership stake, the right to have
a matter falling within the competence of the general meeting dealt with by the general
meeting if the shareholder so demands in writing from the board of directors well in advance
to be included in the notice of the general meeting.

**Decision-making at the general meeting**

As a general rule, each share carries one vote. However, it can be arranged through the articles
of association that shares carry multiple voting rights or that a certain class of shares carries
no voting rights at all.

Normally, a proposal that is supported by more than half of the votes cast constitutes
the decision of the general meeting. However, pursuant to the Companies Act, certain
decisions must be made by a qualified majority of two-thirds of the votes cast and of the
shares represented in the general meeting.

**Voting disqualifications**

A shareholder is disqualified from voting in a matter pertaining to a civil action against
the shareholder or the discharge of the shareholder from liability towards the company. A
shareholder is likewise disqualified from voting in a matter pertaining to a civil action against
a third party or the discharge of a third party from liability, if the shareholder is likely to
derive an essential benefit which may be contrary to the interests of the company. Following
the implementation of SHRD II, a shareholder who is a related party (as defined in the IFRS)
to the listed company is also disqualified, with certain exceptions, from voting in a matter
pertaining to a contract or other transaction that involves the shareholder or persons closely
associated with the shareholder, provided that the transaction is not made in the ordinary
course of business or concluded on market terms.

**Minority shareholder rights**

The protection of minority shareholders is based on the principle of equal treatment. The
principle prohibits general meeting, the board of directors, the managing director and the
supervisory board from making a decision and taking other measures that are conducive
to conferring an undue benefit to a shareholder or another person at the expense of the
company or another shareholder without the consent of the shareholder or shareholders at
whose expense such undue benefit is to be given.

The Companies Act imposes various provisions relating to the exercise of minority
rights. Typically, such rights may be exercised by a shareholder or shareholders who together
hold at least one-tenth of the total amount of shares in the company. The minority rights
include the right to:

- demand an extraordinary general meeting be called to address a specific issue;
- demand a minority dividend be distributed;
- bring a derivative action against the company's directors, the managing director or
  another shareholder for damages incurred to the company; and
- propose that a special audit be carried out.

Moreover, a shareholder may, in certain cases, demand that another shareholder who has
deliberately abused influence in the company redeem the shares of the offended shareholder.
However, such situations are uncommon and would require a harsh violation to have taken
place.
The right to request information

A shareholder has the right to review the proposed resolutions and the financial data concerning the company before a matter is decided at a general meeting. Such information shall be kept available on the company’s website and at the headquarters for at least a week before the general meeting.

At the request of a shareholder, the board of directors and the managing director shall provide more detailed information on circumstances that may affect the evaluation of a matter handled by the general meeting. If the meeting deals with financial statements, the obligation applies also to general information on the financial position of the company. However, such information shall not be provided if it were to cause substantial harm to the company (for example by revealing trade secrets or other confidential information).

Objection to a decision by the general meeting

The decision of a general meeting can be challenged if it violates the Companies Act or the articles of association. Pursuant to the Companies Act, a shareholder may object such decision by bringing an action against the company within three months of the decision.

Void decision by the general meeting

Pursuant to the Companies Act, a decision by the general meeting can be considered void, if:

- no notice has been delivered of the general meeting or the provisions on the notice have been materially breached;
- the decision requires the consent of a shareholder and such consent has not been obtained;
- the decision is clearly contrary to the principle of equal treatment; or
- according to the law, the decision could not have been made, even with the consent of all shareholders.

A shareholder may plead the invalidity of a void decision without a specific time limit, but it has been established that an action of objection shall nevertheless be made within a reasonable time.

Shareholders’ duties and responsibilities

Duties of a majority shareholder

As a rule, shareholders have the right to pursue self-interest, (i.e., shareholders are not required to act for the benefit of the company, other shareholders or other persons). However, a majority shareholder cannot in any capacity make a decision that would violate the principle of equal treatment.

Under the Securities Markets Act, a shareholder whose proportion of voting rights increases to over 30 per cent or 50 per cent of the votes attached to the shares of the company (bid thresholds) is required to launch a mandatory takeover bid for the remaining shares in the company. According to the Companies Act, a shareholder with more than 90 per cent of all the shares and votes in the company has the right to redeem the shares of the other shareholders at a fair price (right of squeeze-out). Respectively, a shareholder whose shares may be redeemed has the right to demand such redemption (right of sell-out).
Shareholder activism

Shareholder activism has remained a fairly modest phenomenon in Finland in the recent decades. However, institutional investors are seeking to take a more active role and have been instrumental in a few recent structural arrangements of listed companies. In Finland, there is a long tradition of the state being a large shareholder of listed companies, and the activity or passivity of the state as a shareholder has been a frequent topic in public discussion. Other significant and influential shareholders of listed companies in Finland are the large mutual pension insurance companies, of which there are only a few.

As a result of the implementation of SHRD II, a large number of different institutional investors and asset managers that have invested in shares traded on a regulated market in the European Economic Area are obligated to develop and disclose an engagement policy that describes how they have integrated shareholder engagement in their investment strategies. They must also disclose on an annual basis how their engagement policies have been implemented including, for example, a general description of voting behaviour. In the case of non-compliance with such requirements, a clear and reasoned explanation must be given.

Takeover defences

The Finnish poison pill

In Finnish company law practice, the term poison pill refers to a provision in the articles of association, according to which a shareholder has an obligation to launch a takeover bid for all the other shares in the company for a specified price if the shareholder’s proportion of shares or voting right reaches or exceeds a certain threshold.

The importance of poison pills for listed companies decreased after the introduction in the Securities Markets Act of the mandatory 30 per cent takeover bid threshold (while also retaining the 50 per cent threshold) in 2006.

Consent and redemption clauses

According to the Companies Act, it may be provided in the articles of association that the acquisition of a share requires the consent of the company (consent clause), or that a shareholder, the company or another person has the right to redeem shares due to be transferred to a third party by a shareholder other than the company (redemption clause). However, these kinds of provisions restrict the free transferability of shares and are therefore prohibited by the rules of Helsinki Stock Exchange.

Other defences

In a takeover bid situation, the board is required to take active steps to ensure that the best possible outcome is achieved for the shareholders, which may require the board to seek for a competing bid (white knight defence).

A vote cutter refers to a provision in the articles of association that restricts the voting rights of a shareholder in general meeting. According to the Companies Act, a share may be set to carry a vote in a given matter or no voting rights at all. Vote cutters, which are valid also in listed companies, can be used to hinder majority control and takeover attempts.
v Contact with shareholders
As noted in the Code, due to the principle of equal treatment of shareholders, regulations governing inside information, disclosure obligations, reasons related to competitions law and confidentiality obligations of company managers, to name a few, companies should refrain from giving undisclosed information on company matters to individual shareholders. However, if the board deems that it is in the best interest of the company, it may contact an individual shareholder and give such information subject to proper protection of confidentiality and possible inside information.

With respect to matters falling within the competence of the general meeting, in Finnish corporate governance practice it is customary for the board of directors to be aware of the opinions that the shareholders with significant ownership shares have on the matter being brought for resolution.

VI OUTLOOK
The newly implemented SHRD II has altered the operational environment of many listed companies in Finland in the preceding year – especially together with the increasing focus on climate change, aim for sustainable development, strive for gender and other forms of equality as well as other similar issues of a global nature strongly relating to corporate social responsibility. As a Nordic country Finland can be considered a good example with respect to many such trends mentioned, although discussion on corporate social responsibility in Finland can be considered still in its infancy. Transparency in its various forms and aspects has affected and continues to affect the corporate governance regime in Finland not only through regulation and guidelines but increasingly through self-assessment and increase in sense of responsibility on a wider scale.
I OVERVIEW OF GOVERNANCE REGIME

Corporate governance rules are mainly set out in statutory provisions contained in the French Commercial Code and in recommendations contained in corporate governance codes (such as the French Association of Private Enterprises (AFEP) – Movement of French Enterprises (MEDEF) Code) or in positions expressed by various professional bodies and associations.

The AFEP-MEDEF Code has become a reference in matters of corporate governance. Besides compulsory rules, the implementation of corporate governance principles is also monitored by the French Financial Markets Authority (AMF), which publishes an annual report assessing corporate governance practices and executive directors’ compensation in listed companies.

Even if corporate governance codes and the positions expressed by professional bodies or associations do not have any legal authority and are considered to be soft law, these rules are generally applied by companies. This can be explained by market pressure, since compliance with these rules is a criterion used by proxy advisers in their recommendations on how to vote on shareholders’ resolutions. Almost all large listed companies have selected to use the AFEP-MEDEF Code. The application of the AFEP-MEDEF Code’s provisions is monitored by a high committee on corporate governance, which issued its first report in October 2014 and a guide on the application of the AFEP-MEDEF Code in December 2014. The revised AFEP-MEDEF Code of June 2018 has further strengthened the enforcement powers of the high committee on corporate governance by enhancing its ability to use the name and shame policy.

Corporate governance in France has changed considerably during the past two decades as a result of the increased number of foreign shareholders in CAC 40-listed companies.

With respect to executive compensation, much greater scrutiny has been introduced in France, which now stands as one of the European countries with the most extensive range of requirements. The level of disclosure has continued to increase in recent years under the pressure of shareholders and proxy advisers, and after several controversies concerning executive compensation and severance packages. Regulations have also been used to address market failures and restore public confidence, especially after the turmoil created in 2016 by the lack of reaction from the boards of directors of two companies after the shareholders rejected the executives’ compensation. This caused the legislator to introduce, in December

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1 Didier Martin is a partner at Bredin Prat.
2 High Committee on Corporate Governance 2014 Annual Report. The High Committee issued its sixth report in October 2019.
3 The High Committee issued its third updated guide in January 2019.
2016, a say-on-pay procedure that is both mandatory and binding. Such procedure was further strengthened in November 2019, via an Order transposing into French law the main provisions of Directive 2017/828 amending Directive 2007/36/EC as regards the encouragement of long-term shareholder engagement adopted on 17 May 2017.

Another notable trend is the preference among listed companies for the one-tier governance structure. Companies with a one-tier board tend to combine the positions of chair of the board and CEO although shareholders and proxy advisors increasingly challenge this practice. As recommended by the AMF and the AFEP-MEDEF Code, the majority of CAC 40-listed companies have appointed a lead director in order to counterbalance the concentration of power in the CEO’s hands (when he or she is also the chair of the board). The AFEP-MEDEF Code provides that lead directors should be independent directors.

In other areas, such as director independence, diversity of the board composition and board committees, the French corporate governance regime continues to converge with existing best practice.

There has also been increased focus on corporate and social responsibility in recent years. The practice of extra-financial analyses and rating has developed considerably to enable investors to include the extra-financial performance of companies in their investment criteria, and both law and soft law have been amended to increase the level of disclosure made with respect to environmental, social and governance issues.

These recent trends are notably reflected in the revised AFEP-MEDEF Code of June 2018, which includes provisions aimed at:

a. reinforcing the role of the board to promote corporate social responsibility (CSR), long-term value creation and risk prevention, and introducing one or more CSR criteria into executives’ compensation;

b. restricting the conclusion of non-compete agreements with executives;

c. encouraging shareholders to dialogue with the board;

d. strengthening directors’ ethics regarding conflicts of interest;

e. increasing the number of directors representing employees; and

f. extending the requirement for the board to ensure the implementation of a policy of non-discrimination and diversity, notably with regard to the balanced representation of men and women in governing bodies (and not only at the board level).

Further developments took place in 2019 with the Law for an Action Plan for the Growth and Transformation of Businesses (Pacte Law) and the Order 2019-1234 on the compensation of corporate officers of listed companies together with its implementing decree. The Pacte Law, which was adopted by the French Parliament on 11 April 2019, reinforced (1) the presence of directors representing employees and (2) the transparency of the remuneration of

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4 the High Committee on Corporate Governance 2019 Annual Report (83.3 per cent of the CAC 40-listed companies have such one-tier structure).

5 2016 AMF report on corporate governance and executive compensation.

6 Paragraph 3.2 of the AFEP-MEDEF Code.

7 Prerogatives commonly attributed to the lead independent director include communications with shareholders of the company not represented on the board, prevention of conflicts of interest, evaluation of directors’ performance and remuneration, coordination of independent directors’ activities and coordination of the work of board committees.

8 Paragraph 3.2 of the AFEP-MEDEF Code.

9 Paragraph 1.7 of the AFEP-MEDEF Code.
corporate officers. Issuers are now required to provide a ratio comparing the compensation of the chairman of the board of directors and of each executive corporate officers to the average and median compensation on a full-time equivalent basis of employees within the group and the evolution of this ratio over the past five financial years.

II CORPORATE LEADERSHIP

i Board structure and practices

Structure

Listed companies in France may have either a one-tier governance structure comprising a board of directors in charge of the company’s general management together with a CEO (who may or may not be a director) who is the legal representative of the company; or a two-tier structure comprising a management board, whose chair is the legal representative of the company, and a supervisory board that supervises the management board and must not interfere in the management of the company.

Composition of the board

Under the one-tier system, the board of directors is composed of a minimum of three and a maximum of 18 members. Under the two-tier system (i.e., with a management board and a supervisory board), the supervisory board is also composed of between three and 18 members.

As a statutory requirement to have no less than 40 per cent of women10 (or men) on boards of directors or on supervisory boards as from 1 January 2017, the percentage of women on the boards of CAC 40-listed companies has continued to rise from 46 per cent in December 2018 to 46.7 per cent in 2019.

While French law does not provide for specific details concerning the presence of independent directors, corporate governance codes strongly recommend the appointment of a certain proportion of independent members. According to the AFEP-MEDEF Code, independent directors should account for half of the members of the board in widely held corporations that do not have controlling shareholders. In other corporations, at least one-third of the board should be composed of independent directors.11

Election of board members representing employee shareholders is an obligation in state-controlled companies, in listed companies where the employees hold more than 3 per cent of the share capital and in companies that employ, jointly with their subsidiaries, more than 1,000 employees in France or more than 5,000 employees worldwide, except for those that already have employee representatives on their board. There should be one employee shareholder representative on any board with fewer than eight members and two on boards with more than eight members.12 The revised AFEP-MEDEF Code also provides that the directors representing employees within a group must sit on the board of the company that takes strategic decisions for the group.

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10 Except for boards composed of more than eight members, for which the gap between the number of men and women should not exceed two.
11 Paragraph 8.3 of the AFEP-MEDEF Code.
12 Threshold reduced from 12 to 8 by the Action Plan.
Representation and management of the company

In companies with a one-tier structure, the board of directors decides whether the management of the company is carried out by the chair of the board or by a separate CEO. The CEO has the broadest powers to represent the company and act on its behalf in all circumstances. Limitations on the CEO’s powers can be set out in the articles of association or decided by the board, but are not enforceable against third parties.

In companies with a two-tier structure, the management board is vested with the broadest powers to act in any circumstances on behalf of the company, which is represented by the chair of the management board.

Legal responsibilities of the board

In companies with a one-tier structure, the board of directors is responsible for determining the corporate strategy and supervising its implementation. It is also responsible for controlling the management of the company, for appointing and removing the chair, CEO and deputy CEOs and determining their remuneration, and for convening the shareholders’ meetings.

In companies with a two-tier structure, the supervisory board supervises the management board and carries out the verifications and inspections it considers appropriate. The supervisory board also has specific attributions, which are similar to those attributed to the board of directors.

Delegation of board responsibilities

Decisions taken by the board of directors are collective decisions and cannot be delegated to one or more specific directors or to third parties.

The board of directors or supervisory board may give specific mandates to certain members to study identified issues.

Separation of roles of CEO and chair

The chair organises the work of the board of directors and chairs the meetings. He or she also ensures that the different decision-making bodies of the company operate properly. Although it is not expressly specified as being one of his or her responsibilities, the chair can communicate directly with shareholders but will remain bound by an absolute duty of confidentiality and is thus prohibited from disclosing privileged information.

Remuneration of directors and senior management

Non-executive directors’ remuneration consists exclusively of attendance fees. The Pacte Law introduced the possibility of allocating share warrants for company founders (BSPCE) to the members of the board of directors and supervisory board. Any other remuneration is prohibited, except that resulting from either an employment contract non-executive directors may otherwise have with the company for separate functions, or a special temporary assignment.

As from 2020, the total amount of attendance fees and its allocation among the directors will be subject to the say on pay procedure. In accordance with the duty of care

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imposed on board members, which requires assiduity and involvement, such fees usually include a variable portion that depends on attendance at board meetings and, as the case may be, committee meetings.

Executives’ remuneration generally includes fixed and variable components, and stock options or performance shares, or both. The AFEP-MEDEF Code provides that variable remuneration must be capped at a specific percentage of the fixed part, and that the non-executive chair of the board should not receive any variable remuneration, stock options or performance shares.\textsuperscript{14} The board must ensure that executives’ compensation aims to improve the medium and long-term performance and competitiveness of the company, in particular by incorporating one or more criteria related to social and environmental responsibility.\textsuperscript{15}

When determining the overall compensation of an executive, the board of directors takes into account all components such as bonuses, stock options, performance shares, directors’ attendance fees and pension schemes.

While it is recommended that the fixed part of the remuneration is reassessed only every three years, variable remuneration and stock options or free share awards should reward both short-term and medium-term performance. Quantitative performance criteria must be simple, objective, measurable and coherent with the corporate strategy and not solely determined by stock price. Four main categories of quantitative criteria can be identified: financial ratios (notably return on capital employed), revenue growth (as well as free cash flow, operating profit, and earnings before interest, tax, depreciation and amortisation growth), increases in the share price and performance in comparison with the company’s main competitors. It also provides that quantitative performance criteria do not necessarily have to be financial criteria.\textsuperscript{16} Furthermore, the AFEP-MEDEF Code recommends that a specific cap be set for qualitative criteria.

Benchmarking with other companies operating in the same market is common, although proxy advisers tend to consider that it is not a sufficient justification.

Executives’ remuneration is decided by the board of directors or supervisory board on the recommendation of the remuneration committee.

France provides for a say on pay mechanism with both \textit{ex ante} and \textit{ex post} approval by the shareholders.

Through the \textit{ex ante} vote, shareholders are required to approve the compensation policy, namely the elements, principles and criteria for setting, allocating and granting the fixed, variable and exceptional components of the total compensation and benefits of any kind attributable to corporate officers (including any termination or non compete indemnity).\textsuperscript{17} In addition, the law provides for a binding \textit{ex post} vote on the remuneration paid or granted to each corporate officer during the past fiscal year or in connection thereto (binding say-on-pay).\textsuperscript{18} Payment of variable or exceptional compensation is subject to the approval by the shareholders’ meeting, and no payment may take place if shareholders did not approve the relevant resolution. In addition, board members are now prevented from receiving their attendance fees in case a negative vote is issued by the shareholders.

\textsuperscript{14} Paragraph 24.2 of the AFEP-MEDEF Code.
\textsuperscript{15} Paragraph 24.1.1 of the AFEP-MEDEF Code.
\textsuperscript{16} Paragraph 24.3.2 of the AFEP-MEDEF Code.
\textsuperscript{17} Article L 225-37-2 of the French Commercial Code.
\textsuperscript{18} Article L 225-100 of the French Commercial Code.
There is no longer a cumulative application of the procedure for regulated agreements and the say on pay system. Henceforth, commitment to pay a termination fee, non-compete or top hat pensions are only be subject to the say on pay system. According to the revised Commercial Code, any amount paid out on a departure (termination fee, pension purposes) must be subject to performance conditions. It also prohibits any payment pursuant to a non-compete undertaking when the executive is able to claim his or her pension rights.

The AFEP-MEDEF Code recommends capping termination fees at a maximum of two years’ annual fixed and variable compensation, taking into account the non-compete compensation and any potential severance payment due as a result of the termination of the employment agreement, if any.19

The revised AFEP-MEDEF Code recommends prohibiting any payment pursuant to a non-compete undertaking when an executive is over 65 years old.20 The Code also recommends that a non-compete undertaking should not be entered into at the time the executive leaves when no such clause had previously been stipulated.21

Committees
An audit committee is compulsory in listed companies, the powers of which have been reinforced since the European reform of audit quality. The AFEP-MEDEF Code also recommends the creation of a remuneration committee (headed by an independent director, and with one member being an employee representative)22 and a nomination committee (the two may be combined). Members of committees should be non-executives, and a majority of such members should be independent (two-thirds in an audit committee, which must include a member with accounting and finance skills). Most companies also have other specialised committees dedicated to strategy, internal control, CSR, ethics, science and technology, and risks.

Board and company practice in takeovers
During a takeover bid, the board of directors may adopt any provisions to thwart the takeover, without shareholder approval, subject to the powers expressly granted to general meetings and with due regard to the company’s corporate interests. However, companies may amend their articles of association (with the shareholders’ approval) to opt out of the ability to adopt anti-takeover measures without shareholders’ prior approval.

ii Directors
Role and involvement of outside directors
The AFEP-MEDEF Code emphasises the importance of having a significant proportion of outside directors (or independent directors) on the board to improve the quality of proceedings. Outside directors have the same rights as other directors, but they are encouraged to play an active role and protect themselves against possible liability.

19 Paragraph 24.5.1 of the AFEP-MEDEF Code. Pursuant to a decree dated 27 July 2012, public sector executives’ remuneration was capped at €450,000 per year (i.e., 20 times the average of the lowest wages in public sector companies).
20 Paragraph 23.4 of the AFEP-MEDEF Code.
21 Paragraph 23.5 of the AFEP-MEDEF Code.
22 Paragraph 17 of the AFEP-MEDEF Code.
**Legal duties and best practice**

Directors principally have the legal duty to act in the best interests of the company and to be diligent. Pursuant to case law, other specific duties, such as the duty of loyalty and the duty of care, are also incumbent upon directors.

**Civil liability**

In companies with a one-tier structure, the chair of the board, CEO and members of the board of directors can be held liable in relation to the company, shareholders or third parties for any breach of laws, regulations or the company's articles of association, as well as wrongful acts of management by directors in carrying out their duties. Breach of the duty of loyalty is also recognised by case law.

If a wrongful act is committed, the CEO and directors may only be held liable if it can be proved that a loss has been suffered, and that there is a direct causal link between such loss and the wrongful conduct. This civil action may be brought:

a. by the company, either directly acting through its legal representatives, or through a derivative action called an *ut singuli* action, which is exercised by a shareholder acting on behalf of the company; or

b. by a third party (e.g., creditors or employees) or shareholders (who are distinct from third parties) if the loss suffered is distinct from that suffered by the company. Whereas actions brought by third parties require that the wrongful act be deemed to be unrelated to the directors’ duties (traditionally defined as wilful misconduct that is particularly serious and incompatible with the normal exercise of duties), actions brought by shareholders do not require, following a decision of the French Supreme Court, that such a condition be met.

In the case of insolvency of a company, directors who have committed acts of mismanagement can be held liable for all or part of the company's debts.

In companies with a two-tier structure, the same rules apply to members of the management board. While members of the supervisory board cannot be held liable for mismanagement, they can be held liable for negligent or tortious acts committed in the performance of their duties, and may be held civilly liable for criminal offences committed by members of the management board if, although aware of such offences, they did not report them to the general meeting.

**Criminal liability**

The chair of the board, CEO, members of the board of directors, or members of the management board and the supervisory board, can be sentenced to five years’ imprisonment, ordered to pay a fine of €375,000, or both, for having:

a. distributed sham dividends in the absence or on the basis of false inventories;

b. published or presented to the shareholders annual accounts not providing, for each financial year, a fair representation of the results of the operations; or

c. directly or indirectly used the company's assets, in bad faith, in a way that they know is contrary to the interests of the company, for personal purposes.

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23 Court of Cassation, 9 March 2010.
Appointment and term of office of directors

Members of the board of directors or supervisory board are appointed by the ordinary general meeting of the shareholders. Under certain circumstances, the board of directors may appoint new members by co-optation, subject to the shareholders’ meeting subsequently ratifying such appointments.

Directors are appointed for a term set out in the articles of association, up to a maximum of six years (four years in the two-tier system). In practice, due to the influence of the AFEP-MEDEF Code, the four-year term of office is prevalent. Re-election is possible, and almost all of the companies listed on the SBF-120 Index rotate renewal of the terms of office to avoid replacement of all directors at the same time. The office of members of the board of directors can in any event be terminated upon a decision by a shareholders’ meeting at any time, without specific reason (ad nutum).

Specific requirements include the following:

a in the absence of an express provision in the articles of association, directors over 70 may not represent more than one-third of the members of the board;

b employees may be appointed as board directors only if their employment contract corresponds to actual duties performed for the company and for as long as the employee-director remains in a position of subordination in relation to the company. The number of directors with an employment contract cannot exceed one-third of the entire board; and

c to guarantee the availability of directors, French law prohibits members of boards of directors or supervisory boards of listed companies from simultaneously holding more than five directorships. The AFEP-MEDEF Code now recommends setting this limit at three directorships for executive directors. Furthermore, executives of credit institutions and investment companies cannot hold more than three offices as executive director and more than four offices as board member.

Members of boards of directors are no longer required to hold a specific number of shares, unless such a condition is provided for in a company’s articles of association. The AFEP-MEDEF Code, however, provides that directors should be shareholders and hold a fairly significant number of shares fixed by the articles of association or the board’s internal rules.

Conflicts of interest of directors

French law and corporate governance codes require that directors must inform the board of directors of any conflicts of interest, whether actual or potential, and should abstain from participating in the discussions and voting on such matters.

Under French law there are also some prohibitions or specific procedures for related-party transactions, which can create a conflict of interest: directors are prohibited from contracting loans from the company or arranging for the company to act as guarantor in respect of their obligations. In addition, to be valid, any significant transaction between

24 The 2018 AFEP-MEDEF Code provides that an executive director should not hold more than two other directorships in listed corporations, including foreign corporations, not affiliated with his or her group. He or she must also seek the opinion of the board before accepting a new directorship in a listed corporation. Furthermore, a non-exclusive director should not hold more than four other directorships in listed corporations, including foreign corporations, not affiliated with his or her group.
the company and one of its executives or directors, a direct or indirect shareholder holding more than 10 per cent, or another company having executives or directors in common, must receive prior authorisation from the board (without the directors concerned voting and participating to such board meeting), while grounds for approving related-party transactions must be detailed and reassessed annually. Related-party transactions entered into between a parent company and a wholly owned subsidiary are no longer subject to the authorisation procedure. Finally, specific information must be given to shareholders regarding agreements entered into between a subsidiary of a company and a director or major shareholder of this company. The AFEP-MEDEF Code provides that the internal rules of the board should set out provisions on the prevention and management of conflicts of interest.25 In accordance with the new Directive on shareholders’ rights,26 the Pacte Law provides that information regarding transactions with related parties must be publicly disclosed on listed companies’ websites at the latest on the day of their conclusion, and the related party must not participate in the board’s discussions or take part in the vote on the relevant resolutions.

The auditors present a report on the authorised transactions to the shareholders’ meeting, and the shareholders vote on them. If a transaction is not approved by the shareholders, the interested party and the directors can be held liable for any adverse consequences of that transaction for the company.

III DISCLOSURE

i Financial reporting and accountability

Reporting of financial information required by French law for listed companies is subject to regulations that distinguish between periodic information and ongoing information.

Periodic information is information provided by listed companies at regular intervals. Most notably, this includes the requirement to disclose an annual financial report, a half-yearly report and quarterly financial information.

Ongoing information is information published by listed companies to notify the public without delay of all information likely to have a material impact on the share price. It also includes disclosures related to the crossing of thresholds or share transactions carried out by an issuer’s executives or board members.

Executive Order No. 2017-1162 dated 12 July 2017 reorganised the reporting obligations regarding financial information, internal control and corporate governance, requiring that the information previously contained in the management report should be divided between a new corporate governance report and the management report.

ii Auditors’ role, authority and independence

External auditors are required to audit the company’s accounting documents and check whether the accounting principles applied in the company comply with the applicable accounting standards. They certify that the annual or consolidated accounts give a true and fair view of the financial situation of the company. They draft a general report on the accounts, as well as special reports on specific corporate transactions (share capital increases, contributions in kind, related-party transactions, etc.), which are presented to the annual general meeting of the shareholders.

25 Paragraph 19 of the AFEP-MEDEF Code.
Although many listed companies used to ask their auditors to prepare specific reports on CSR matters, auditors are now required to check whether the new non-financial statement has been provided (see Sections III.iii and IV.iii).

The reform regarding auditing, which transposed Directive 2014/56/EU, was adopted in France on 17 June 2016. It features mandatory statutory auditor rotation and enhanced transparency and reporting requirements by audit firms (including a detailed report to shareholders, a report intended for the audit committee and a report for the authorities on any irregularities). It also establishes a list of non-audit services that cannot be provided by the statutory auditor or audit firm to the audited entity, imposes limitations on the fees charged for non-audit services and enhances the role of the audit committee.

### Corporate social and environmental responsibility

Over the past few years, corporate social and environmental responsibility has been increasingly taken into account in the corporate governance of listed companies. As no reference guide exists regarding this matter, in 2014 the MEDEF issued the first guide on CSR initiatives to support the sharing of best practices. Furthermore, the government issued a report on CSR, providing advice to reinforce the involvement of companies in CSR issues, and launched a CSR Platform, a think-tank supervised by the Prime Minister. Directive 2014/95/EU of the European Parliament dated 22 October 2015 (transposed into French law by executive order No. 2017-1180 dated 19 July 2017) introduced an obligation to disclose non-financial and diversity information for large companies (the non-financial statement). Henceforth, large companies have to explain the environmental and social risks related to their activities and how they intend to manage such risks through a statement on the non-financial performance to be included in the annual management report.

French Law No. 2017-399 dated 27 March 2017 also introduced the obligation for companies employing at least 5,000 employees in France or at least 10,000 employees worldwide to develop and enact annual vigilance plans detailing steps taken to detect risks and prevent serious violations with respect to human rights and fundamental freedoms, and the health and safety of persons and the environment, which result from activities of the company and of its subsidiaries, suppliers and subcontractors.

### CORPORATE RESPONSIBILITY

#### Risk management

French listed companies must set up a special risk committee, known as the audit and risks committee, which is responsible for issues relating to internal control and risk management.

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27 Non-audit services are capped at 70 per cent of annual fees.

28 For example, CSR committees have been created.


30 See the report entitled ‘Organisations’ responsibility and performance’ dated 13 June 2013.
ii Compliance policies and whistle-blowing
The Sapin II Law has introduced legal protection for whistle-blowers, in both public and private organisations, for any alerts in any field when there is a threat to the public interest.31 Whistle-blowers are granted immunity from criminal liability under certain conditions.32 Several rules also provide for alert procedures in, for example, the fields of labour law (in cases of discrimination or harassment) and banking (in cases of money laundering suspicions). External auditors are also required to inform the board of any irregularities found during their audit.

iii Corporate social responsibility
CSR has been progressively taken into account under French law.33 In particular, French listed companies are obliged to publish data in the statement on non-financial performance to be included in their management reports. Information on how they take into account the social and environmental consequences of their activity, as well as, for some companies, the effects of this activity with respect to human rights and the fight against corruption and tax evasion, must be provided in this report.34 The AFEP-MEDEF Code also provides that the board should ensure that measures are implemented to prevent and detect corruption and influence peddling.35 The AMF also recommends36 that issuers draw up a list of the types of industrial and environmental risks, and provide a description of material risks to which they are exposed as a result of their business activities and characteristics.

The revised AFEP-MEDEF Code now provides that the board of directors should endeavour to promote long-term value creation by the company by considering the social and environmental aspects of the company's activities.37 Accordingly, the board should be informed of the main CSR issues,38 and should review financial, legal, operational, social and environmental risks as well as the measures taken to reduce such risks.39 Shareholders and investors should be informed of the significant non-financial issues for the company.40

The Pacte Law also focuses on the sharing of value within companies and on companies’ social commitment. The legal definition of ‘corporate interest’ have been broadened and it is now expressly specified that corporations must be managed in the interests of all stakeholders by considering the social and environmental concerns of its activity. Companies are also able to define in their articles of association the principles that guide their business policy and strategic decisions. The Pacte Law also introduces a new type of company, called a ‘company with a mission’, the corporate purpose of which will be defined in the articles of association as the pursuit of social and environmental objectives.

31 Except for medical secrecy, legal privilege, and intelligence and national security secrets.
32 Article 122-9 of the French Criminal Code.
35 Paragraph 1.6 of the AFEP-MEDEF Code.
36 See AMF Recommendation on risk factors, dated 29 October 2009.
37 Paragraph 1.1 of the AFEP-MEDEF Code.
38 Paragraph 1.4 of the AFEP-MEDEF Code.
39 Paragraph 1.5 of the AFEP-MEDEF Code.
40 Paragraph 4.3 of the AFEP-MEDEF Code.
V SHAREHOLDERS

i Shareholder rights and powers

Equality of voting rights

The Commercial Code lays down a principle of proportionality of voting rights, according to which voting rights attached to capital or dividend shares must be in proportion to the share of the capital they represent. However, it provides for the following exceptions:

a shares that are fully paid up and that have been registered in the name of the same shareholder for at least two years are automatically granted double voting rights, unless the articles of association provide otherwise following a shareholder decision. It appears that a large number of companies have opted out and maintained the one share, one vote principle, in accordance with proxy advisers’ recommendations;

b the voting rights attached to preference shares can be suspended or cancelled;

c limitation of voting rights: for example, a potential target’s articles of association may include a provision limiting the number of votes that may be exercised by a single shareholder, regardless of the number of shares held. Under AMF rules, however, these voting right limitations will be inoperative where a party acquires two-thirds or more of a target’s outstanding share capital or voting rights through an offer; and

d the Action Plan provides that unlisted companies are able to issue preference shares with multiple voting rights.

Powers of shareholders to influence the board

Shareholders’ rights regarding corporate governance remain limited, although it can be noted that they have been an increasing influence in France through the introduction of the mandatory say-on-pay. Their only means of action is in exercising their voting rights at shareholders’ meetings on the appointment or dismissal of board directors on related-party transactions and on rejecting say-on-pay resolutions, which will result in the company being prohibited from paying the relevant corporate officers the variable and exceptional component of their compensation.

When they represent a certain percentage of the share capital, shareholders can propose their own candidates to the shareholders’ meeting. In addition, the shareholders’ meeting can decide at any time to replace the board. Shareholders may also put questions to the board on corporate governance matters, which the board must answer at the shareholders’ meeting, or request, in court, the appointment of an expert who will present a report on a specific transaction. Finally, decisions or actions of the company violating mandatory provisions relating to remuneration and related-party transactions may be cancelled at the request of a shareholder.

Decisions reserved to shareholders

Decisions reserved to shareholders are those that fall within the ambit of the ordinary or extraordinary general meetings of shareholders. Ordinary general meetings of shareholders may notably decide on, inter alia, the approval of the annual accounts, appointment and dismissal of directors or members of the supervisory board, appointment of auditors and approval of related-party transactions. Extraordinary general meetings of shareholders can amend the articles of association of the company and decide, inter alia, to increase or reduce the share capital.
Rights of dissenting shareholders

Dissenting minority shareholders may bring a claim arguing that majority shareholders have committed an abuse of majority, which, if successful, could result in cancellation of a decision and the award of damages. This cause of action requires that two cumulative conditions be met: the decision must have been taken with the sole purpose of favouring the members of the majority to the detriment of minority shareholders, and it must be contrary to the company’s corporate interests.

Benefits for long-term shareholders

Besides automatic double voting rights, which are only granted to shareholders evidencing that they have held their registered shares for at least two years, listed companies may grant loyal shareholders increased dividends, also known as loyalty dividends. French law provides that payment of such loyalty dividends also requires that the shares have been held for more than two years. In addition, such dividends may not be more than 10 per cent higher than ordinary dividends, and the relevant shares must represent, for a particular shareholder, no more than 0.5 per cent of the company’s capital.

Board decisions subject to shareholder approval

Related-party agreements are subject to shareholder approval, as are all decisions that fall within the scope of the ordinary or extraordinary general meetings of the shareholders.

The AMF also recommends that listed companies organise a consultative vote of the shareholders prior to making any disposal of a significant asset. In addition, to better supervise all major asset disposals, the AMF requests more detailed reporting from shareholders and recommends that best practices be followed to demonstrate that the transactions are in accordance with the corporate interest.

Shareholders’ duties and responsibilities

Controlling shareholders’ duties and liability

Pursuant to the AFEP-MEDEF Code, controlling shareholders must take particular care to avoid possible conflicts of interest, ensure transparency of the information provided to the market and equitably take all interests into account. They may be held personally liable if they use their votes in their own interest to the detriment of other shareholders and the company (majority abuse).

Institutional investors’ duties and best practice

The AFEP-MEDEF Code does not specifically address the issue of institutional investors. There is a separate governance code for asset managers containing recommendations on voting at shareholders’ meetings of the companies in which the funds are invested, and reporting on such voting. In addition, the AMF has required that asset management companies report to shareholders and unit holders of collective investment schemes about their practices as regards exercising voting rights in the sole interest of shareholders and to provide an explanation if they do not exercise these rights.

The Pacte Law aims to transpose the Directive as regards the encouragement of long-term shareholder engagement, and provides that institutional investors and asset managers will have
to disclose their engagement policy describing how they integrate shareholder engagement into their investment strategy, and disclose key information about the performance of their mandates. It also provides that proxy advisers must:

a explain any instances of non-compliance with their code of conduct;

b provide key information on the preparation of their research, advice, voting recommendations, and the prevention and management of any actual or potential conflicts of interest or business relationships that may influence their activities; and

c disclose any such information, as the case may be.

iii Shareholder activism

Say on pay
The Sapin II Law has implemented a mandatory and binding regime for the say-on-pay procedure.41 Such procedure was further reinforced in November 2019, via an Order transposing into French law the main provisions of Directive 2017/828 amending Directive 2007/36/EC as regards the encouragement of long-term shareholder engagement adopted on 17 May 2017.

In light of such developments, proxies agencies will be in a position to strengthen their pressure on companies through the say on pay mechanism.

Proxy battles
Shareholders of French listed companies can appoint any person as proxy, thus giving rise to an increase in the use of professional proxy solicitors.

Professional proxy solicitors must disclose their voting policy. On 18 March 2011, the AMF published a specific recommendation,42 which notably urges proxy advisers to issue voting policies in a transparent manner, communicate with listed companies, submit draft reports to the relevant company for review and take measures to avoid conflicts of interest.

Since a report issued on 19 February 2010, the European Securities and Markets Authority also recommends that proxy advisers issue a code of conduct regarding conflicts of interest, transparency and communication with the shareholders. In March 2014, six proxy advisers made public their Best Practice Principles for Shareholder Voting Research and Analysis.43 In October 2017, the Best Practice Principles Group undertook a stakeholder consultation to evaluate the effectiveness of such principles and to consider what actions are needed to ensure that these are fully compatible with the requirements of the revised European shareholders’ rights directive.

Long-term shareholder value
Directive 2017/828 on shareholders’ rights aims to encourage long-term shareholder engagement, in particular by facilitating the identification of shareholders. It enables companies to communicate with their shareholders with a view to facilitating the exercise of

42 See AMF recommendation on risk factors, dated 29 October 2009.
43 Glass, Lewis & Co, Institutional Shareholder Services Inc, Manifest Information Services Ltd, PIRC Ltd and Proxinvest and IVOX GmbH, which has been acquired by Glass, Lewis & Co.
shareholder rights. The Pacte Law transposed this set of measures and to adapt the French regime with regard to shareholder identification. In October 2018, the AMF issued seven new recommendations to:

- better identify shareholders;
- improve information provided to shareholders on votes processing;
- encourage their effective participation in general meetings; and
- promote the modernisation of voting processes.\(^{44}\)

Law No. 2019-744 dated 19 July 2019 provides that the majority required for making decisions in shareholders meetings will now be determined only regarding the votes made by shareholders present or represented (e.g., votes expressed do not include those attached to the shares for which the shareholder did not take part in the vote, refrained from voting or made a blank or null and void vote). Accordingly, abstentions and blank or null and void votes will not be counted as negative votes any longer.

A good practice code has been issued by an association, the Best Practice Principles for Shareholder Voting Research Providers, which provide for general principles to be applied by proxy agencies. Such proxy agencies are required to disclose their voting policy and rules governing their analysis and research approach.

Following the AMF recommendations, a report of the Finance Committee of the Assemblée Nationale issued a report on October 2019 on shareholders’ activism and several other non-governmental entities (i.e., the AFEP, Paris Europlace etc.) have issued reports on these topics of shareholders’ activism.

iv  **Takeover defences**

**Shareholder and voting rights plans, and similar measures**

A French company may first try to identify its shareholding by providing in its articles of association an obligation to disclose any interests over 0.5 per cent in its share capital or a right to request certain information from the central securities depository (Euroclear France) as to the identity of its shareholders and the size of their shareholdings.

In addition, articles of association may include a provision limiting the number of votes that may be exercised by a single shareholder. Such limitation will, however, be suspended for the duration of the first shareholders’ meeting following completion of the offer, provided that the offeror has acquired at least two-thirds of the target’s shares in the offer.

The directors also have the right to take measures to frustrate an unsolicited offer, provided that such measures are not against the corporate interests of the target company. As a consequence, the target’s board is not required to obtain the prior authorisation of the shareholders before implementing a sale or acquisition of strategic assets, the sale of a block of treasury stocks to a white knight or arranging a counter-offer.

By way of derogation, the company’s articles of association may impose an obligation of neutrality on the management of the target during offer periods.

It can be noted that proxy advisers and institutional investors recommend voting for the implementation of statutory limitations preventing the board from putting defensive measures in place, and against financial authorisations that are not suspended in cases where an offer is filed.

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\(^{44}\) AMF report on shareholders’ rights and voting at general meetings, published on 5 October 2018.
French law also permits equity warrants to be issued during an offer period. The warrants may be issued free of charge to all shareholders of the target prior to closing of the offer and may entitle the holders to subscribe for new shares on preferential terms. Such issuance can be authorised by the shareholders:

a. either during the offer to allow the target to defend a hostile bid (in which case the shareholders’ authorisation only requires a simple majority of votes cast at a shareholder meeting, whereas an authority to issue equity securities directly usually requires a two-thirds majority vote of the votes cast, and only a quorum of 20 per cent on first call and no minimum on second call (instead of 25 and 20 per cent, respectively, in a normal extraordinary general meeting); or

b. in advance, in view of a potential offer, by way of delegation given by the shareholders to the board of directors that can be used during an offer period.

White-knight defence

There should be no legal objection to a target board seeking a third party (a white knight) to make a competing offer for the target. Theoretically, a target could alternatively issue new shares to a third-party ‘friendly’ shareholder. However, such an issue would generally require specific shareholder approval, and therefore such a tactic would, in practice, be unusual.

When arranging for a white-knight defence, the target’s board of directors must comply with the company’s interest and ensure that it does not infringe the principle of free interplay of bids and counterbids and maintains a level playing field.

Staggered boards

The AFEP-MEDEF Code recommends avoiding replacement of the board as a whole to enhance a smooth replacement of directors. As a result, French companies commonly use staggered boards.

The efficiency of staggered boards as a takeover defence under French law is limited, as the general meeting of the shareholders may dismiss directors at any time and without cause.

Contact with shareholders

Mandatory and best-practice reporting to all shareholders

Listed companies have developed various communication practices that differ for individual shareholders or financial investors.

Financial communication tools (specific sections of the company’s website, financial publicity, publication of a shareholders’ letter, shareholders’ guides and even custodial services) and club and advisory committees are generally used to maintain contact with individual shareholders. To assist listed companies, notably in the use of social media as a means of sharing information, the AMF has published several recommendations and created briefing sheets covering usage and best practices in different areas, ranging from online and social media strategies to shareholder guides and consultative committees.

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45 Paragraph 13 of the AFEP-MEDEF Code.
46 AMF Recommendation 2014-15 for listed companies on communication using their websites and social media, now included in the AMF Guide on ongoing information 2016-08, AMF Recommendation 2015-09 on communication by companies aimed at promoting their securities among individual investors, and AMF, study on communication practices among listed companies December 2015.
Telephone or individual meetings, roadshows, conferences organised by brokerage firms, analysts’ and investors’ days, and on-site visits are used to communicate with institutional and financial investors.

Selective meetings and communications, circumstances of meetings with individual shareholders

It is customary for investor relations services to organise meetings or conference calls with large shareholders prior to shareholders’ meetings. This same approach may be taken with proxy advisers, who also often seek meetings with the chair of the remuneration committee. These meetings allow shareholders to be fully informed before voting. The AFEP-MEDEF Code provides that the chair of the board or the lead director, if one has been appointed, will be responsible for the board’s relations with the shareholders, particularly with regard to corporate governance aspects. In accordance with this recommendations, a large number of listed companies (26 out of the 40 companies of the SBF 120 index examined in 2019 by the AMF in its annual report) have a board member (either the chairman or a lead director) who is responsible for discussing with shareholders, in particular with those who are not represented on the board of directors.

Individual meetings may also be organised regularly between senior executives, investor relations departments and analysts and investors. For investors, one-on-one meetings provide an opportunity to assess, inter alia, the vision that senior managers have for their company, their analysis of the competitive environment and market trends.

Executives should, of course, be especially careful not to disclose privileged information, in particular in view of the entry into force on 3 July 2016 of Regulation (EU) 596/2014 on market abuse, which, among other things, widens the scope of regulation regarding market soundings and raises the amount of the penalties.

Listed companies generally have quiet periods preceding the release of their annual, half-yearly and quarterly financial information during which they must refrain from any contact with analysts and investors.

Information received by shareholders before shareholders’ meetings

Shareholders are informed of the date of a meeting 35 days in advance. Companies make certain documents available on their websites at least 21 days before the meeting. Such documents must include, inter alia, a summary statement of the company’s situation and its annual financial statements, and draft resolutions.

VI OUTLOOK

Over the past few years, investors and proxies have gained some traction in their ability to influence companies and push for more disclosure and diversification. The development of these trends has become apparent in French corporate governance regulation. Based on the various reforms conducted in 2019, such trends will no doubt continue.

47 Paragraph 4.4 of the AFEP-MEDEF Code.
48 Speech by Robert Ophéle, AMF Chairman – Droit & Croissance Conference ‘Corporate governance and shareholders engagement: the new normal conference’ – Friday 18 October 2019.
Whereas gender diversity has been successfully implemented in boards of directors or supervisory boards of public listed companies, the regulators now focus on the feminisation of executives positions (e.g., CEO, chair, deputy CEO). The Pacte Law introduced provisions requiring issuers to enhance selection processes of executives that guarantee the presence of at least a person of each sex amongst the applicants. This follows the revision of the AFEP-MEDEF Code that now recommends that executive officers implement a policy of non-discrimination and diversity in the governing bodies, and further developments may be expected on this point.

In 2019, shareholder activism was the subject of intense debate in France. Whereas opinions are divided about the opportunity to amend the legal environment, a consensus seemed to emerge on the relevance of reinforcing shareholder dialogue and transparency. Several reports have been issued by the French national assembly and other non-governmental bodies (i.e, Club des Juristes, Paris Europlace, etc.) on shareholder’s activism, which are likely to lead to recommendation and legal reforms.

The AMF is likely to have a close look to the proxy agencies following the implementation of the Action Plan as the French legislator has entrusted the AMF with the task of preparing an annual report on the application of new transparency provisions by proxy advisers operating in France as from 2020.

Several listed companies already amended their by-laws to include their purpose during the 2019 annual general meeting and many others have indicated their intention to do so in the near future.

Finally, political pressure shall keep bolstering the debate around the sharing of values within companies and on companies’ societal commitment. As introduced by the Action Plan, the obligation for companies to take into account the social and environmental concerns of their activities that ultimately lead the companies to be more accountable to their stakeholders will be watched closely by the market.

49 Paragraph 1.7 of the AFEP-MEDEF Code.
I OVERVIEW OF GOVERNANCE REGIME

Germany has one of the most solid corporate governance systems in the world owing to its well-balanced control mechanisms, capital preservation and market transparency rules as well as equal opportunities for women and men.

The German stock corporation is the common legal form among listed companies in Germany. Its corporate governance regime is determined by the following statutory provisions and non-binding best practice rules:

- the Stock Corporation Act, which sets out the – largely mandatory – framework for the organisation of a stock corporation as well as the rights and duties of the corporate bodies, the management board, the supervisory board and shareholders’ meeting, as well as the shareholders;
- the EU Market Abuse Regulation (MAR), which governs market abuse and market manipulation, disclosure of non-public information and directors’ dealings;
- the Securities Trading Act, containing provisions on the enforcement of violations of the MAR under German law;
- the Securities Acquisition and Takeover Act, which provides for rules on mandatory and voluntary takeover offers and defensive measures;
- the Co-Determination Act and the One-Third Participation Act, granting employees co-determination rights at the supervisory board level;
- the Commercial Code, which stipulates the general accounting rules for German companies; and
- non-binding guidelines on non-financial reporting, which were published by the EU-Commission in 2017 and last updated on 18 June 2019.

The German Corporate Governance Code is a collection of best practice rules and non-binding recommendations for the corporate governance of stock corporations, which has a growing influence on how corporate governance is practised in Germany.

Although the rules and recommendations set out in the Corporate Governance Code are not legally binding, the company must explain the extent and the reasons for non-compliance (the ‘comply or explain’ principle).

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1 Dr Carsten van de Sande and Dr Sven H Schneider are partners at Hengeler Mueller Partnerschaft von Rechtsanwälten mbB. The authors thank Dr Conrad Ruppel, senior associate at Hengeler Mueller Partnerschaft von Rechtsanwälten mbB, for his contribution to this article.
II CORPORATE LEADERSHIP

i Board structure and practices

Mandatory two-tier structure
The two-tiered board structure of German stock corporations requires a management board and a supervisory board.

Composition of the management board
The management board must consist of natural persons who are appointed by the supervisory board. The Corporate Governance Code requires that, when appointing management board members, the supervisory board must pay attention to diversity and shall, in particular, aim for appropriate representation of women on the management board.

Members of the management board may not be appointed for a period exceeding five years. For first-time appointments, the new Corporate Governance Code recommends that members of the management board should not be appointed for more than three years. The appointment may be renewed or the term of office may be extended, provided that the term of each such renewal or extension does not exceed five years.

The supervisory board may only dismiss members of the management board for good cause. Good cause is, in particular, deemed to exist in the event of material breaches of duty; for example, if a management board member is not able to properly fulfil his or her duties (e.g., owing to long-lasting illness or a lack of required skills or knowledge) or where the general meeting has adopted a vote of no-confidence and provided that the vote has not been adopted for apparently inappropriate reasons.

Composition of the supervisory board
The supervisory board must consist of at least three members, who are generally elected by the shareholder’s meeting. The maximum number of supervisory board members permitted by law increases depending on the amount of the stock corporation’s registered share capital. In any event, the total number of supervisory board members must be divisible by three.

Where a stock corporation generally has more than 500 employees, one-third of the supervisory board members must be employee representatives. In companies with more than 2,000 employees, half of the supervisory board members must be employee representatives. At least 30 per cent of the supervisory board members of listed companies with more than 2,000 employees must be women. In addition, companies with more than 500 employees must adopt certain target ratios regarding the representation of female members on their supervisory and management boards as well as in their senior management.

According to the Corporate Governance Code, the supervisory board should be composed in such a way that its members jointly have the knowledge, ability and experience to properly carry out its tasks and shall include an adequate number of independent members.

Supervisory board members are considered to be independent from the company and its management board if they have no personal or business relationship with the company or its management board that may cause a substantial – and not merely temporary – conflict of interest. More than half of the shareholder representatives shall be independent from the company and the management board. The new Corporate Governance Code defines a supervisory board member as independent from the controlling shareholder, if he, she or
a close family member is neither a controlling shareholder nor a member of the executive governing body of the controlling shareholder and does not have a personal or business relationship with the controlling shareholder that may cause a substantial conflict of interest.

In practice, the supervisory board members are appointed for a period of five years; renewed appointments are permissible.

ii Legal responsibilities and representation

Management board

The management board is responsible for managing the business of the stock corporation and legally represents the corporation in relation to third parties. Under the statutory concept, all members of the management board manage and represent the corporation jointly. However, in practice, the rule is that the corporation is represented by each member of the management board acting individually or by two members of the management board acting jointly.

In managing the business of the corporation, the members of the management board must apply the care of a prudent and diligent businessperson. According to the duty of loyalty, each management board member is obligated to give the stock corporation's interest priority over their personal interests. Failure by a management board member to meet these duties may lead to personal civil law liability for damages of the company.

A member of the management board cannot be held personally liable if, in making an entrepreneurial decision, he or she had adequate information and believed they were acting in the best interests of the stock corporation. This ‘business judgement rule’ applies in the context of decisions that are not predetermined by the law, the articles of association or resolutions of the shareholders’ meeting. The management board is considered to have had adequate information for making its decision if it has consulted all sources of factual and legal information reasonably available to it in the specific situation and, on that basis, has weighed the advantages and disadvantages of its decision against each other. However, it is not required that all conceivable information is obtained and every conceivable impact is quantified before making the decision.

The management board is subject to a duty of legality. This means that the management board may not itself commit, and may not order third parties to commit on behalf of the company, any violations of the law. In an unclear legal situation, the board members may also rely on the advice of a third-party expert. The members of the management board may rely on the third party expert’s advice if: (1) they have provided the expert with the necessary documents and a comprehensive description of the facts to be examined; (2) the expert is independent and professionally qualified to advise on the issue; and (3) they carry out a careful plausibility check of the advice provided by the expert.

The management board must ensure that all employees of the company, when acting within the scope of their operational activities, act in compliance with the law. This presumes that the management board must establish an appropriate system of organisation and control to prevent violations of law from within the company.

The management board is obligated to manage the stock corporation independently. It is not subject to instructions by the supervisory board or the general meeting. However, the shareholder’s prior consent is required for transactions of outstanding importance, for example, selling the most valuable parts of the company, or if by-laws of the management board provide for the shareholder’s consent.

Apart from that, material transactions with related parties are subject to prior approval of the supervisory board or, if the supervisory board refuses to grant its approval, by the
general meeting. Whether a transaction is deemed to be material is determined by a number of aspects such as the influence that the information about the transaction may have on the economic decisions of shareholders or the risks associated with the transaction. A transaction constitutes a material related-party transaction if its economic value is at least 1.5 per cent of the total of the company’s fixed and current assets. No approval is required for transactions that are concluded in the ordinary course of business and on customary market terms or for transactions with directly or indirectly wholly owned subsidiaries. Companies must publicly announce related-party transactions at the latest when the transaction is concluded, which is when the transaction documents are signed.

**Supervisory board**

The supervisory board is responsible for supervising and controlling the management board. To this end, the supervisory board is entitled to inspect the corporation’s books and records and may, at any time, request the management board to report about the corporation’s affairs.

Like members of the management board, members of the supervisory board must act in the best interests of the stock corporation and must demonstrate the care of a prudent and diligent businessperson. They are obligated to keep confidential any non-public information that they receive in their capacity as supervisory board members. One of the notable responsibilities of the supervisory board is enforcing damage claims of the stock corporation against members of the management board. In particular in the wake of the global financial and economic crisis of 2008, this has led to a significant increase in the number of lawsuits brought by corporations against former members of the management board.

The supervisory board’s responsibility to supervise the management imposes a duty to avert actions by the management that may be detrimental to the company and that do not fall within the ambit of the business judgement rule. A supervisory board member may even be subject to criminal liability if, by consenting to certain transactions, the supervisory board member allows behaviour of the management that is not covered by the business judgement rule.

### iii Delegation of board responsibilities

All members of the management board manage the stock corporation collectively and are jointly responsible for their actions.

In practice, responsibility for the management of certain business divisions or certain functions (e.g., finances, accounting, controlling, human resources, tax, legal, compliance) is delegated to individual members of the management board. Insofar, each management board member is primarily responsible for her or his delegated tasks, but the other board members still monitor and control the other members’ performances within their divisions. As a general rule, it is deemed to be sufficient to carefully, continuously and appropriately observe developments in the delegated divisions or functions and the performance of other management board members’ duties.

### iv Roles of the chair of the management board and the chair of the supervisory board

Where the management board consists of more than one person, the supervisory board may appoint one of them as chair. The chair is responsible for administrative tasks relating to the work of the management board, such as preparing and chairing meetings and keeping minutes, as well as for coordinating and supervising the work of the management board.
He or she typically is in charge of liaising with the supervisory board and represents the management board in public, and thus has a prominent position among the other members of the management board. The manner in which many chairs of management boards discharge these responsibilities in practice has given rise to the perception that the position is comparable to that of the chief executive officer of a US corporation. However, from a legal perspective, this is not the case. In particular, the chair has no right to give instructions to other management board members and is not entitled to decide matters against a majority of the other members of the management board.

The members of the supervisory board must elect a chair and a deputy chair. The chair of the supervisory board is a largely administrative role that is not endowed with any particular powers. The chair calls, prepares and leads meetings of the supervisory board. Typically, the articles of incorporation provide that the chair of the supervisory board also chairs the general meeting.

v Compensation of members of the management board and the supervisory board

In accordance with the German law implementing the Shareholder Rights Directive (EU) 2017/828 (SRD II) and the new German Corporate Governance Code, the compensation of each member of the management board (e.g., fixed salary, variable salary components and pensions) must be clear, comprehensible and reasonable in light of the responsibilities and individual performance of that management board member as well as the situation of the company. It is required to determine the total remuneration in the event that all agreed goals are achieved as well as to set a ‘cap’ for the maximum remuneration of the management board. In addition, the share of long-term variable remuneration of members of the management board shall exceed the share of short-term variable remuneration also by taking into account the sustainable corporate development as well as social and ecological aspects.

The compensation of members of the management board is determined by the supervisory board, usually following a recommendation by a committee established for that purpose. Pursuant to the German law implementing SRD II, the general meeting must vote on the company’s remuneration policy in the event of a material change but at least every four years. Since the German two-tiered board structure still requires that the supervisory board determines the management board compensation, the vote of the general meeting has an advisory function and is non-binding only. The general meeting cannot change the management board’s remuneration policy but it has now the right to vote against the maximum remuneration of the management board (‘cap’) as set by the supervisory board.

The compensation of the supervisory board is determined in the articles of incorporation or by the general meeting. Pursuant to the German law implementing SRD II, the general meeting is obligated to resolve upon the supervisory board’s compensation on a four-year basis. Like the management board members’ compensation, it must take into account the duties of the supervisory board member and the condition of the company. The supervisory board members’ compensation may also comprise variable components based on the corporation's long-term performance.

Listed stock corporations must disclose the aggregate and individual remuneration granted to members of the management board and the supervisory board, respectively, in their financial statements. In addition, the German law implementing SRD II and the new German Corporate Governance Code require that the management board as well as the supervisory board prepare an annual remuneration report. The information in the remuneration report
is extensive and includes a five-year comparison of a member’s compensation, the company’s earnings performance and employee compensation. The remuneration report must be formally reviewed by the auditor and made publicly available on the company’s website.

vi Committees
The supervisory board is not required to, but may form committees, in particular for the purpose of preparing its deliberations and supervising the implementation of its resolutions.

Where the supervisory board is composed of both shareholders and employee representatives, the supervisory board must form a reconciliation committee composed of the chair of the supervisory board, his or her deputy and one member of the supervisory board elected by the shareholder and the employees, respectively.

The supervisory board may establish an audit committee to deal with matters relating to the preparation of the corporation’s financial statements, the effectiveness of the internal audit and risk management systems. The audit committee is also responsible for monitoring the accounting process and the efficacy of the internal control system. The Corporate Governance Code recommends that the chairman of the audit committee should have specialist knowledge and expertise in the application of accounting principles and internal control processes.

The Corporate Governance Code further recommends forming a nomination committee that is composed exclusively of shareholder representatives and that is tasked with proposing suitable candidates that the supervisory board may recommend to the general meeting for election to the supervisory board.

vii Board and company practice in takeovers
In the event a company becomes the target of a takeover offer, the management board and the supervisory board must publish a reasoned statement regarding the offer on the internet. The statement is intended to enable the shareholders to make an informed decision on the offer and must, in particular, contain the management board and the supervisory board’s assessment of the consideration offered by the bidder, the expected consequences of a successful takeover offer for the company, its employees, the employee representatives (i.e., the works council), the terms and conditions of employment and the company’s production and other sites, the goals pursued by the bidder, and information on whether the members of the management board and the supervisory board intend to accept the offer.

III DISCLOSURE

i Regular reporting and disclosure requirements
Stock corporations must disclose their annual financial statements (consisting of the corporation's balance sheet and profit and loss statement as well as the notes thereto) by publishing them electronically in the German Federal Gazette. Together with the annual financial statements, the management report of listed stock corporations and other companies must contain a corporate governance statement including:

a. statements regarding compliance with the Corporate Governance Code;

b. information regarding any practices and standards applied by the corporation in addition to statutory requirements, such as codes of conduct;

c. information regarding the composition of boards and committees as well as the manner in which they conduct their affairs; and
information on the concept of diversity addressing specific aspects such as age, gender, educational or professional background.

As part of the management report, large capital market-oriented corporations as well as certain credit institutions and insurance companies are also obligated to submit a non-financial declaration. This includes information on the approach adopted by the company to improve environmental, employee and social issues, respect for human rights and the fight against corruption as well as information on the result of the measures taken to date. If no particular approach is pursued for one of these matters, this is to be justified in sense of the ‘comply or explain’ principle.

Within the first three months of each financial year, the management board of a stock corporation on which another enterprise can exercise a dominating influence must prepare a report on the corporation’s relations with affiliated companies.

**Disclosure of inside information**

As a general rule, any issuer of securities that are admitted or requested for admission to trading on an organised market or multilateral trading facility in Germany must disclose, without undue delay, any information directly relating to the issuer that is not publicly known, if the information could have a material impact on the market price of the relevant securities.

Disclosure of this information must be made in German language in at least one mandatory stock exchange newspaper of nationwide circulation or through a system for the electronic dissemination of information, as well as on the issuer’s website. Prior to disclosing it to the public, the issuer must inform the management of each stock exchange on which the securities or derivatives thereof are traded and the Federal Financial Supervisory Authority of the information.

An issuer may, on its own responsibility, delay disclosure of inside information, if (1) disclosure is likely to prejudice the issuer’s legitimate interests, for example during ongoing contract negotiations concerning material assets of the company or in restructuring situations, (2) the delay is not likely to mislead the public, and (3) the issuer ensures the confidentiality of the inside information. Upon disclosure, the issuer must inform the Federal Financial Supervisory Authority of this, and of why disclosure was delayed.

**ii Directors’ dealings**

Members of the management board and the supervisory board of an issuer as well as all other senior executives with regular access to inside information are obligated to notify both the issuer and the Federal Financial Supervisory Authority, within three business days, about transactions conducted on their own account relating to (1) shares or debt instruments of the issuer that are traded on the financial markets, or (2) financial instruments linked thereto (e.g., derivatives). The disclosure obligation also relates to transactions for the account of legal entities, trusts or persons closely associated with the issuer’s board members or senior executives, such as spouses, registered partners or dependent children. Relevant transactions include purchase and sale, as well as pledging and lending of the relevant financial instruments.

The disclosure obligation does not apply if the total value of all transactions conducted by a single person within a calendar year does not exceed €5,000.
The issuer is responsible for ensuring that information regarding the relevant transactions are published without delay, at the latest three days after the transaction, in media suitable for the dissemination throughout the European Union. In addition, the issuer is required to submit the published information to the German company register.

iii  Disclosure of shareholdings in listed companies

Any person whose shares of a company with its corporate seat in Germany reach, exceed or fall below the thresholds of 3 per cent, 5 per cent, 10 per cent, 15 per cent, 20 per cent, 25 per cent, 30 per cent, 50 per cent or 75 per cent of the voting rights in the company is obligated to disclose this circumstance to the Federal Financial Supervisory Authority. This applies for shareholders who are admitted to trading on the organised market on a stock exchange of a member state of the European Union. Furthermore, they have to disclose the issue to the company without undue delay, but in no event later than four trading days thereafter. The company must then pass on the information without undue delay, namely within three trading days, to ‘a combination of media for Europe-wide dissemination’ as well as to the German company register.

For the purpose of calculating the relevant threshold amounts, voting rights arising from shares held by a third party may be attributed to the person obligated to disclose the shareholding. Voting rights will, for example, be attributed if the third party is a subsidiary of the person obligated to disclose the shareholding, or if the person obligated to disclose the shareholding, by other means has a controlling influence on the exercising of the voting rights arising from the shares. The same holds true for shares held by third parties who act in concert with the person obligated to disclose the shareholding.

IV  CORPORATE RESPONSIBILITY

All publicly listed companies and other German companies have adopted modern compliance programmes and created a compliance organisation that is headed by a chief compliance office or a member of the management board to whom responsibility for compliance has been delegated.

Nearly all compliance programmes emphasise the importance of the ‘tone from the top’ for a corporation’s compliance culture, and measures are taken to ensure compliance manuals are distributed and employees are trained with respect to compliance-related issues. Many companies have established whistle-blowing hotlines where employees can report misconduct anonymously (see Section VI.ii).

In addition, companies must disclose non-financial information that is deemed to be vital for a change towards a sustainable global economy by combining long-term profitability with social justice and environmental protection.

V  SHAREHOLDERS

i  Shareholder rights and powers

As a general rule, all shares in a German stock corporation provide for equal rights, including equal voting rights, rights to receive dividends and information rights.
Voting rights are usually exercised per share or in proportion to the par value of the shares. The Stock Corporation Act prohibits the creation of shares with multiple voting rights. With the approval of the general meeting, a stock corporation may issue non-voting preferred shares in a nominal amount of up to half of its registered share capital.

The shareholders of a stock corporation, unlike shareholders of German limited companies, have no direct influence on the management board. Their influence is limited to electing the members of the supervisory board, who in turn appoint and remove the members of the management board.

Since a shareholder representing a majority of the voting rights or the share capital of a corporation may de facto have a controlling influence on the stock corporation's management because of its ability to elect and dismiss the shareholder representatives on the corporation's supervisory board, a controlling shareholder must compensate any disadvantage suffered by the corporation as a result of any exercises by the controlling shareholder of its influence.

The controlling shareholder may 'legalise' its influence on the stock corporation by concluding a domination agreement with the stock corporation. Once a domination agreement has been concluded, the Stock Corporation Act recognises the shareholder's right to give instructions to the management board. In order to become effective, the domination agreement must be approved by the corporation's general meeting with a supermajority of at least 75 per cent of the share capital represented at the meeting. The controlling shareholder is obligated to compensate any loss incurred by the controlled company during the term of the domination agreement and to acquire, at a minority shareholder's request, that shareholder's shares against adequate compensation.

Certain decisions are reserved for the shareholders' meeting by statutory law: this includes the appointment of members of the supervisory board, the appropriation of distributable profits, the appointment of the auditor, the amendment of the articles of association, measures to increase or reduce the share capital or obligations to transfer significant assets of the company.

In addition, the shareholders' meeting must approve management decisions that could fundamentally affect the shareholders' rights and economic position, such as the sale or the hive-down of a business division into a subsidiary if the division contributes a significant portion of the corporation's revenue. Apart from these exceptional cases, the management board can make business decisions autonomously without the shareholders' consent. For example, the management board can decide to delist the company from the stock exchange without the consent of the general meeting (see Section II.v. for general meeting's votes on board compensation).

**ii Shareholders' duties and responsibilities**

All shareholders are subject to the duty of loyalty in relation to the company and other shareholders. In particular, shareholders are prohibited from causing harm to the company.

In principle, the duty of loyalty is defined by the articles of association and the company's purpose. However, in exceptional circumstances, a shareholder may even be obligated to exercise his or her voting rights in favour of a specific measure that is deemed to be necessary for the avoidance of the collapse of the company.
iii Shareholder activism

Germany has experienced several waves of shareholder activism. Owing to changes of the law and restrictive court decisions, the practice of ‘greenmailing’ companies through lawsuits by individual minority shareholders seeking to set aside shareholder resolutions or to delay corporate transactions is largely a thing of the past. Nowadays, activist shareholders are often hedge funds that seek to influence the strategy and the share price of a company even though they only hold a minority stake in the company. This is typically done through the exercise of minority rights. Often, these attempts are accompanied by aggressive publicity and media campaigns designed to pressure the company’s management into adopting the measures proposed by the activist shareholder. Another means for activist minority shareholders to exercise a disproportionate influence on a company is through proxy fights. Foreign and institutional investors especially increasingly follow the voting recommendations of proxy advisers. If an activist shareholder succeeds in persuading a proxy adviser to favour the measures proposed by the activist shareholder, this will result in a significant increase in the activist shareholder’s factual voting power.

iv Takeover defences

Once the bidder has published its decision to make a takeover offer, the management board may no longer take any actions that could prevent the success of the offer. There are, however, some statutory exceptions to this ‘prohibition of frustrating action’. The management board remains entitled to solicit competing offers from third parties (white knights) and to take actions approved by the supervisory board. Moreover, the management board continues to be entitled to take all measures that are in the ordinary course of the company’s business and not subject of the takeover offer or that are intended to implement a business strategy that the company has embarked on before the publication of the takeover offer.

The management board may also take defensive measures that are authorised by the general meeting before the takeover offer was announced and approved by the supervisory board. These include: (1) repurchasing shares equalling up to 10 per cent of the registered share capital; (2) establishing increased majority requirements for shareholder votes; (3) electing shareholder representatives in the supervisory board at different points in time to create a ‘staggered board’ and at the same time increasing the majority requirements for their dismissal; (4) selling important assets of the corporation; or (5) acquiring a direct competitor of the bidder.

v Contact with shareholders

Each shareholder may request the management board to provide information regarding the affairs of the company. The shareholders’ information right may, however, only be exercised during a shareholders’ meeting and is limited to information that is reasonably required by the shareholders to appropriately assess the topics on the agenda of the shareholders’ meeting. The management board may refuse to provide the requested information only for a limited number of reasons enumerated in the Stock Corporation Act, in particular if providing the information would, in the assessment of a reasonable businessman, be harmful to the company. To the extent the management board proactively communicates with shareholders, it must observe the principle of equal treatment of shareholders as well as the rules regarding disclosure of inside information.
Corporations must identify their shareholders (know your shareholder). In particular, financial intermediaries must provide, at the request of the company, the information that is necessary to identify the shareholders, including names and contact details.

While fostering investor relations and communication with (potential) investors and other stakeholders of the company generally falls within the remit of the management board, the supervisory board and, particularly, its chairman may, within certain boundaries, also communicate with the company’s stakeholders. The Corporate Governance Code suggests that the chair of the supervisory board should be available – within reasonable limits – to discuss supervisory board-related issues with investors. Especially the chair of the supervisory board may also exchange views with representatives of politics and the press.

However, investor communication by the (chair of the) supervisory board is limited to issues that fall within the remit of the supervisory board. These do, in particular, not include issues of corporate strategy and the management of the company, which are the sole responsibility of the management board.

VI OUTLOOK

i The EU Company law package

The two European Directives amending Directive (EU) 2017/1132 must be transposed into national law within the next years. The Company law package includes the following two sets of rules:

a The first directive concerns the use of digital tools and processes in company law. It aims to digitise the entire communication between the commercial register, the company and all its legal business partners. This should, for example, allow for the establishment of a company via online communication. The directive was adopted on 20 June 2019 and must be implemented into national law within two years.

b The second directive aims to improve the transnational mobility of companies and provides rules for cross-border conversions, mergers and divisions. The Directive also contains substantive rules aimed at protecting minority shareholders, creditors and employees. This directive was adopted on 18 November 2019 and must be implemented into national law within three years.

ii EU Whistle-blower protection

The Directive of the European Parliament and of the Council on the protection of persons reporting on breaches of Union law (2018/0160) became effective on 16 December 2019 and has to be implemented by the EU member states within the next two years. The directive aims to better protect whistle-blowers as well as to improve law enforcement and the protection of the freedom of speech and freedom of information.

The directive has a wide scope as it protects Union citizens and third country nationals as well as company’s employees and other persons related to the company, such as suppliers, interns and job applicants. The directive provides for rules that deal with whistle-blower reports of serious concerns regarding unlawful actions or abuses of law. Since the implementation period will end in December 2021, it is expected that the discussion on the German implementation of the EU Whistle-blower protection regime will gain momentum in 2020.
iii  German Corporate Sanctions Act

On 22 August 2019, the German Federal Ministry of Justice introduced a first draft of a Corporate Sanctions Act allowing for the prosecution of corporate crimes.

The draft aims at enhancing enforcement against corporations for business-related crimes and higher penalties for companies as well as facilitating the conduct of internal investigations and setting incentives for establishing internal compliance programmes. Since this quite far-reaching legislative draft is controversially discussed in the German public press and between legal scholars, it can be assumed that the legislative process is likely to take some time. However, in light of the global political trend of enhancing enforcement powers, the draft Corporate Sanctions Act is a piece of legislation that will have to be considered by listed and unlisted companies.
Chapter 8

GHANA

NanaAma Botchway and Emmanueler Ewurabena Quaye

I OVERVIEW OF GOVERNANCE REGIME

The principal legislation affecting the governance of listed companies is the Companies Act, 2019 (Act 992). The Companies Act includes general provisions relating to the organisational framework of all companies, both public and private, as well as special provisions for public companies only, relating to invitations to the public for the acquisition or disposal of listed securities, standards for financial reporting, procedures for appointing directors, etcetera. Apart from the Companies Act, other relevant legislation that affects the governance of listed companies includes the Securities Industry Act, 2016 (Act 929) and the Securities and Exchange Commission Regulations, 2003 (LI 1728), which regulate public invitations for and trading in listed securities, as well as disclosure obligations and financial reporting standards for listed companies.

The Listing Rules of the Ghana Stock Exchange (Listing Rules), the Code on Takeovers and Mergers (Takeover Code) issued by the Securities and Exchange Commission (SEC), the SEC’s Code of Best Practices on Corporate Governance (Corporate Governance Code) and the SEC’s Guidelines on the Registration of Auditors and Accountants Reporting for Public Companies and SEC Licensees (SEC Guidelines) are also key to the governance regime of listed companies. The Listing Rules is a comprehensive rulebook that sets out various rules and guidelines on the governance of companies listed on the Ghana Stock Exchange (GSE). It prescribes mandatory disclosure obligations for issuers of listed securities, rules on board governance, and practices and protections in respect of shareholders’ rights. The Takeover Code regulates takeovers and mergers by, between or affecting public companies. The Corporate Governance Code contains principles, guidelines and recommendations for ensuring the effective governance of listed companies. The SEC Guidelines sets out registration requirements applicable to auditors and accountants reporting for public companies Sector-specific legislation, such as the Banks and Specialised Deposit Taking Institutions Act, 2016 (Act 930), the Insurance Act, 2006 (Act 724) and their respective regulations, also contain important provisions that affect listed companies operating within the relevant sectors, particularly in relation to board composition and governance.

The SEC, together with the GSE and the Registrar of Companies, bear the primary responsibility for overseeing the listed company regime in Ghana. However, there are other supervisory bodies (such as the Bank of Ghana for the banking sector and the National Insurance Commission for the insurance industry) that regulate listed companies operating

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in specific sectors of the economy. The SEC is empowered under its enabling law to impose administrative penalties for non-compliance with its codes, directives, guidelines and circulars. With respect to instances of non-compliance that also constitute criminal offences, prosecutorial powers are administered by the Attorney General, who may authorise the SEC to prosecute such offences on his or her behalf.

The GSE enforces compliance with its rules through sanctions such as the suspension or delisting of listed companies. A listed company may be suspended from the exchange or its securities delisted for non-compliance with the GSE’s rules on disclosure and its policy on quality management of listed companies. Where a listed company has disposed of its principal assets or discontinued a significant portion of its operations without shareholder approval, or persistently failed to comply with GSE and SEC rules and directives, it could also be suspended or delisted. The Registrar of Companies is also authorised, under the Companies Act, to impose penalties on companies in respect of breaches of the mandatory provisions of the Companies Act, and by so doing ensure compliance with the Companies Act. The Registrar of Companies may also go to court to compel compliance with the requirements of the Companies Act.

The corporate governance regime for listed companies in Ghana is essentially a combination of statutory law, subsidiary legislation and regulatory guidelines and directives. The Corporate Governance Code does not have the force of law, and is merely used as a benchmark for assessing the governance practices of listed companies and companies that operate within the securities industry. However, some regulators in the financial services sector have developed detailed mandatory guidelines on governance structures and control systems for regulated companies, non-compliance with which could have adverse implications on their licences. For instance, the National Insurance Commission has developed governance and risk management guidelines for both life and non-life insurers. The detailed framework provides the minimum standards for the corporate governance structures and internal control systems that insurers must comply with. This includes board composition, mandatory board committees and their composition, their mandate and responsibilities, and audit and risk control functions. Another sector that has seen steady development in corporate governance practices is the banking sector. The Bank of Ghana (BoG) issues notices and directives on governance structures and control systems for banks and specialised deposit-taking institutions in line with the corporate governance principles of the Basel Committee on Banking Supervision. Following the collapse of a number of banks, in December 2018 the BoG released a comprehensive corporate governance code (BoG Directive) for the banking industry, specifically banks, savings and loans companies, finance houses and financial holding companies licensed or registered under the Banks and Specialised Deposit Taking Institutions Act, 2016 (regulated financial institutions). In July 2019, the BoG – as part of its efforts in supporting sound corporate governance practices and preventing ineligible persons from engaging in any licensed activities – rereleased the Fit and Proper Persons Directive (the BoG Fitness Directive). This directive provides the criteria to be used by regulated financial institutions in adjudging the suitability of significant shareholders, directors and key management personnel within the institution. Unlike the Corporate Governance Code, compliance with the BoG Directives (the BoG Directive and BoG Fitness Directive) is mandatory, and in some cases it provides deadlines for its implementation.

In addition to the BoG Directives, compliance with the various laws and constitution relevant to listed companies is strictly compulsory, subject to certain special circumstances when waivers in respect of some specific provisions or requirements may be granted by the
appropriate supervisory body under conditions imposed by the supervisory body. Compliance with the Corporate Governance Code is entirely voluntary, and listed companies are not obliged to explain their reasons for not complying with the best practices identified therein.

Increasing multinational interests in Ghanaian companies have led to a growing advocacy for the adoption of international standards and best practices in the governance of Ghanaian companies. Companies with foreign shareholders, particularly institutional investors with significant or controlling shareholding, are greatly influenced by the corporate governance practices of these investors. Government-led efforts aimed at developing mandatory corporate governance rules for Ghanaian companies are largely sector or industry-driven, and this has resulted in regulators developing sector-specific corporate governance guidelines or manuals. A national corporate social responsibility (CSR) policy, which seeks to change the traditional focus of CSR activities on charity, was also launched in 2016.

II CORPORATE LEADERSHIP

i Board structure and practices

Ghanaian boards do not have a two-tier structure. The normal practice is for a single-tier board, made up of executive and non-executive directors, to collectively manage the business of the company.

The company’s constitution may prescribe a minimum or maximum number of directors, subject to the requirement under the Companies Act for every company to have at least two directors and for at least one director to be ordinarily resident in Ghana. Public companies, whose constitution authorises cumulative voting in the appointment of directors, are required to have a minimum of three directors on their board. In addition to any other disqualifications specified under the constitution of a company, infants, body corporates, persons of unsound mind, fraudulent persons and undischarged bankrupts are disqualified from being appointed to the board. The BoG Fitness Directive requires persons nominated for directorship and key management positions in regulated financial institutions to comply with the fit and proper assessment criteria in order to be appointed to act. Non-executive directors must make up at least 50 per cent of the board of a listed company; in addition, there shall be at least two independent directors, or independent directors shall constitute approximately 25 per cent of the board. Sector-specific legislation and constitution may also specify additional requirements relating to the competencies and qualifications of members of the board, as well as representation of non-executive or independent directors on the board. The Corporate Governance Code recommends a board of between eight to 16 members that has a balanced representation of executive and non-executive directors, and that at least one-third be independent. The BoG Directive requires that the board of regulated financial institutions have a minimum of five and a maximum of 13 members, with the majority being non-executive directors who are ordinarily resident in Ghana. In addition, regulated financial institutions boards must be composed of 30 per cent Ghanaian nationals who are ordinarily resident in Ghana, and independent directors must also make up at least 30 per cent of these boards.

An act of the board of directors or the managing director of the company while carrying on the usual business of the company is regarded as an act of the company itself, and the company shall bear civil and criminal liability for that act unless it can be shown that the person with whom the board or managing director was dealing with had actual or
constructive knowledge at the time of the transaction that the managing director or the board did not have the power to act in the transaction. A single director, other than the managing director, can only represent the company with the board’s express or implicit approval.

The board is responsible for directing and administering the business of the company. In managing the business of the company, the board may not exceed the powers granted to it under the Companies Act or the company’s constitution, or exercise those powers for a purpose different from that for which they were granted, whether or not it may be in the best interests of the company to do so. The board has a legal duty to not act on the directions or instructions of any other person, and to ensure that the affairs of the company are being managed in accordance with law and the company’s constitution. In filling a casual vacancy on the board, the directors have a duty to satisfy themselves that any person they intend appointing to the vacant office is suitable and has the requisite integrity to be a director of the company.

Unless otherwise specified by the company’s constitution, the board may elect one of their number to act as chair at their meetings for a specified period. The BoG Directive, however, makes specific requirements for the board chair: that is, the position must be occupied by an independent director who is also ordinarily resident in Ghana, and the term of office is restricted to three years renewable for only one additional term. Subject to a contrary provision in the constitution of the company, the chair has a casting vote in the event of an equality of votes during the decision-making process of the board, and also presides at meetings of shareholders. The chair is required to sign minutes of board and shareholders’ meetings at the end of the meeting or on the next adjourned date, and if duly signed, such minutes are prima facie deemed to be a true record of the proceedings at the meeting. Audited accounts and balance sheets of companies may be signed by any two directors with the approval of the board. Regulatory filings may also be signed by the company secretary and any director of the company.

The board of directors may delegate any of their powers to a committee consisting of one or more of their number. The board may also appoint one or more directors to the office of managing director and entrust any of the powers exercisable by the board to the managing director or managing directors, subject to any restrictions or conditions that they deem fit. The delegation of its responsibilities to a committee or managing director does not absolve the remaining directors of any liability that may arise in the performance of the delegated duties by the committee or managing director. Directors must, therefore, ensure that they have proper oversight over their delegated responsibilities.

The Companies Act provides for the executive office of managing director of the company. The managing director is appointed from among the board, and may exercise all or any of the powers of the board that the board may confer. There is no requirement under the Companies Act that the role of board chair and managing director be separately performed by two different directors. However, the Corporate Governance Code recommends a separation of the two roles, and it is standard practice for the two positions to be occupied by different people. For regulated financial institutions, and per the BoG Directive, the separation of these roles is a requirement and not a recommendation. Further, the position of managing director can only be held for a maximum of 12 years, split into three terms with each term not exceeding four years. The chair’s traditional role is to act as leader of the board and to chair board and shareholder meetings. Outside general meetings of the company, direct communications by directors (the chair included) with shareholders are not common, although not prohibited under the Companies Act.
Fees and other remuneration payable to directors in their capacity as directors may only be determined by the ordinary resolution of members. The remuneration of executive directors in respect of the executive positions that they hold at the company may be fixed by the board as part of the board’s terms of employment; however, these terms must be approved by ordinary resolution of the members of the company prior to any payments being made. Unless the company’s constitution provides otherwise, the board has the power to determine the remuneration of senior management. Directors’ remuneration may not be paid free of income tax; nor can it be calculated by reference to or varying with the amount of income tax payable by directors.

The board may exercise any of its powers through committees consisting of one or more of its number. The Corporate Governance Code recommends the constitution of at least an audit committee and a remuneration committee composed of a majority of non-executive directors. It also advocates the inclusion of executives who are not directors of the company on whatever committees that the board considers appropriate to effectively discharge their functions so long as the responsibility for decision making remains with the directors on the committees. The BoG Directive on the other hand makes it a requirement for regulated financial institutions to have at least two board committees, an audit committee and a risk committee, which must be chaired by independent directors.

Directors of a listed company are guided by the tenets of the SEC’s Takeover Code. The board of a target company is required to make a recommendation to shareholders on the acceptance or rejection of any takeover offers made by third parties. The board must appoint an independent adviser upon receipt of a takeover offer, who shall advise the board and the company on all relevant issues and information relating to the takeover for the purpose of enabling shareholders to make an informed assessment of the takeover offer.

ii Directors

Under the Companies Act, no distinction is made between executive or non-executive directors of the company with respect to their duties and liabilities. Directors’ duties and liabilities are the same irrespective of whether they are non-executive directors or otherwise. In addition, directors may exercise any power that has not been reserved for the members under the Companies Act or the company’s constitution. Further, to the extent that a person is described as a director, with or without a qualifying title, that person is deemed to be a director, whose role and involvement is expected to be the same as all other directors of the company.

Companies are required to circulate information to all directors, including non-executive directors, at the same time. Non-executive directors are not prohibited from conducting on-site visits of subsidiaries of the company. They are also at liberty to freely interact with lower management. In practice, it is usual, especially at the board committee level, for directors to work directly with the relevant management team to achieve their mandate. For example, directors on a risk subcommittee of the board may freely interact with the head of finance or another relevant department of the company, and may make enquiries with respect to reports or other information submitted to the board or board committee.

The generally applicable legal duties and best practice for directors in Ghana are summed up in Sections 190 to 198 of the Companies Act. Essentially, a director of a company is deemed to stand in a fiduciary relationship towards the company, and must at all times observe the utmost good faith towards the company whether in a transaction on behalf of the company or with it. Further, the actions of a director must at all times be what he or she
believes is in the best interests of the company in order to preserve its assets and further its business, and the purpose for which it was formed. Directors must act in the faithful, diligent and careful manner in which an ordinarily skilful director would be expected to act. They may not place themselves in any position in which their duty to the company conflicts with their personal interests.

A director is liable to compensate the company for any loss that it suffers as a result of a breach of the director’s duties to the company. Directors must also account to the company for any profits they make from transactions involving a breach of their duties to the company. Contracts entered into between the company and a director who acts in breach of his or her duty to the company are subject to rescission.

Directors are appointed by ordinary resolution of members. The constitution of a company may validly provide for the appointment of one or more directors by a class of shareholders, debenture holders, creditors, employees or any other person. The board may also appoint a director to fill a casual vacancy on the board. A director of a private company shall continue in office until he or she vacates the office or is removed in accordance with the law and the company's constitution. For regulated financial institutions however, the BoG has the power to remove a director where it considers that such an appointee is not fit and proper after hearing a representation made by the Bank. Directors of public companies, except the managing director, are subject to retirement by rotation – usually one-third of the board must retire every year. There are formal processes and default rules regulating the appointment and removal of directors of both private and public companies. With respect to public companies limited by shares, a resolution for the appointment of two or more directors shall not be moved as a single resolution except with unanimous approval of the shareholders. Nonetheless, the company's constitution may authorise cumulative voting for appointing directors.

Directors are prohibited from putting themselves in situations where a conflict arises between their duty to the company and their own personal interests or the interests of other persons. In very limited circumstances, the company may consent to a conflict situation following full disclosure of all relevant information to the board or members in general meeting. These include instances where a director is directly or indirectly personally interested in a transaction entered into by the company or in a competing business with that of the company, or intends to use for personal advantage money or property belonging to the company or confidential information obtained in his or her capacity as a director of the company. Sector-specific laws may also require directors to disclose conflict situations to the company. For instance, directors of banks, specialised deposit-taking institutions or financial holding companies must declare on an annual basis any personal interests and business or investment interests that they may have in the company, and notify their board in the event of any changes to that declaration.

There are no provisions regulating the manner of interaction between executive and non-executive directors. In practice, directors cooperate fully with each other for the purpose of ensuring the effective management of the company.
III DISCLOSURE

Comprehensive disclosure obligations, both periodic and event-driven, are imposed on listed companies especially under the Companies Act, the GSE Listing Rules and the SEC Act and Regulations, and the BoG Directives in the case of regulated financial institutions. Shareholders and directors of listed companies also have significant disclosure obligations.

i Disclosure by the company

Generally, companies are required to file, with the Registrar of Companies, annual and other periodic returns of particulars of the company, including when there is a change in the board of directors, of the company secretary or of the auditors. Annual returns must state the current position of the company with regard to such information as its name, address, authorised business, directors and secretary, subsidiaries, shareholding and beneficial ownership structure, and are required to be filed within 36 days of the day on which the company’s financial statements, accounts and reports are circulated to members and debenture holders.

Under the GSE’s rules, the disclosure obligations require that a listed company makes full and timely disclosure to the public of all information necessary to enable an investor make informed investment decisions, and information that is likely to have a material effect on the market activity and price of its listed securities. Disclosure of significant corporate events and price-sensitive information cannot be made on a selective basis. Corporate disclosure covers:

a periodic financial reporting and prompt announcements of changes in management;
b control or capital investment plans of the company;
c labour or contractor disputes;
d insolvency events;
e issuance of additional securities;
f restructuring of the company;
g default on loans;
h imposition of fines or sanctions by regulators;
i profit or revenue-related matters; and
j acquisition of significant interests in another company.

If considered material by the board, a listed company shall also immediately disclose:

a the acquisition or loss of a contract;
b borrowing of funds by the company;
c the purchase or sale of an asset;
d changes in the corporate purpose;
e judicial and quasi-judicial actions initiated by or against the company; and
f other material events.

Disclosure of material information may be withheld by the company in very limited circumstances, such as where immediate disclosure would be prejudicial to the company’s ability to pursue its corporate objectives, where the facts requiring disclosure are in a state of flux and a more appropriate moment for disclosure is imminent, and where negotiations regarding the subject matter for disclosure are ongoing and an agreement in principle has not yet been reached. A listed company that withholds the disclosure of material information must ensure that strict confidentiality is maintained, and the company shall immediately disclose the relevant facts where rumours about the withheld information surface.
ii Disclosure by shareholders
Shareholders of listed companies are required to disclose to the public the acquisition or disposal of any interest in the company that causes the shareholder's stake in the company to attain, exceed or fall below each 5 per cent threshold starting from 10 per cent up to 50 per cent plus one share. This announcement must be made within 48 hours of the transaction, and shall indicate the number of shares sold or purchased and the percentage of the share capital and votes in the company held by the shareholder after the transaction.

iii Disclosure by directors
A director of a listed company has a duty to disclose to the members of the company the terms of any payment made or proposed to be made to that director in connection with a takeover bid by any person. The nature and extent of the holdings of a director in respect of the company’s securities or the securities of an associated company must also be disclosed to the company and recorded in a register to be produced at the company’s general meetings and made available for inspection by members. Under the Companies Act, directors who have an interest that is likely to create a conflict of interest situation are also required to enter the details of their interest in an interests register established by the company and disclose that to the board immediately after becoming aware.

iv Financial reporting and accountability
Listed companies must provide quarterly reports to the GSE at least 48 hours before they are published in the newspapers. Companies are required to also circulate annual reports to their members comprising financial statements, together with the reports of directors and auditors on the same, prepared in strict compliance with the requirements of the Companies Act and International Financial Reporting Standards adopted by the Institute of Chartered Accountants Ghana. A company’s annual report must be laid before the company at an annual general meeting held by the company within three months of the annual report being circulated, and must include or indicate:

- a statement of each director’s holdings in the issued shares of the company;
- a statement on the corporate social responsibility of the company and an associated company and the amounts spent during the financial year;
- a statement of the amount payable by way of audit fees;
- particulars of the steps taken to build the capacity of the directors to discharge their duties;
- particulars of material contracts in which directors are interested and entries in the interest register;
- the aggregate number of directors’ emoluments;
- the aggregate amount of directors’ or past directors’ pensions;
- the aggregate amount of compensation to directors or past directors in respect of loss of office; and
- the aggregate amount of monies due to the company or an associated company from its officers at the end of the financial year, as well as the maximum amount that was due it from officers at any time during the financial year.

Regulated financial institutions are, in addition, required to include a certification in their annual reports as to their compliance or otherwise with the contents of the BoG Directives.
v Auditors’ role, authority and independence

Auditors play a fundamental role in ensuring the accountability of listed companies. They are not regarded as officers or agents of the company, but stand in a fiduciary relationship to the members of the company. Hence, they are required to act with due care, skill and diligence, and may incur liability for a breach of their duties to the company. To safeguard the independence of auditors, a person does not qualify to be an auditor of a listed company if that person is an officer of the company or an associated company, or is a partner of or in the employment of an officer of the company or an associated company. Further, under the SEC Guidelines auditors are to comply with the code of ethics for professional accountants of International Federation of Accountants and be independent of the auditee firm. Auditors cannot simultaneously act as reporting accountants of the same public company, and accountants who have provided reporting services for a public company cannot act as auditors for the same company within a period of 12 months. The appointment of a person as an auditor of a listed company must also be approved in writing by the SEC. Duly appointed auditors may serve a maximum term of six years and shall only be re-eligible for appointment following a cooling-off period of at least six years. Auditors are entitled to attend general meetings of the company, receive notices and other communication relating to a general meeting, and be heard at a general meeting on any part of the business of that meeting that concerns them in their role as auditors of the company. Auditors of a company are guaranteed a right of access at all times to the accounting records and financial statements of the company and may require any information that they deem necessary from officers of the company in order to fully carry out their functions.

vi The comply or explain model and mandatory disclosure

In the area of corporate disclosure, Ghana operates a prescriptive regulatory model. Therefore, all disclosure obligations under the Listing Rules, the Takeover Code, the BoG Directives and the Companies Act are mandatory. Where, on very limited and specific grounds, a listed company wishes to be exempt from the application of a particular obligation, it must seek and be granted a waiver from the appropriate regulator before taking any action that would result in non-compliance with a specific obligation.

vii One-on-one meetings of directors with shareholders

One-on-one meetings between directors and shareholders are not common.

IV CORPORATE RESPONSIBILITY

It is normal practice in the financial services industry to have a risk subcommittee of the board of directors, as well as a risk department with a functional head. In other sectors, the appointment of a special risk officer or constitution of a risk committee may be necessary depending on the business of the company and its exposure to various risks in the sector. The risk management culture of the company is usually dictated by its risk policy and the general attitude and practices of top-level management.

Companies whose activities require anti-money laundering (AML) monitoring are required to formulate AML policies and train, and to monitor their employees for compliance with the internal AML policy and the applicable AML laws. Under the AML Act, 2008 (Act 749) as amended and AML Regulations, 2011 (L.I 1987) a designated AML compliance officer must be appointed to report suspicious transactions to regulatory authorities.
Companies also adopt appropriate policies on bribery and corruption, data protection and other areas of risk relevant to their operations. In addition, the Corporate Governance Code recommends the adoption of a code of ethics and statement of business practices.

Legally, the board’s overriding obligation to always act in the best interests of the company as a whole may impose an implicit obligation on directors to consider other factors beyond the maximisation of shareholder value. The Companies Act provides that in deciding whether a particular transaction or course of action is in the best interests of the company as a whole, the directors may consider the interests of not just shareholders, but also employees and creditors. Beyond employees and creditors, there is no legal obligation, express or implied, to consider the interests of any other stakeholders. A national CSR policy was launched in 2016. Compliance with the policy, which focuses on, inter alia, human rights, employee welfare, the environment, safety, accountability and transparency, and ethical practices, is entirely voluntary. In practice, however, CSR activities of Ghanaian companies and multinationals tend to focus on philanthropy and charity. In this regard, shareholder approval must be obtained by the directors of a company before any voluntary contributions to charitable or other funds in excess of 2 per cent of the retained earnings of the company can be made.

V SHAREHOLDERS

i Shareholder rights and powers

The constitution may also provide for different classes of shares by attaching special rights, including voting rights, to those shares. Each equity share in a company carries the right to one vote for each share, notwithstanding any contrary provision in the constitution of the company. Preference shares shall also carry the right to one vote per share, except that, in certain circumstances relating to a variation of the rights of their holders, winding up of the company or replacement of the auditors etcetera, preference shares may carry the right to more than one vote for each share. The constitution of a company may validly provide for the suspension of a shareholder’s voting rights in respect of shares on which there are unpaid calls.

Directors, collectively and individually, have a duty to act in accordance with what they believe to be in the best interests of the company and are not bound to follow the directions or recommendations of shareholders. This restricts the power of shareholders to influence the board, other than in respect of the holding of extraordinary general meetings – directors must proceed to hold a meeting upon the requisition by shareholders holding at least 5 per cent of the total voting rights in a public company or 10 per cent of the total voting rights in a private company.

The constitution of a company may reserve certain decisions for shareholders’ action only. Under the Companies Act, only shareholders have the power to:

a appoint and remove auditors;
b appoint directors (other than in respect of a casual vacancy) and remove them;
c determine the remuneration of directors;
d declare dividends; and
e decide to wind up the company.

Shareholders may also act in matters that fall within the powers of the board, such as where there is a deadlock, and as such the directors cannot act; commencing legal action in the name of the company where the directors have failed to do so; and acting for the purpose of ratification of acts of the directors.
Shareholders take decisions by voting in general meeting and then passing resolutions to give effect to their decisions. In spite of this, a dissenting shareholder has the right to pursue an action in court if he or she is of the opinion that any decision, action or transaction of the company is illegal, irregular, ultra vires or contravenes the provisions of the constitution of the company. Additionally, a dissenting shareholder on special resolutions seeking to vary or dispense with the business of the company or approve a major transaction, arrangement, merger or division of the company or variation of class rights may require the company to purchase his or her shares and that of other members.

There is no legal mechanism that expressly permits the implementation of loyalty programmes for long-term shareholders. Given the underlying principle of one share, one vote in Ghanaian company law, equity shareholders cannot be granted additional votes for their existing equity shares without a corresponding and proportionate increase in the number of equity shares that they hold in the company. However, it would be possible to issue preference shares and attach additional voting rights to those shares.

Directors have very broad powers with respect to the management of the company’s business. However, these powers are limited when shareholder approval is required before any action can be taken in the following instances:

- the acquisition or disposition of the company’s assets the value of which is more than 75 per cent of the assets of the company before the disposition or acquisition;
- the entering into of any transaction that has or is likely to have the effect of the company acquiring rights or interests, obligations or liabilities, the value of which is seventy five percent of the value of the assets of the company before the transaction;
- issuance of new or unissued shares other than treasury shares, unless these have been offered on the same terms to all existing shareholders or class of shareholders;
- making voluntary contributions to charity of an amount exceeding 2 per cent of the retained earnings of the company recorded for the immediately preceding financial year;
- borrowing money or charging the company’s assets as security for any loan, where the amount to be borrowed together with the outstanding balance of any existing loans will exceed the stated capital of the company; and
- allotment of shares to executive directors as part of an employee share scheme.

### Shareholders’ duties and responsibilities

Controlling shareholders do not have any special responsibilities to the company, other than the duty shared by all shareholders to pay any outstanding liability on shares in the event of a call being made and on the winding-up of the company. All shareholders are mandated to disclose the particulars of the beneficial owners of their shares, details of the arrangement giving rise to the beneficial ownership and a confirmation as to whether they are politically exposed persons.

Institutional investors also do not owe any obligations to the company, although owing to recent advocacy for improved corporate governance methods, institutional investors are encouraged to increase their level of engagement with, and monitoring of, the board and management.

There is no code of best practice for shareholders.
Shareholder activism

Shareholders must approve the amount of remuneration payable to directors in their capacities as directors or as executive officers of the company.

Shareholders are mandated to commence legal action in the name of the company if the directors refuse or neglect to do so. A shareholder may bring an action against a third party or against a director who acts in breach of his or her duty to the company. Actions brought by a shareholder to enforce an obligation owed under the constitution of the company to that shareholder and any other shareholders, that shareholder shall sue in a representative capacity for himself or herself and on behalf of any others affected by the act complained about, and the shareholder is not required to seek the consent and approval of any other affected shareholder before doing so.

Shareholders are not prohibited from soliciting proxy votes prior to a general meeting of the company. Proxy battles are, however, not very common in Ghana.

The Companies Act allows a shareholder to propose a resolution on any matter and to provide to the company a statement on the proposed resolution for circulation to persons entitled to attend and vote at meetings. Shareholders are also permitted to provide statements on any issue already on the agenda of a proposed meeting for circulation to all shareholders prior to the holding of the meeting. These provisions allow shareholders to engage the board on issues that directors may for various reasons want to avoid discussing. They encourage shareholders to be proactive, and to monitor and hold management accountable.

Takeover defences

The provisions of the Companies Act, the Listing Rules and the Takeover Code are generally non-facilitative of the use of most defensive mechanisms that a company may use to protect itself from a hostile takeover. Under the Takeover Code, the target company in a takeover is precluded from issuing new shares or granting options over unissued shares upon receipt of a takeover offer or if the board has reason to believe that a takeover of the company is imminent. This prevents a target company from embarking on a shareholder rights plan as a means of thwarting a hostile takeover. The use of voting rights plans are also precluded because although preferential shareholders may be issued with special voting rights that entitle them to more than one vote per share, these rights are exercisable in very limited circumstances prescribed under the Companies Act, and voting against a hostile takeover is not one of those circumstances. The use of staggered boards as a takeover defence is also not effective as under the Companies Act, the shareholders of a company may remove directors from the board at any time, and hence a person that gains control of a company through a hostile takeover is at liberty to change the entire board upon completion of the takeover. On the other hand, the Takeover Code permits a competing offer to be made during the pendency of a takeover offer by another person, thus permitting the use of the white-knight defence by a board in the event of a hostile takeover.

Contact with shareholders

The reporting obligations of the company relate mainly to periodic financial reporting and event-driven announcements, which must be made to all shareholders within certain timelines or on the occurrence of certain events discussed above.

Selective disclosure of price-sensitive information to shareholders, individually or collectively, is not permitted under the Listing Rules. Listed companies must ensure that shareholders and the general investing public have simultaneous and equal access to the
same information. Meetings and communications with individual shareholders following the public disclosure of price-sensitive information is not prohibited. Thus, it is possible for the board to approach and engage particularly influential shareholders to obtain their views and court their approval on certain key issues that are in the public domain before proposing resolutions on them at shareholders’ meetings.

All shareholders are entitled to receive the same information at the same time. The disclosure of price-sensitive information to any person prior to its release to the public automatically precludes that person from dealing in any securities of a listed company.

Standstill agreements are purely contractual and may be made between the company and its controlling shareholders, particularly in respect of the disposal of large blocks of control shares to outsiders. As long as they do not contain any unlawful provisions, they are enforceable.

Shareholders are entitled to receive information at least 21 days before shareholders’ meetings. The constitution of the company may provide for longer notice periods.

Proxy solicitation is permitted, although it is not widely used in practice.

To some extent, shareholders are able to give their views in advance of meetings. The Companies Act permits shareholders to send statements to the company for circulation to shareholders on any business to be dealt with at a proposed meeting. This is usually circulated with the notice of the meeting, or soon thereafter, at the shareholder’s cost.

There are no relevant issues regarding large blocks of shareholders.

VI OUTLOOK

The Ghanaian corporate governance space is in a burgeoning state. The existence of mandatory rules on certain corporate governance issues ensures that minimum standards are met by companies. However, owing to the voluntary nature of the Corporate Governance Code, compliance with other important governance practices in accordance with widely recognised international standards has been slow. With the failure of a number of Ghanaian indigenous banks, the shutdown and revocation of licenses by regulators of some microfinance institutions and the hostile takeover of the country’s premier mortgage finance institution by a Caribbean banking conglomerate, interest in the adoption of policies that protect wider stakeholder interests in Ghanaian companies has been generated. The banking sector has been, understandably, particularly responsive on the subject. With the laissez-faire attitudes of most individual shareholders, the active engagement and involvement of institutional investors is critical in shaping the governance culture of local companies. The current BoG Directives reflect the changing attitude towards the importance of corporate governance in sustaining various sectors of the Ghanaian economy.
Chapter 9

HONG KONG

Robert Ashworth and Chris Mo

I  OVERVIEW OF CORPORATE GOVERNANCE REGIME

Over the years, with the growing pre-eminence of its stock exchange and the enhancement of its supporting market infrastructure and regulation, Hong Kong has moved on from being a regional market dominated by local tycoons and their traditional (often real-estate focused) businesses to become a truly international, and thoroughly modern, financial centre that facilitates efficient and friction-less access to international capital for all participants. The turning point arguably came in 1992, when the former Chinese Premier, Zhu Rongji, looked south for further impetus to his state-owned enterprise reform agenda. He believed that the listing of Chinese companies in Hong Kong would, over time, bring them (and therefore China more broadly) up to speed with international best practice and corporate governance standards. Since then, Chinese companies have flocked to the Hong Kong securities market, propelling Hong Kong to become one of the pre-eminent financial centres in the world.

The governance regime for Hong Kong listed companies derives from the common law, certain key statutes, and from a strong reliance on non-statutory rules, codes and best practices. In broad terms, laws and regulations operate to penalise companies and their directors for non-compliance and provide remedies for the aggrieved, while non-statutory rules and best practices serve to guide corporate behaviours.

i  Securities and Futures Ordinance

The Securities and Futures Commission (SFC) is the principal regulator of the Hong Kong securities and futures markets. It derives its powers from the Securities and Futures Ordinance (SFO) – the key piece of legislation that in 2003 consolidated and modernised Hong Kong’s diversified securities laws. All Hong Kong listed companies are subject to the SFO, regardless of their place of incorporation. This extra-territorial application is a particularly crucial feature of the SFO, as almost 90 per cent of Hong Kong listed companies are incorporated abroad.2

In the area of corporate governance, key functions of the SFO include:

a  requiring directors to disclose their personal interests in the listed company and its affiliates;

b  requiring timely disclosure of price sensitive information; and

c  prohibiting insider dealing.

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2 HKEx. HKEx Factbook 2018, p. 32.
A breach of the SFO can lead to disciplinary proceedings, and at times, criminal sanctions. With the leave of the court, the SFC can also unwind transactions to remedy a breach. This is a power that the SFC has readily exercised in recent years, providing redress to victims of false corporate disclosures and insider dealing.

ii Listing rules
The Stock Exchange of Hong Kong Limited (SEHK) is the only entity approved by the SFC as a 'recognised exchange company' under the SFO. This arrangement grants the SEHK a statutory monopoly to operate the securities market in Hong Kong, and in turn, to act as frontline regulator for the companies listed on its stock exchange. Under the SFO, ultimate powers of oversight are, however, reserved to the SFC.

The SEHK promulgates and administers the listing rules, which set out the principal regulatory mechanisms for companies listed or who wish to seek a listing in Hong Kong. As most Hong Kong listed companies are incorporated outside Hong Kong, the company law in Hong Kong has no direct application, save for a few exceptions. Against this background, a key function of the listing rules is to align the governance standards of PRC and overseas companies with what is expected under Hong Kong law. As a general requirement, PRC and other overseas incorporated listing applicants must demonstrate a level of shareholder protection that is at least on a par with standards in Hong Kong. Failing that, the applicant will not be granted approval to list on the SEHK.

On top of these gateway requirements, the listing rules also contain ongoing compliance and corporate governance obligations for listed companies. These include rules on regular financial reporting, appointment and retirement of directors (including independent directors), and shareholders’ approval for certain important transactions. Although the listing rules do not carry the force of law, compliance is, in practice, mandatory as the SEHK ultimately has the power to cancel the listing of a non-compliant issuer. This power is exercised cautiously, as it can harm the shareholders and other stakeholders that the listing rules seek to protect. More often, the SEHK will rely on other options, including:

a public censure of delinquent issuers and the responsible directors;
b ‘cold shoulder orders’ that prohibit dealers and financial advisers from acting for the issuers; or
c referral of the matter to the SFC for further investigation and possible sanction.

iii Corporate governance code
A key underpinning of the corporate governance regime in Hong Kong is the Corporate Governance Code (CG Code), which is appended to the listing rules. The CG Code has a three-tier structure. It sets out at a high-level the ‘principles’ of good corporate governance, followed by ‘code provisions’ and ‘recommended best practices’. Recognising that there is no such thing as ‘one size fits all’ when it comes to corporate governance, compliance with the code provisions and recommended best practices is not mandatory. The code provisions operate on a ‘comply or explain’ basis. A listed company may deviate from a code provision, provided it can find alternative ways to achieve the principles. The issuer must, however, explain in its annual report why good corporate governance is achieved by means other than strict compliance with the code provisions. For recommended best practices, these are for guidance only, and there is no reporting requirement for deviation.
iv SEHK – dual role as regulator and commercial company

One peculiar feature of the Hong Kong market is the SEHK’s dual role of regulator and profit-making company. On the one hand, the SEHK is the frontline regulator of companies listed on its stock exchange. On the other, SEHK listing fees are a significant stream of revenue for its parent company, Hong Kong Exchanges and Clearing Limited (HKEx), which is itself listed on the Main Board of the SEHK. This gives rise to a real and perceived tension between the SEHK’s regulatory functions and the commercial interests of HKEx as a listed company. The tension is ameliorated through various measures, including:

a delegation of HKEx’s listing approval functions to an independent Listing Committee constituted by experienced market practitioners;

b a statutory requirement that all listing rules amendments have to be approved by the SFC; and

c HKEx being directly regulated by the SFC.

The debate as to the effectiveness of these arrangements will likely continue, although in this regard it is worth noting HKEx’s own consistently high standards of transparency and disclosure. Through the years, HKEx has complied with virtually all code provisions and recommended best practices, setting itself up as a model of good corporate governance that other market participants can look up to.

II CORPORATE LEADERSHIP

i Board structure and practices

Hong Kong adopts a unitary board structure. Executive directors, non-executive directors and independent non-executive directors (INEDs) act collectively as one board. It is a mandatory requirement that issuers must have a minimum of three INEDs on its board, representing at least one-third of the entire board. In addition, at least one of the INEDs must have appropriate professional qualifications, or expertise in accounting or financial management.

The same board composition requirement applies to People’s Republic of China (PRC) issuers with a dual board structure. Minor adjustments are made so that most requirements that are applicable to directors are extended to cover supervisors of a PRC company.

The CG Code requires the board to meet at least four times a year, at approximately quarterly intervals, with a majority of eligible directors attending. Directors can meet in person or through electronic means of communication. However, the passing of written resolutions does not count as a meeting, as directors are expected to actively participate in the decision making process.

To promote checks and balances on the executives, the CG Code further requires the chairman to hold meetings solely with INEDs at least once a year and with the exclusion of any other directors. The purpose is to create a forum for open discussion without the presence of the company’s management. This is a relatively new requirement that came into effect in 2019. Previously, the CG Code simply required the chairman and non-executive directors (including INEDs) to meet annually. The SEHK later surmises that the involvement of all non-executive directors may defeat the purpose of meeting without management, because in family-controlled companies, non-executive directors (who are not INEDs) are often
family members appointed by the controlling shareholder. It should be noted that the code provision, in its current form, may not fully accomplish what it set out to achieve. Where the same person acts both as the chief executive and the chairman, the management will remain present in this forum.

**Independence of directors**

The listing rules do not expressly define ‘independence’ with regard to INEDs. Instead, the Rules set out a non-exhaustive list of situations where the SEHK would cast doubt on a director’s independence. Examples include where the director:

- holds more than a 1 per cent stake in the listed issuer;
- has received the listed issuers’ securities as a gift from the listed issuer or its core connected persons;
- has a material interest in the listed issuer’s principal business activity, or has material business dealings with the listed issuer’s group;
- is or was a director, partner or principal of a professional adviser to the listed issuer during the two years prior to his or her appointment; or
- had a management role in the listed issuer’s group during the two years prior to his appointment.

In addition, if an INED has served more than nine years in the company, that could undermine his or her independence. In this situation, the CG Code requires that the INED’s further appointment be subject to a separate shareholders’ resolution.

Independence might also be called into question if an INED holds cross-directorships or has significant business links with other directors. A new recommended best practice was introduced recently, such that the board should explain why the director remains independent despite having such ties.

**Chairman and chief executive**

It is an express principle under the CG Code that there be a clear division of responsibilities for the management of the board and the management of the company’s day-to-day business. The purpose is to encourage a balance of power and authority, and avoid power being concentrated in one individual. Flowing from this principle, issuers should split the roles of chairman and chief executive, and have them performed by different people. The chief executive should focus on strategy and operations, while the chairman should lead the board and promote good corporate governance. If there is any financial, business, family or other material relationship between the chairman and the chief executive, that must be disclosed in the issuer’s annual report.

As mentioned above, the CG Code operates on a ‘comply or explain’ basis, so it remains possible in Hong Kong to have the same person conduct both roles, so long as there is good reason justifying such an arrangement. In fact, among all code provisions, the requirement for separating the chairman and chief executive has consistently recorded the lowest compliance

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4 A cross-directorship arises when two directors sit on each other’s board.
rates, with issuers citing as reasons for this the need for ‘strong and consistent leadership’ and ‘more effective formulation and implementation of long-term business strategies’. This is, perhaps, no surprise given the make-up of the Hong Kong market, where many listed companies remain family-controlled, dominated by a majority shareholder or both.

**Delegation of corporate governance responsibilities**

While the board is ultimately responsible for ensuring compliance with corporate governance standards, it may delegate responsibilities for implementation to board committees. The key board committees for a Hong Kong listed company are the audit, nomination and remuneration committees. Common to them is the requirement for significant involvement of INEDs in each committee. The chairman of the board and the chair of each committee are expected to attend general meetings and to answer questions from shareholders.

**Audit committee**

The listing rules require issuers to set up an audit committee. Its key functions include monitoring the integrity of the issuer’s financial statements, risk management and internal control, and reviewing the independence of external auditors. Members should be proactive in understanding the issuer’s affairs and watch out for potential red flags.

Only non-executive directors are eligible for membership. The committee should have at least three members, with a majority being INEDs. At least one of the INEDs must possess professional qualifications or expertise in accounting or financial management. The committee must be chaired by an INED.

**Nomination committee**

It is a CG Code requirement to establish a nomination committee. The committee should have a majority of INEDs, and be chaired by either the chairman of the board or an INED. The committee’s core function is board recruitment. Members should work towards a board that possesses a balance of skills, experience and diversity of perspectives appropriate to the issuer’s business. The committee should do so through a fair and transparent selection process. It is also the committee’s duty to consider succession planning and promote the long-term success of the company.

**Remuneration committee**

As a listing rule requirement, issuers must establish a remuneration committee. The committee must have a majority of INEDs, and be chaired by an INED. The committee should ensure that remuneration levels of the management are sufficient to attract and retain those who are crucial to the company’s success, but without paying more than necessary. In formulating remuneration packages, the committee should have regard to salaries paid by comparable issuers. No director should decide his own remuneration. If the board decides to approve any remuneration arrangements with which the remuneration committee disagrees, the board should explain their decision in the next corporate governance report, which usually comes as a chapter of the annual report.

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5 This code provision A.2.1 recorded a 64 per cent compliance rate in the 2017/2018 review and a 63 per cent compliance rate in the 2016 review. See HKEx, (2018). Analysis of Corporate Governance Practice Disclosure in June and December Year-End 2017 and March Year-End 2018 Annual Reports, p. 14.
Executive pay
The listing rules require that details of directors’ basic salary, discretionary bonuses, contributions to pension schemes, and other forms of remuneration be disclosed in the company’s financial statements on an individual and named basis. Furthermore, it is a recommended best practice that a significant portion of the executive directors’ remuneration be linked to corporate and individual performance.

Issuers must also disclose on a no-name aggregate basis the information relating to the five highest paid individuals for the financial year, unless all of the five are directors, in which case their remuneration would have been disclosed as discussed anyway. The CG Code expects issuers to disclose pay ranges for senior management in bands. It is also a recommended best practice to disclose the remuneration of senior management in annual reports on an individual and named basis.

ii Directors
Director’s duties
Regardless of an issuer’s place of incorporation, the listing rules specifically require that all directors fulfill fiduciary duties and duties of care, skill and diligence to a standard commensurate with Hong Kong law requirements. In Hong Kong, only the duty of care of directors has been codified in the Companies Ordinance. Fiduciary duties remain a matter of common law.

Directors are fiduciaries of the company, and as such are entrusted to manage the company’s assets and affairs. The ultimate goal of fiduciary law is to police the exercise of discretion. It does so by removing temptation and unconscious bias that may lead a fiduciary to exercise powers for an extraneous purpose. In the words of Lord Herschell, fiduciary law is ‘based on the consideration that, human nature being what it is, there is danger, in such circumstances, of the person holding a fiduciary position being swayed by interest rather than by duty, and thus prejudicing those whom he was bound to protect’. It follows that a fiduciary must, therefore, not profit from his or her position, or have conflicting interests or duties, unless the beneficiary has given informed consent.

Flowing from these principles, and unless the company has consented otherwise through shareholders’ approval, a director is under a duty:

- to act in good faith in the interests of the company as a whole;
- to exercise powers for proper purposes;
- to avoid conflict of interest; and
- not to profit from his position at the expense of the company.

The listing rules contain various provisions that spell out directors’ fiduciary duties. For instance, subject to certain narrow exceptions, the listing rules prohibit a director from voting on any board resolution that approves a contract, arrangement or proposal in which that director (or associates) has a material interest. A proposed transaction between the issuer and a director or his or her associates will, in most circumstances, constitute a connected transaction, which will trigger the requirement for the company’s informed consent by virtue of an independent shareholders’ approval.

6 Bray v Ford [1896] AC 44 (HL) 51.
As for a director’s duty of care, the Companies Ordinance requires a director to exercise a standard of care, skill and diligence that would be exercised by a reasonably diligent person with:

- the general knowledge, skill and experience that may reasonably be expected of a person carrying out the functions carried out by the director in relation to the company; and
- the general knowledge, skill and experience that the director actually has.

Requirement (a) sets out the minimum objective standards expected of all directors. A director who did his or her incompetent best could still fall short of this objective standard of care. In cases where the director possesses special knowledge, skills and experience, requirement (b) holds him or her accountable to that higher standard.

Directors may delegate responsibilities to members of the company’s management, but in order to properly discharge their duty of care, directors must establish reporting mechanisms and controls that facilitate meaningful oversight. Under the CG Code, issuers should set out a schedule of reserved matters, such that management can know with clarity which decisions can only be made by the board.

**Dealing in securities**

Directors’ dealings in the issuer’s securities are primarily governed by the Model Code for Securities Transactions by Directors of Listed Issuers (Model Code). The listing rules require all issuers to adopt the Model Code, or alternatively, a securities dealing code that is at least as strict. In practice, most issuers adopt the Model Code, sometimes with minor adaptations. A breach of the Model Code is regarded as a breach of the listing rules.

The key function of the Model Code is to prohibit dealings in securities when a director is in possession of unpublished price sensitive information. It also lays down certain ‘blackout periods’ prior to the release of annual and interim financial results, during which directors are prohibited from dealing, save in very exceptional circumstances. During the windows where directors are not prohibited from trading, the Model Code sets out the procedures for obtaining dealing clearances.

**Term of service and re-election**

The CG Code requires that all directors be subject to retirement by rotation at least once every three years. Under the listing rules, if an issuer proposes to enter into an employment contract for a duration that may exceed three years, with a termination notice period of more than one year, this will require prior shareholder’s approval at a general meeting. In this situation, the remuneration committee must advise shareholders as to whether the terms are fair and reasonable, and whether such a contract is in the interests of the issuer and its shareholders as a whole.

**Board diversity**

Promoting board diversity has been one of the SEHK’s key initiatives in recent years. The SEHK introduced a code provision in 2013 requiring issuers to adopt a policy for achieving board diversity, with measurable objectives to assess its implementation. As a code provision, issuers could choose to deviate and explain why a diversity of perspectives in the board could be achieved despite not having a formal diversity policy in place. After further consultation,
and with much support from market participants, the code provision has been upgraded to a Listing Rule starting in 2019. It is now a mandatory requirement to have in place a policy for board diversity, and to disclose it in the issuer’s corporate governance report.

Since the inception of the code provision in 2013, female representation on the boards of Hang Seng Index constituent companies has increased from 9.4 per cent in 2013 to 13.4 per cent in 2019.7 Whilst such increase in numbers may look encouraging at first sight, Hong Kong still lags behind other international financial centres such as Singapore (15.7 per cent), the United States (27.0 per cent) and the United Kingdom (32.0 per cent).8 The picture is even less encouraging if we look behind the figures. It is not uncommon for founders of family-controlled issuers to appoint their spouses or daughters as non-executive directors. These female directors often play a less substantive role in management, meaning that statistics on female board representation tend to overstate the actual level of gender diversity in Hong Kong listed companies. Whether the recent upgrade of the code provision to a Listing Rule will give further impetus to board diversity remains to be seen. For now, suffice to say there is still a long way for the Hong Kong market to go on board diversity.

III DISCLOSURE

i Financial reporting

Timely disclosure of financial information is one of the most critical requirements under the listing rules. Non-compliance will normally lead to suspension of trading in the issuer’s securities, until the requisite financial information is published.

Annual reports containing audited accounts must be published within four months of the financial year-end. Issuers also need to publish interim reports within three months of the end of the half-year period. In the run-up to the publication of annual reports and interim reports, there will inevitably be a time gap between the financial statements being approved by the board and their actual publication. Since information in the financial statements is usually highly price sensitive, and with a view to maintaining a fair and orderly market, the listing rules require the publication of ‘preliminary announcements’ of financial results, which must be published no later than the day following the board’s approval of the issuer’s financial statements. If an issuer fails to publish preliminary announcements in time, for example due to uncertainties around certain figures, it must issue a holding announcement, suspend trading, and explain to the market the reasons behind the delay.

The CG Code expects directors to acknowledge their responsibilities for preparing financial accounts. It also requires directors to include a statement in the annual report, setting out their discussion and analysis of the issuer’s performance, an explanation of the business model and their strategy for delivering the issuer’s objectives. The CG Code stresses that long-term financial performance, rather than short term rewards, should be a corporate governance objective.

8 ibid.
ii Disclosure of price-sensitive information

Another key disclosure obligation for Hong Kong issuers is the timely disclosure of price-sensitive information – a critical measure to eliminate asymmetry of information and possible abuse by corporate insiders. This obligation was previously a Listing Rule requirement, but it received statutory backing in the SFO in 2013 with a view to imposing stricter penalties on offenders. Currently, the SFC enforces the statutory disclosure regime under the SFO.

The obligation to make disclosure is triggered once the issuer is in possession of price sensitive information. Knowledge of the issuer’s management is imputed to the issuer. It follows that issuers must establish and maintain an effective internal control system, such that material information known to its management is promptly escalated to board level for assessment. Directors should take reasonable steps to ensure that proper safeguards for timely disclosures are in place, failing which directors can be personally liable.

It is acknowledged that premature disclosure of price sensitive information may at times be prejudicial to a company’s legitimate interests. To strike a balance, the statutory disclosure regime carves out several safe harbours. For instance, issuers are exempted from disclosing proposals or negotiations when they are at a formulative stage, so long as the discussions are kept confidential. If confidentiality is lost, issuers must suspend trading, until an announcement is made to eliminate any asymmetry of information.

Late disclosure may lead to civil sanctions. The SFC can take enforcement proceedings at the Market Misconduct Tribunal. Sanctions available to the tribunal include fines, disqualification orders for officers and cold shoulder orders. Since the regime’s inception in 2013, the SFC has commenced eight proceedings, with four concluded to date. Fines for non-compliant directors range from around HK$1 million, together with an additional order covering the SFC’s investigation costs.

iii Notifiable transactions and connected transactions

The listing rules contain announcement requirements when an issuer enters into connected transactions, or significant transactions that are out of the ordinary course of the issuer’s business (known as ‘notifiable transactions’). Depending on the size and nature of the transactions, there may be further requirements for shareholders’ approval.

iv Disclosure of interests

The SFO also contains a separate regime that aims to provide the investing public with transparency on the ownership of listed issuers. Shareholders who are directly or indirectly interested in 5 per cent or more of a listed company’s voting share capital must report their interests and short positions through an online filing system. Further reporting is required if their shareholding percentage changes and crosses, whether up or down, a whole number percentage level (e.g. an increase from 6.8 per cent to 7.2 per cent or vice versa). Directors and chief executives of listed issuers must disclose all their interests and short positions in the relevant issuer and its associated corporations, regardless of the size of their stake.
IV CORPORATE RESPONSIBILITY

i Risk management

The incurrence of risk is an inevitable element in the conduct of a company's business, and it is the board’s responsibility to identify and seek to control such risks. The board should assess its risk appetite in light of the company’s objectives, and set the right ‘tone at the top’. The CG Code requires the board to review and test its risk management and internal control systems on an annual basis, with a view to assessing their effectiveness and responding to changes of circumstances. After the annual review, the board should report their findings in its corporate governance report.

ii ESG reporting

Since 2016, Hong Kong listed companies have a ‘comply or explain’ obligation to assess and disclose environmental, social and governance (ESG) risks. The SEHK’s ESG reporting guide sets out a list of areas for issuers to attend to, including emissions, use of resources, employment, labour standards, and anti-corruption. If these areas raise material concerns in an issuer’s business operations, the issuer should evaluate the associated risks and disclose its policies surrounding these ESG issues. Issuers are also required to make use of key performance indexes (KPIs) in their ESG reports, so that investors can evaluate the implementation of their policies and management systems.

The SEHK recognises that every business is different. Certain areas in the ESG reporting guide may well be immaterial to a particular issuer. In such circumstances, the SEHK has stressed the importance of substance over form. Issuers should explain in the ESG report any aspects that are not relevant, and focus its disclosures on material and relevant ESG issues.9

The SEHK is committed to broadening and deepening ESG reporting obligations.10 Starting in July 2020, the ESG reporting guide will be revised to require disclosures on climate-related issues. Certain KPIs will be amended to provide more particularity on issuers’ ESG performance. Issuers are further encouraged to include independent third-party assurances to enhance the credibility and quality of their ESG reporting. All these moves are indicative of the SEHK’s firm belief that ESG is more than a reputational issue but is closely allied to the governance and financial performance of a company.

iii Whistle-blowing

Hong Kong does not have in place specific legislation on whistle-blowing, although certain protections are available under employment and discrimination laws. It is a recommended best practice for audit committees to establish whistle-blowing policies, so that employees and those dealing with the issuer are able to report improprieties on a confidential basis.

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V SHAREHOLDERS

i Shareholder rights and powers
Shareholders in a Hong Kong incorporated company enjoy powers set out in the Companies Ordinance. For instance, members holding 5 per cent of the company’s voting rights can requisition a general meeting, and put forward matters to be voted on. Certain important decisions, such as change of name, amendments to articles of association and voluntary winding-up, can only be made with a 75 per cent super-majority approval.

The listing rules expect no less from PRC and overseas issuers. Before a PRC or overseas applicant is approved for listing, it must demonstrate that its place of incorporation offers shareholder protection standards that are at least equivalent to those in Hong Kong. If there is any shortfall, the issuer must address the gap through amendments to its constitutional documents. The specific requirements are further set out in a joint policy statement issued by the SFC and HKEx.11

ii Notifiable and connected transactions
A core shareholder right under the listing rules is the right to vote on certain notifiable transactions, and most ‘related-party’ or connected transactions.

For notifiable transactions, shareholders’ approval is required if the transaction exceeds a certain size relative to the issuer. Shareholders’ involvement is considered necessary in this situation, as the issuer is committing itself to a transaction not routine to its business, but with substantive potential impact on its resources and prospects.

As for connected transactions, the complexity of the relevant rules is a unique feature of the Hong Kong regulatory regime. This is largely due to the prevalence of family or state-controlled issuers and the high level of cross-holding in the Hong Kong market. To limit the risks that come with this structure, the listing rules cast a wide net on what constitutes a connected transaction, and subject to certain limited de minimis and other exceptions, renders such transactions conditional upon independent shareholders’ approval. To help independent shareholders make a well-informed decision, issuers are further required to form an independent board committee (IBC) constituted by INEDs only and commission an independent financial adviser (IFA). The IBC and IFA will then tender their advice in a circular to shareholders, providing comments on the fairness of the transaction terms.

iii Takeovers
In the context of a takeover, the interests of directors and shareholders can conflict. The Hong Kong Takeovers Code builds in safeguards, such that directors may not deny shareholders the opportunity to consider an offer, unless shareholders’ approval at general meeting has been obtained.12

Another important shareholder right under the Takeovers Code is the right to exit the company’s shares in the event of a consolidation or change in control. For the purpose of the Takeovers Code, holding 30 per cent or more of the company’s voting rights is regarded as having ‘control’ of the company. Whenever a person (or a group of persons acting in concert) acquires 30 per cent-control of a company, or when a 30 per cent-controller further acquires a 2 per cent stake in the company in any 12-month period, the Takeovers Code requires

that a general offer be made to all other shareholders. The spirit behind this is to ensure that shareholders are given the opportunity to exit after a change or consolidation of control occurs.

iv Shareholders' remedies

Though local legislation generally does not apply to overseas incorporated issuers, shareholders of all Hong Kong listed issuers can bring unfair prejudice petitions and derivative actions under the Companies Ordinance, regardless of the issuer's jurisdiction of incorporation. When the company's affairs have been conducted in a manner unfairly prejudicial to certain members, a shareholder can petition for relief. The court has flexibility in the relief it may grant, including buy-out orders. In the event that directors act in breach of their fiduciary duties or duty of care to the company, shareholders can, with the leave of the court, bring statutory derivative actions against the wrongdoers in the name of the company.

v Shareholder activism

In 2016, the SFC published the Principles of Responsible Ownership, providing non-binding and voluntary guidance to investors on how to fulfill their ownership responsibilities. The principles seek to promote an investment culture where investors actively communicate with management and speak and vote at general meetings. When appropriate, shareholders may even consider taking collective action or making public statements through the media.

The level of shareholders activism in Hong Kong has traditionally been low, mostly as a result of the concentrated shareholding structures in Hong Kong listed companies. Behind-the-scene private settlements are more common, reflecting the cultural aversion against confrontations in this part of the world. Typical arrangements between issuers and activists include trade-offs on board composition, in return for dropping demands or the signing of non-disparagement agreements.

Yet the landscape is changing. As the younger generation succeeds the founders, shareholdings in family-controlled issuers are beginning to diversify. Couple this with a regulatory atmosphere that encourages dialogue between investors and management, and one could well expect that activism in Hong Kong will gradually become more prevalent in the years ahead.

vi Weighted voting rights

After much debate, the listing rules were amended in April 2018 to permit the listing of companies with a weighted voting rights (WVR) structure. This option is, however, only available to companies that the SEHK considers to be ‘innovative’. To address the risks inherent in a WVR structure, where managers are able to maintain majority control with a relatively small stake, the listing rules built in certain safeguards. These protections include:

a requiring resolutions on the amendment of articles, variation of class rights, appointment and removal of INEDs and auditors, and voluntary winding-up to be approved on a one-share-one-vote basis;

b allowing shareholders with at least a 10 per cent stake calculated on a one-share-one-vote basis to convene general meetings and put resolutions on the agenda;

c requiring the establishment of a Corporate Governance Committee constituted by INEDs only, to review the management’s compliance with listing rules and monitor any conflicts of interests; and
imposing a sunset arrangement, such that the WVR structure will cease when the
beneficiary ceases to be a director of the issuer.

Whether these arrangements will prove sufficient to protect investors’ interests will remain
a subject of debate. However, investor safeguards for Hong Kong listed WVR companies
are already more comprehensive than those available in New York, London, Tokyo and
Singapore.13

VI OUTLOOK
The dominance of family and closely controlled companies will continue to be a feature
of the Hong Kong market for some time to come. While significant steps have been taken
to address the challenges such structures present, corporate governance standards must
continue to evolve if Hong Kong is to keep pace with international best practices. Going
forward, institutional investors have an important role to play. By taking greater stewardship
of the company’s management as often happens in developed markets, this will significantly
enhance the quality of corporate governance in Hong Kong listed companies.

13 HKEx, (2019). Research Report – Weighted Voting Rights: Angel or Evil To Investors?, Section 2.4 and
Appendix.
Chapter 10

INDONESIA

Daniel Pardede and Preti Suralaga

I OVERVIEW OF GOVERNANCE REGIME

Indonesia is a civil law jurisdiction, and as such does not have a doctrine of precedents similar to a common law system, which means Indonesian courts are not bound by previous court decisions.

Law No. 40 of 2007 on Limited Liability Companies (Company Law) governs limited liability companies in Indonesia. The Company Law provides the general roles of shareholders, boards of directors, boards of commissioners. Further, a company’s articles of association are the general governance document of the company, for example, limitation on the authority of the board of directors and the mechanism on how decisions are made at board of directors meetings, board of commissioners meetings and general meetings of shareholders. In addition, in practice, normally companies also prepare their own good corporate governance manual as a reference for the companies’ ethics and business practices.

The general principle under the Company Law is that the management and its supervisors (the board of directors and board of commissioners, respectively) represent the company and not the shareholders. Under the Company Law, the board of directors is defined as the company organ with the authority and full responsibility for managing the company in the interests of the company, in accordance with the purposes and objectives of the company, and is the organ that represents the company inside and outside the courts in accordance with the provisions of its articles of association. The board of commissioners is defined as the company organ with the duty to conduct general and special supervision of, and provide advice to, the board of directors.

Further, for public companies (i.e., companies with at least 300 shareholders and paid-up capital of at least 300 billion rupiah), the members of the board of directors and the board of commissioners are also subject to capital market regulations, including Law No. 8 of 1995 on Capital Market. Public companies are also supervised by the Financial Services Authority (OJK). Therefore, the conduct of public companies must also comply with the regulations issued by the OJK, which are more detailed and provide clarity on how corporate governance should be implemented: for example, the requirement to establish certain committees and functions, such as an audit committee and a nomination and remuneration function, and to have at least 30 per cent of the commissioners be independent commissioners.

Meanwhile, private foreign investment companies and private local companies are subject to the regulations regarding the field of capital investment. Other specific sectors may

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also have laws and regulations governing how entities engaged in the relevant sectors conduct their corporate governance, for example banks and non-bank financial institutions, and have guidance on compliance with good corporate governance.

In relation to licensing, the government is currently moving all licensing systems into one large national investment licensing platform, the Online Single Submission (OSS) system, as regulated in Government Regulation No. 24 of 2018 on Electronic Integrated Business Licensing Services. The OSS system is now operated by BKPM (initially, the Coordinating Minister of Economic Affairs took the lead in operating the OSS system when it was launched in July 2018). For most sectors, companies no longer need to obtain licences from several authorities: they can now get all the licences they require through the OSS system.

Every business entity (including companies) needs to register with the OSS system. Upon registration, a business identity number (NIB), a business licence and a commercial licence (as relevant) will be issued. The NIB serves as an identity card for companies, and remains valid as long as the company operates. Sectoral ministries or government authorities (e.g., the Ministry of Trade, the Ministry of Communication and Informatics, the Ministry of Agrarian Affairs and Spatial Planning and the National Land Office) determine the business licences or commercial licences required for lines of business under their authority, and the commitments or conditions required to be fulfilled to make the business licences or commercial licences become effective. These sectoral ministries or government authorities could also determine that no commitments or conditions are required. If commitments or conditions exist, they will be mentioned in the business or commercial licences, or both, issued by the OSS system. Business licences and commercial licences will only become effective after a licence owner completes the required commitments or conditions.

II CORPORATE LEADERSHIP

i Board structure and practices

Limited liability companies in Indonesia use a two-tier management structure. The executive functions are managed by the board of directors, which is supervised by the board of commissioners. The board of commissioners does not have an executive function or authority, except in the absence of all members of the board of directors or if all members of the board of directors have conflicting interests with the company. Companies with a shariah-related business activity should have a shariah supervisory board.

The board of directors or the board of commissioners may consist of one or more members. If the board of directors consists of two or more members, the liability is joint and several for each member. A company must have at least two members on the board of directors and two members on the board of commissioners if the company is a public company or if it is collecting or managing public funds or issuing acknowledgements of indebtedness to the public.

If the board of directors consists of more than one member, any member of the board of directors has the authority to act for and on behalf of the board of directors and to represent the company unless the company’s articles of association specify otherwise. In practice, there are a variety of structures used by shareholders and inserted into the articles of association to limit the authority of the members of the board of directors to represent the company, including the following:

a the articles of association require two directors to act for and on behalf of the board of directors and the company;
the articles of association require the president director together with one other director to act for and on behalf of the board of directors and the company;

- the articles of association require that in the absence of the president director, one other director may only act for and on behalf of the company if he or she has first received a written appointment from the president director; or

- the articles of association require the board of directors to obtain approval from the board of commissioners or the general shareholders’ meeting before proceeding with a corporate action.

The above depend on how the shareholders want a company to run its daily activities.

If a director is a party to a court dispute with the company or has a conflict of interest with the company, that director cannot represent the company. In this case, the company must be represented by any of the following:

- another director or other directors who do not have a conflict of interest with the company;

- the board of commissioners, in the event that all members of the board of directors have conflicts of interests with the company; or

- another party appointed by a general shareholders’ meeting if all members of the board of directors and the board of commissioners have conflicts of interests with the company.

Unlike the board of directors, if the board of commissioners has more than one member, no member may act alone in representing the board of commissioners unless it is based on resolutions of the board of commissioners.

The board of directors must act only in the best interests of the company and in accordance with the company’s purpose and objectives. Every director is obligated to fulfil his or her tasks in good faith and with full responsibility. Each director will be personally liable if he or she is wilfully negligent and does not execute his or her tasks as mentioned above unless the director can prove all of the following (as relevant):

- the losses of the company were not caused by his or her fault or negligence;

- he or she has conducted the management of the company in good faith and with prudence, and in line with the purposes and objectives of the company;

- he or she does not have a personal interest, directly or indirectly, in the management act that caused the losses; and

- he or she has taken steps to prevent the occurrence or continuation of such losses.

Under the Company Law, similar to the board of directors, each member of the board of commissioners must undertake his or her duties in good faith and with full responsibility in the interests of the company, in accordance with the purposes and objectives of the company. The main duties of the members of the board of commissioners are to supervise the board of directors’s management policy and to give it advice.

The distribution of the tasks and authorities of the board of directors is determined by a general shareholders’ meeting, or by the board of directors itself if the general shareholders’ meeting does not do so. No law restricts a director from delegating certain responsibilities to other parties, but the director shall continue to be liable for all actions taken by the delegate.
ii Directors
The Company Law does not recognise chair or CEO positions: it only acknowledges the position of members of the board of directors (or board of commissioners in the absence of a board of directors) who may act for and on behalf of the company. In practice, some companies include persons in senior positions, such as a chair or CEO, as members of the board of directors, who are appointed through a general shareholders’ meeting, with the following reasons under the Company Law: only the board of directors can act for and on behalf of a company; and only members of the board of directors have rights to attend and vote in board of directors meetings. Therefore, if a CEO or chair is not a member of board of directors, they cannot act for and on behalf of the company (e.g., represent the company and sign any agreements or documents on behalf of the company) unless they are given the authority to act by the board of directors under powers of attorney. Further, a CEO or chair who is not a member of the board of directors also does not have rights to attend and vote in board of directors meetings, and the employment relationship between the CEO or chair and the company would merely be an employee–employer relationship.

Under the Company Law, the remuneration of directors is usually determined by the shareholders (unless such determination is delegated to the board of commissioners) through a general shareholders’ meeting, and the remuneration of the commissioners is determined by the shareholders through a general shareholders’ meeting. Further, the Company Law does not stipulate the remuneration of senior management who are not members of the board of directors. Therefore, the senior management would likely be treated as employees of the company, and their remuneration would be determined by the board of directors or the remuneration policy that has been implemented in the company.

iii Acquisition
Acquisitions (or takeovers) are legal actions taken by a legal entity or an individual to acquire shares in a company that result in a change of control in the company. Although there is no clear definition of control under the Company Law, the common view is that a transfer or acquisition that results in the acquirer holding a majority of the shares or more than 50 per cent of the shares in a company, whether existing or newly issued shares, which causes a change of control of the company. Another trigger for a change of control is an action that results in the ability to nominate directors and commissioners, and to stipulate management policies shifting to the acquiring entity, but this is more relevant to the acquisition of a public company.

The Company Law requires several actions to be conducted by the boards of directors of the acquiring and target companies in relation to protecting any party having interests in the target company: for example, creditors and employees of the target company.

The shareholders or the board of directors may initiate an acquisition. If the board of directors of the target and acquiring companies initiate an acquisition, the boards of directors of the acquiring and target companies must prepare an acquisition plan. The abridged acquisition plan must then be announced in at least one national newspaper and the proposed acquisition must be notified in writing to the employees of the target company, at the latest 30 days before the calling of the general shareholders’ meeting. The newspaper announcement must include a notice that interested parties can obtain copies of the acquisition plan from the companies’ offices from the date of the newspaper announcement until the date of the general shareholders’ meeting. The creditors of the target company have 14 days after the date of the announcement to file their objections to the plan of the acquisition. If no creditors’
objections are filed within this period, the creditors will be deemed to have approved the acquisition. If objections are filed by creditors, the board of directors of the target company must first settle the objections. If any objections remain unsettled on the date of the general shareholders’ meeting, these objections must be presented at the general shareholders’ meeting to be settled. If any objections remain unsettled after the general shareholders’ meeting, the acquisition cannot be continued.

In addition to the above, the board of directors of the target company should also announce the change of ownership due to the acquisition to its employees in accordance with Law No. 13 of 2003 on Labour (Labour Law). The target company’s employees may choose to not continue their employment and be paid with the applicable termination payments for the change of ownership in the target company under the Labour Law.

With regard to public companies, takeovers and mandatory tender offers (MTO) of public companies in Indonesia are governed by OJK Rule No. 9/POJK.04/2018 dated 27 July 2018 on Takeovers of Public Companies (POJK 9). The definition of a ‘takeover’ of a public company pursuant to POJK 9 is an action that directly or indirectly causes changes to the controller or controllers of a public company. The controller of a public company is defined as a party or parties who either:

a. owns more than 50 per cent of the total issued and paid up shares; or
b. has the ability to determine, directly or indirectly, in whatsoever manner, the management or the policy of the public company, or both.

As a general rule, unless exempted, if there is a takeover, the new controller must undertake an MTO for the remaining shares at the target public company. POJK 9 regulates, among other things, the disclosure requirements for a takeover and MTO, the minimum price in an MTO and the procedures of an MTO.

III DISCLOSURE

i Annual report

The Company Law obliges every company to make an annual report. The board of directors must submit the annual report to the general shareholders’ meeting after it has been reviewed by the board of commissioners, no later than six months after the end of the company’s financial year. The annual report must contain at least:

a. financial statements;
b. a report on the company’s activities;
c. a report on the implementation of social and environmental responsibility;
d. details of issues during the financial year that affect the company’s activities;
e. a report on the supervisory duty that has been performed by the board of commissioners during the previous financial year;
f. the names of the members of the board of directors and board of commissioners; and
g. the remuneration for the members of the board of directors, and the remuneration and compensation for the members of the board of commissioners for the previous year.

ii Audited financial statements

Under the Company Law, a company’s financial statements must be audited if:

a. the activities of the company are to collect or to manage funds from the public;
b. the company issues a debt acknowledgement letter to the public;
If the company fulfils one of the above conditions, but the financial statements are not audited, the general shareholders’ meeting must not approve the financial statements. Balance sheet, and profit and loss statement, of the companies that fall under the criteria in item (c) in Section III.ii, after being approved by a general shareholders’ meeting, must be published in a newspaper. The purpose of this publication is so that the company is transparent and accountable to the public.

Further, Ministry of Trade regulations also require financial statements of certain companies to be filed with the Minister of Trade. There are concerns from private companies about confidentiality, and as a consequence the level of compliance is low.

### iii Mandatory disclosure

The Company Law does not contain extensive stipulations about the mandatory disclosure obligation or a comply and explain model for the implementation of corporate governance by private companies. Meanwhile, the capital market regulations specifically govern those matters, which are applicable for public companies.

With respect to mandatory disclosure, public companies are required to make a disclosure (whether periodical or incidental) under the prevailing capital market rules. For example:

- disclosure of quarterly, semi annual and annual financial statements;
- disclosure of annual reports;
- disclosure of the occurrence of any material information or facts;
- disclosure of certain transactions (e.g., affiliated party or material transactions);
- disclosure of certain corporate actions (e.g., rights issues and non-preemptive rights issuance); and
- disclosure for the purpose of convening a general shareholders’ meeting.

The Company Law regulates the mandatory disclosure (in the form of a newspaper announcement or notification to the employees, or both) for private companies that would like to conduct the following corporate actions (among others):

- acquisitions, mergers, consolidations and spin-offs;
- capital reduction;
- nullification of the appointment of members of the board of directors who fail to meet the requirements according to the Company Law;
- nullification of the appointment of members of the board of commissioners who fail to meet the requirements according to the Company Law;
- remittance of shares in the form of immovable goods; and
- dissolution and liquidation.

### iv Shareholders’ meetings with the board of directors

The Company Law does not regulate one-on-one meetings of directors with shareholders. Normally, shareholders will have a meeting and discussion with the directors through a general shareholders’ meeting. There are two types of general shareholders’ meeting: an
annual general shareholders’ meeting that is conducted annually and an extraordinary general shareholders’ meeting that may be held at any time pursuant to the needs and interests of a company.

The general shareholders’ meeting may adopt resolutions if they meet the quorum and voting criteria as stipulated under the Company Law and articles of association. Consequently, any discussion between the shareholders and directors outside of the meeting should not bind the directors in running the company’s activities. For public companies, there are additional requirements that must be satisfied for convening a general shareholders’ meeting under the prevailing capital market rules. For example, OJK Rule No. 32/POJK.04/2014 on Planning and Conducting General Meetings of Shareholders (as amended by OJK Rule No. 10/POJK.04/2017) (POJK 32) requires that:

a. a general shareholders’ meeting notification be submitted to OJK no later than five business days before the general shareholders’ meeting announcement is made, excluding the date of the general shareholders’ meeting announcement;
b. a general shareholders’ meeting announcement be published at the latest 14 days prior to the date of the general shareholders’ meeting invitation, excluding the date of the general shareholders’ meeting announcement and the date of the general shareholders’ meeting invitation; and
c. a general shareholders’ meeting invitation be published at the latest 21 days prior to the date of the general shareholders’ meeting, excluding the date of the general shareholders’ meeting invitation and the date of the general shareholders’ meeting.

IV CORPORATE RESPONSIBILITY

i Risk management committee

A non-financial services company is not required by the Company Law to have a risk management committee within its management structure. Nevertheless, the OJK regulations require financial services companies (e.g., banks and insurance companies) to have a risk management plan, including having a special officer or committee responsible for all risk management issues (e.g., liquidity or financial compliance). In practice, some non-financial services companies may have established risk management committees, as this may indicate good corporate governance to mitigate or control risks within their companies.

In the absence of a risk management committee, the board of directors is responsible for managing the risks, as the board of directors must act only in consideration of the best interests of the company and in accordance with the company’s purpose and objectives.

ii Compliance

The Company Law provides general requirements regarding a company’s compliance. Meanwhile, Law No. 25 of 2007 on Investment (Investment Law) provides more extensive compliance requirements as follows:

a. implementing the principles of good corporate governance;
b. carrying out corporate social responsibility (CSR) programmes;
c. submitting periodical investment activities reports;
d. complying with all applicable laws and regulations; and
e. respecting the cultural traditions of communities living around the business locations of investments.
iii Whistle-blowing

The Labour Law does not specifically address whistle-blowing by an employee. However, the Labour Law sets out various prohibited reasons for terminating an employee. One of the prohibited reasons is if the employee reports the employer to the authorities due to a criminal action committed by the employer. This reflects that employees who have knowledge of criminal acts of their employers (e.g., corruption or bribery) and have reported those criminal acts to the relevant government authority are protected from retaliation (in form of termination of employment) by their employer.

The implementation of whistle-blower protections arose following practices and scandals, including but not limited to corruption and fraud, involving companies with government institutions and government officials. Whistle-blowing has now become a trend, and one of the main goals of the government is to eradicate corruption in Indonesia.

iv Corporate social responsibility

Under the Company Law, companies that manage or utilise natural resources or whose activities may have an impact on natural resources must fulfil all relevant corporate social and environmental responsibilities. A CSR plan must be inserted into a company’s annual report to be approved by the board of commissioners or the general shareholders’ meeting. Nevertheless, the Company Law is silent on the sanctions that will be imposed on a company if the board of commissioners or shareholders do not approve a CSR plan so that it cannot be conducted or implemented.

The Investment Law, which is currently only applicable for private foreign investment companies and private local companies, provides sanctions for the failure to conduct CSR as follows:

a a written warning;

b a limitation of business activities;

c the temporary suspension of business activities or capital investment facilities, or both;

and

d the revocation of business activities or capital investment facilities, or both.

Moreover, there are no provisions that set out a CSR threshold that companies must meet. Without a threshold, companies may not implement a CSR plan effectively; therefore, this can be deemed to be allowing companies to perform their CSR commitments in any manner they choose as long this fulfils their CSR obligations.

The concept of CSR in Indonesia has been widened by numerous companies, covering, inter alia, employee, consumer and social aspects. Although CSR obligations are not mandatory for companies, some companies have adopted this approach to ensure that the welfare of their employees, consumers and society are accommodated in various forms. Examples of CSR include leadership training for employees and consumer complaints hotlines. By adopting a CSR concept that covers numerous aspects (i.e., not limited to the environment and social wellbeing), companies may enjoy a good corporate image and reputation.
V SHAREHOLDERS

i Shareholder rights and powers

Shareholders’ voting rights

Each of a company’s shares gives a right of one vote to its holder, unless the articles of association determine otherwise. The articles of association may determine the classification of each share issued by the company. Under the Company Law, the classification of shares includes, among others, shares:

a with or without voting rights;

b with special rights to nominate members of the board of directors and the board of commissioners;

c that after a certain period are withdrawn or exchanged for other shares classifications;

d that entitle their holders the priority to receive dividends before the holders of shares with another classification in the allocation of dividends cumulatively or non-cumulatively; and

e shares that entitle their holders to the priority to receive allocations of the remainder of the company’s assets in liquidation.

As described above, a company may issue shares without voting rights. Although the shares were issued with voting rights, a voting right does not apply to the shares if the company’s shares are controlled by the company itself, or (either directly or indirectly) by another company whose shares are directly or indirectly owned by the company.

In addition, holders of a fraction of a nominal value of shares (fraction) do not have individual voting rights. As an exception, the holders will have voting rights if, individually or jointly with other holders, they hold a fraction belonging to the same classification of shares with a nominal value that is as much as one nominal share of the classification.

For shares with voting rights, even though the voting rights of shares are encumbered by pledge or fiduciary, the holder of the shares still has the right to cast a vote in the general shareholders’ meeting for those encumbered shares.

Specifically for public companies, as far as we are aware, the OJK as a matter of policy requires all issued shares to have voting rights.

The powers of shareholders to influence the board of directors

The Company Law regulates that the authority of the board of directors to act for and on behalf of the company is unlimited and unconditional unless stipulated otherwise by the Company Law, the articles of association or the approval of the general shareholders’ meeting. Therefore, it is clear that shareholders may influence the board of directors through the approval of the general shareholders’ meeting. For instance, before starting the next financial year, the board of directors must prepare a business plan (including an annual budget) to be approved by the shareholders or the board of commissioners. In practice, to get the approval of the shareholders, the board of directors will prepare a business plan (including an annual budget) that is relevant to the objective and purpose of the company and the vision of shareholders. The company’s articles of association may also require the board of directors to first obtain the approval of the general shareholders’ meeting for certain corporate actions before proceeding. Below are the quorum and voting rights required under the Company Law for a company to take certain corporate actions:
<table>
<thead>
<tr>
<th>General shareholders’ meeting</th>
<th>Quorum</th>
<th>Votes required to adopt a resolution</th>
</tr>
</thead>
<tbody>
<tr>
<td>1 General shareholders’ meeting to adopt a resolution to:</td>
<td>More than half</td>
<td>More than half of the votes</td>
</tr>
<tr>
<td>• approve the business plan,* annual report,† the appointment or change of members of the board of directors and board of commissioners, and the increase of the issued and paid up capital; and</td>
<td></td>
<td></td>
</tr>
<tr>
<td>• determine the use of net profits and the amount of reserved fund‡</td>
<td></td>
<td></td>
</tr>
<tr>
<td>If the quorum of the first general shareholders’ meeting is not satisfied, a second general shareholders’ meeting may be held.</td>
<td>At least one-third</td>
<td>More than half of the votes</td>
</tr>
<tr>
<td>If the quorum of the second general shareholders’ meeting is not satisfied, upon the company’s request, the quorum will be determined by the chief justice of the district court where the company is domiciled.</td>
<td></td>
<td></td>
</tr>
<tr>
<td>2 General shareholders’ meeting to adopt a resolution to:</td>
<td>At least two-thirds</td>
<td>At least two-thirds of the votes</td>
</tr>
<tr>
<td>• amend the company’s articles of association;</td>
<td></td>
<td></td>
</tr>
<tr>
<td>• increase the issued and paid-up capital that will result in an increase of the authorised capital;</td>
<td></td>
<td></td>
</tr>
<tr>
<td>• increase the authorised capital alone;</td>
<td></td>
<td></td>
</tr>
<tr>
<td>• reduce the authorised, issued and paid-up capital;</td>
<td></td>
<td></td>
</tr>
<tr>
<td>• repurchase the company’s shares, and subsequent transfer of the company’s shares repurchased by the company; and</td>
<td></td>
<td></td>
</tr>
<tr>
<td>• approve the conversion of the shareholders’ or creditors’ loans into capital in accordance with of the Company Law.</td>
<td></td>
<td></td>
</tr>
<tr>
<td>If the quorum of the first general shareholders’ meeting is not satisfied, a second general shareholders’ meeting may be held.</td>
<td>At least three-fifths</td>
<td>At least two-thirds of the votes</td>
</tr>
<tr>
<td>3 General shareholders’ meeting to adopt a resolution to:</td>
<td>At least three-quarters</td>
<td>At least three-quarters of the votes</td>
</tr>
<tr>
<td>• approve merger, consolidation, acquisition, separation, bankruptcy application of the company, extension of the term of the company and dissolution of the company; and</td>
<td></td>
<td></td>
</tr>
<tr>
<td>• transfer or place as security more than 50 per cent of the company’s assets in one or more transactions.</td>
<td></td>
<td></td>
</tr>
<tr>
<td>If the quorum of the first general shareholders’ meeting is not satisfied, a second general shareholders’ meeting may be held.</td>
<td>At least two-thirds</td>
<td>At least three-quarters of the votes</td>
</tr>
</tbody>
</table>

* The approval can be delegated to the board of commissioners
† Note that an annual report is approved in an annual general shareholders’ meeting
‡ Note that the use of net profits and the amount of reserved fund is determined in an annual general shareholders’ meeting

A company’s articles of association may stipulate different quorum and voting requirements for a general shareholders’ meeting required to pass resolutions. However, the articles of association may only stipulate higher (not lower) quorum and voting requirements from those provided under the Company Law.

In addition, for certain matters, public companies are subject to higher quorum and voting requirements from those provided under the Company Law. For example, for amending a public company’s articles of association under POJK 32 the quorum requirement is at least two-thirds and the voting requirement is more than two-thirds.

### Shareholders’ duties and responsibilities

In general, the Company Law does not put the obligation for corporate governance to the shareholders. However, in some highly regulated sectors – for example, insurance – the controlling shareholders may be required to declare that they are the parties responsible for the insurance company.

### Shareholder activism

If a shareholder disagrees about actions of the company that are causing harm to that shareholder or to the company itself, that shareholder has a right to sell its shares to the company at a reasonable price. The actions are in the form of one of the following:
a an amendment to the articles of association of the company
b a transfer and encumbrance of more than 50 per cent of the net assets of the company
c consolidation, merger, acquisition or spin-off of the company

In the above situation, the shares are to be purchased or repurchased by the company. The company can only hold them for a certain period. In the event that such temporary ownership of shares by the company exceeds the threshold allowed under the Company Law, then the company must find a third party to buy those shares. Concerning the threshold, the buyback must not cause the net assets of the company to be lower than the aggregate of the subscribed capital and the statutory reserved fund of the company; and the total nominal value of the shares that are owned by the company or its subsidiaries (including those held under security) must not exceed 10 per cent of the nominal value of the issued shares in the company).

Further, if the shareholder is harmed by an action of the company that he or she considers to be unfair and unreasonable as a result of resolutions of the general shareholders’ meeting, board of directors or board of commissioners, the shareholder has a right to lodge an action against the company before the relevant district court.

The Company Law also allows one or more shareholders holding at least 10 per cent of the issued voting shares in a company to lodge an examination of the company to the district court. This examination can be requested if there is ‘reason to suspect’ any of the following:

a The company has committed an unlawful act that is detrimental to the shareholders or to third parties.
b The directors or commissioners have committed unlawful acts that are detrimental to the company, the shareholders or third parties.

div Acquisition defences

As mentioned in Section Vi, certain decisions may not be taken by the board of directors without shareholder approval. For example, see the following table:

<table>
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<td>1 General shareholders’ meeting to adopt a resolution to:</td>
<td>At least two-thirds</td>
<td>At least two-thirds of the votes</td>
</tr>
<tr>
<td>• amend the company’s articles of association;</td>
<td></td>
<td></td>
</tr>
<tr>
<td>• increase the issued and paid-up capital that will result in an increase of the authorised capital;</td>
<td></td>
<td></td>
</tr>
<tr>
<td>• increase the authorised capital alone; and</td>
<td></td>
<td></td>
</tr>
<tr>
<td>• reduce the authorised, issued and paid-up capital</td>
<td></td>
<td></td>
</tr>
<tr>
<td>If the quorum of the first general shareholders’ meeting is not satisfied, a second general shareholders’ meeting may be held.</td>
<td>At least three-fifths</td>
<td>At least two-thirds of the votes</td>
</tr>
<tr>
<td>2 General shareholders’ meeting to adopt a resolution to approve the merger, consolidation, acquisition, separation, or bankruptcy application of the company, extension of the term of the company and dissolution of the company.</td>
<td>At least three-quarters</td>
<td>At least three-quarters of the votes</td>
</tr>
<tr>
<td>If the quorum of the first general shareholders’ meeting is not satisfied, a second general shareholders’ meeting may be held.</td>
<td>At least two-thirds</td>
<td>At least three-quarters of the votes</td>
</tr>
<tr>
<td>3 General shareholders’ meeting to adopt a resolution to transfer or place as security more than 50 per cent of the company’s assets in one or more transactions.</td>
<td>At least three-quarters</td>
<td>At least three-quarters of the votes</td>
</tr>
<tr>
<td>If the quorum of the first general shareholders’ meeting is not satisfied, a second general shareholders’ meeting may be held.</td>
<td>At least two-thirds</td>
<td>At least three-quarters of the votes</td>
</tr>
</tbody>
</table>
Further, the Company Law also allows shareholders to include additional provisions in the articles of association to limit the board of directors' authority to conduct certain corporate actions (e.g., requiring approval from the board of commissioners or the shareholders, or both).
Ireland

Paul White

I

OVERVIEW OF GOVERNANCE REGIME

In Ireland, the corporate governance of business organisations is derived from a combination of corporate law, statutory regulations and codes (for the most part non-binding). In addition, for privately owned corporations, while the governance architecture is explicitly dealt with in the constitutional documents and by-laws (known as the constitution or articles of association), it is also often addressed as a matter of contract between the shareholders in a shareholders’ agreement.

For the purposes of this chapter, we will focus on corporate governance in public or listed companies.

Corporate governance requirements for listed companies

In Ireland, companies listed on the principal Irish securities market, Euronext Dublin, are required to comply with both the UK Corporate Governance Code (Corporate Governance Code) and the Irish Corporate Governance Annex.

The terms of the recently updated Corporate Governance Code are dealt with elsewhere in this publication, and it is not proposed that those terms be restated here. An important basis or feature of the Corporate Governance Code is the comply or explain approach to compliance. Under the Irish Stock Exchange Listing Rules (Listing Rules), companies listed on Euronext Dublin are expected to comply with the Corporate Governance Code or set out an explanation for any deviation from its provisions in their annual report to shareholders.

The Irish Corporate Governance Annex asks for meaningful, evidence-based descriptions in the annual report of how the Code is applied rather than ‘recycling’ descriptions that replicate the wording of the Code.

The Irish Annex identifies the following key recommendations for inclusion in the annual report:

a an explanation as to why the number of non-executive directors is regarded as sufficient;
b a description of the skills, expertise and experience of each director – including government appointees;
c the process followed in selecting and appointing new directors;
d the methodology in the annual evaluations of the directors individually and collectively;

1 Paul White is a partner at A&L Goodbody. The information in this chapter is correct as at March 2019.
2 A mixture of primary legislation and common law.
3 The updated Corporate Governance Code applies to accounting periods beginning on or after 1 January 2019.
4 See the United Kingdom chapter.
the factors taken into account when determining a director’s independence;
f a description of the work carried out by the audit committee generally, and in relation to risk oversight more specifically; and
g a description of the remuneration policy, how performance elements are deferred and any clawback arrangements.

Furthermore, companies listed on the smaller Irish securities market, Euronext Growth, are also encouraged to adopt a corporate governance code on admission to that market, and are required to publish details of the corporate governance code it has chosen to apply and how it complies with that code, or a statement that it has not adopted any code if that is the case. In practice, a number of them adhere to the Principles of Corporate Governance issued by the UK Quoted Companies Alliance.

ii Banks and other financial institutions

Banks and insurers in Ireland follow, on a statutory and mandatory basis, separate corporate governance requirements issued by the Central Bank of Ireland in 2016. Banks are required to follow the Corporate Governance Requirements for Credit Institutions 2015 (Credit Institutions Requirements) and insurance undertakings follow the Corporate Governance Requirements for Insurance Undertakings 2015 (Insurance Undertakings Requirements). Captive insurance and reinsurance undertakings are required to follow the Corporate Governance Requirements for Captive Insurance and Captive Reinsurance Undertakings 2015.

The significance of the Credit Institutions Requirements and the Insurance Undertakings Requirements (together, the CBI Requirements) is that they are mandatory; in other words, the comply or explain approach to compliance does not apply.

The CBI Requirements include the following:

a boards must have a minimum of seven directors in major institutions and a minimum of five in all others;
b requirements on the role and number of independent non-executive directors (including internal and external evaluation, training and professional support);
c criteria for director independence and consideration of conflicts of interest;
d limits on the number of directorships that directors may hold in financial and non-financial companies to ensure they can comply with the expected demands of board membership of a credit institution or insurance company;
e clear separation of the roles of chair and chief executive officer;
f a prohibition on an individual who has been a chief executive officer, director or senior manager of an institution during the previous five years from becoming chair of that institution;
g a requirement that board membership is reviewed at a minimum every three years;
h a requirement that boards set the risk appetite for the institution and monitor adherence to this on an ongoing basis;
i minimum requirements for board committees, including audit and risk committees;
j prescriptive measures around how and when board meetings must be held, and attendance by directors;
k a requirement for an annual confirmation of compliance to be submitted to the Central Bank;
l the use of videoconferencing where a director cannot attend a meeting; and
the audit committee as a whole must have relevant financial experience, and one member must have an appropriate qualification.

Corporate governance themes such as diversity and risk are also reflected in the CBI Requirements. For example, the Credit Institutions Requirements provide that a chief risk officer must be appointed to oversee the institution’s risk management function, and that a risk committee must be established. The chair of this committee must be a non-executive director and the committee must be composed of a majority of non-executive directors. The audit and risk committees must have a minimum of three members.

The board or nomination committee is also required to establish a written diversity policy for consideration in future board appointments.

II CORPORATE LEADERSHIP

The principal leadership role for any company is played by the board of directors. The role of the director is governed principally by the Companies Act,\(^5\) the primary source of corporate law in Ireland, and by principles established by case law (in this regard, it is worth noting that English case law is generally regarded as having persuasive authority in Ireland). This body of law is further supplemented by a growing suite of statutory regulations, codes and guidelines, many of which have been mentioned elsewhere throughout this chapter. Below is a brief (and non-exhaustive) discourse on some of the more significant aspects of the law surrounding directors and the structures and practices of boards in Ireland.

i Board structure and practices

One-tier structure

Generally, the board of directors of an Irish company is structured as a one-tier body (usually comprising both executive directors and non-executive directors), unlike in other jurisdictions where two-tier structures are more common. Irish law does not prohibit the two-tier board, but it does not arise in practice: were it to do so, directors would be likely to face the same liability regardless of their position within a two-tier board system.

Composition of the board

Every Irish public company must currently have at least two directors, but the articles of association of the company (i.e., its constitution) may provide for a greater minimum number (as may any applicable corporate governance code that applies to the company). Since the Companies Act, private companies limited by shares are permitted to have a sole director, but they must also have a separate company secretary. A body corporate is prohibited from becoming a director of an Irish company. As in other jurisdictions, a public company or a large private company will generally have a combination of executive and non-executive directors on its board, whereas a small private company will generally have all executive directors.

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\(^5\) The Companies Act 2014.
Authority of the directors to represent the company

A director can only enter into a proposed contract on behalf of a company where it is within his or her permitted delegated authority to do so, unless that contract or commitment has been approved by the board. The authority of the director may be actual or ostensible. Actual authority is usually rooted in the service contract between a company and the director. It can also be implied, for example, by the ordinary course of the business of the office that the director holds, such as managing director or chief executive officer. However, even where no actual authority exists, the company may still be bound by the director’s actions when he or she acts within his or her ostensible or apparent authority (i.e., where he or she is held out by the company as having the authority, for example, of a particular office holder such as managing director or chief executive officer). In grappling with the principles surrounding actual and ostensible authority, it is also necessary to bear in mind the internal management principles, which mean that, if a third party is dealing with a company, he or she is not obliged to enquire into the regularity of its internal proceedings. However, this rule is not absolute, and there are limits to its scope and operation. The board of directors and individuals authorised by the company are entitled to bind it. Persons authorised may be registered on a register maintained in the public Companies Registration Office as being entitled to bind the company, although this is not a mandatory requirement.

Legal responsibilities of the board

The root source of all corporate authority lies with the shareholders. However, as in other jurisdictions, shareholders generally delegate the management of the company to the board of directors and allow them to exercise all the powers of the company except a specific number of matters that must, under statute, be exercised by the shareholders.

Chair

While the chair of a company has specific roles (and, to an extent, responsibilities), including chairing the board of directors and shareholder meetings, he or she does so as a director. As a director, he or she is subject to the same duties and has the same authority as that of any other board member. Where a company adopts a standard constitution or articles of association, the chair will enjoy an additional vote in the event of an equal number of votes being cast in respect of any matter at board level.

Significantly, for companies listed on Euronext Dublin, the Corporate Governance Code contains a number of provisions relating to the role of chair. The chair has responsibility:

a  to ensure that a culture of openness and debate prevails;

b  to ensure that directors receive accurate, timely and clear information;

c  to ensure that all directors are made aware of shareholders’ views: in particular, the chair must seek regular engagement with major shareholders on matters such as governance and performance against strategy;

d  to consider a regular externally facilitated board evaluation; and

e  subject to limited exceptions, not to remain in the post for a term of longer than nine years.
Delegation of board responsibilities

In general, the board of directors may delegate its authority to an individual director, to employees or to committees established by the board. Having delegated powers, the directors are not absolved from all responsibility in relation to the delegated actions, as the directors will continue to be under a duty to investigate the operations of the company diligently and with skill.

It is also open to a director, subject to the constitution or articles of association of the company, to appoint an alternate to fulfil his or her duties on his or her behalf, generally in relation to a specific action or time period. Whereas the alternate is personally liable for his or her own actions, the appointing director again is not absolved and can be held responsible along with the alternate.

Chief executive officer

Irish law is not particularly prescriptive in relation to the role of managing director or chief executive officer. In general, the powers of the chief executive officer are not fixed by law, but depend instead upon the terms of the service agreement agreed from time to time between the board and the chief executive.

To ensure that there is a clear division of responsibilities between the running of the board and the running of the company’s business, the Corporate Governance Code and CBI Requirements (among others) recommend that the role of chair and chief executive officer should not be fulfilled by the same individual. The Corporate Governance Code also suggests that no former chief executive officer should become chair of the same company, and that the division of responsibilities between the chair and the chief executive officer be clearly established, set out in writing and agreed by the board.

Committees of the board

As previously mentioned, Irish companies commonly delegate certain matters to committees established by the board. Under Irish company law, public limited companies are required to establish an audit committee. The Listing Rules require that certain listed companies are further required to constitute certain other governance committees. Credit institutions, insurance or reinsurance undertakings and other regulated entities are subject to separate requirements under applicable authorisation regimes.

Board and company practice in takeovers

The two principal sources of responsibility imposed upon directors of a company in the course of a takeover offer are common law and the Rules of the Irish Takeover Panel (Takeover Rules), which have the force of law in Ireland. Two other important sources of duties and obligations are the Listing Rules and the Companies Act.

The Takeover Rules, in particular, cover a wide range of matters relating to takeovers, and it is the responsibility of each company director, whether executive or non-executive, to ensure, so far as he or she is reasonably able, that the Takeover Rules are complied with during offer periods. In essence, the Takeover Rules prohibit a company from taking any action that might frustrate the making or implementation of an offer for the company, or depriving the

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6 See Section III.ii for further information.
shareholders of the opportunity of considering the merits of such an offer at any time during the course of the offer or at any earlier time at which the board has reason to believe that the making of such an offer may be imminent.

ii Directors

Non-executive or outside directors

Under Irish law, no distinction is drawn between the non-executive director and any other director, so non-executive directors owe the same duties as other directors to the company, its creditors and employees.

Where non-executive directors are appointed on the nomination of a third party, most commonly a shareholder, the nominee is entitled to have regard to the appointer’s interests, but only to the extent that they are not incompatible with his or her duty to act in the interests of the company.

The non-executive director role has attracted much attention recently in terms of the importance of the role as an independent watchdog. The Corporate Governance Code, for example, requires the non-executive directors of listed companies to constructively challenge board strategy. In addition, it recommends that the board should appoint one independent non-executive director to be the senior independent director to provide a sounding board for the chair, and that the board should not agree to a full-time executive director taking on more than one non-executive directorship or the chair in a FTSE 100 company or equivalent Irish company (FTSE 350 equivalent). There are some recent sources of guidance for non-executive directors on care, skill and due diligence, which are available to Irish non-executive directors.

Duties of directors

The duties of directors in Ireland are grounded in case law, legislation and related rules and codes. These duties, predictably, echo those in other jurisdictions.

Since 1 June 2015, a codified set of principal directors’ duties has been in force in Ireland, under the Companies Act. The list of eight codified duties has its origins in the common law historically developed by the courts in Ireland and the United Kingdom.

The principal fiduciary duties of directors that have been enumerated in the Act are as follows:

- the duty to act in good faith in what the director considers to be in the interests of the company;
- the duty to act honestly and responsibly in relation to the conduct of the company’s affairs;
- the duty to act in accordance with the company’s constitution and exercise his or her powers only for the purposes allowed by law;
- the duty to not use the company’s property, information or opportunities for his or her own or anyone else’s benefit unless this is expressly permitted by the constitution or approved by resolution of the members in a general meeting;
- the duty to not agree to restrict the director’s power to exercise an independent judgement, unless this is expressly permitted by the company’s constitution, or the director believes in good faith that it is in the interests of the company for a transaction or arrangement to be entered into for him or her to fetter his or her discretion in the future by agreeing to act in a particular way to achieve this, or the directors agreeing to this has been approved by resolution of the members in general meeting;
the duty to avoid any conflict between the director’s duties to the company and his or her other (including personal) interests unless the director is released from this duty in accordance with the constitution, or by a resolution of the members in general meeting;  
the duty to exercise the care, skill and diligence that would be exercised in the same circumstances by a reasonable person having both the knowledge and experience that may reasonably be expected of a person in the same position as the director; and the knowledge and experience that the director has; and  
the duty to have regard to the interests of the company’s employees in general and of its members.

These duties are owed to the company and are enforceable by the company in the same way as any other statutory duties owed by the director to the company. The Act provides that these principles are based in common law and equitable principles, and that the new statutory duties must be interpreted and applied as such.

**Directors’ compliance statement**

As a result of an obligation introduced by the Companies Act, public limited companies are required to include a compliance statement in the directors’ annual report accompanying their company’s financial statements. This requirement applies in respect of financial years commencing on or after 1 June 2015.

Directors must acknowledge that they are responsible for securing their company’s compliance with its relevant obligations (which includes obligations under tax law, and some of the more serious capital maintenance and financial disclosure and reporting obligations).

Directors must also, on a comply or explain basis, confirm:

- that they have drawn up a compliance policy statement appropriate to their company setting out the company’s policies regarding compliance;
- that appropriate arrangements or structures are in place that are, in the director’s opinion, designed to secure material compliance with its relevant obligations; and
- that they have reviewed, during the financial year, the arrangements or structures that have been put in place to secure this material compliance.

If these statements, confirmations and reviews have not been made or carried out, the directors must specify in their directors’ report the reasons why not.

**Statutory audit confirmation**

The Companies Act introduced a new statutory obligation on the directors of all companies to include a statement in their directors’ report that so far as each director is aware, there is no relevant audit information of which the company’s auditors are unaware, and each director has taken all the steps that he or she ought to have taken as a director to make himself or herself aware of any relevant audit information, and to establish that the company’s auditors are aware of that information. This is similar to the obligation that has existed in the United Kingdom since 2006.

**Liability of directors**

Directors are not liable for the commitments and obligations of the companies they serve. Directors can be held personally liable or subject to fines and, in very serious circumstances, imprisonment for breaches of various statutory provisions such as those
relating to company law, environmental law and health and safety law. Examples under the Companies Act include where the director engages in insider dealing or where the director makes false or misleading statements in certain circumstances.

Under the Companies Act, a new streamlined summary approval procedure (SAP) has been created to enable companies to carry out certain activities that would otherwise be prohibited (such as financial assistance, capital reductions and repayments, mergers). The SAP is only available to public limited companies for a members’ voluntary winding up, the prohibition on pre-acquisition profits or losses being treated in a holding company’s financial statements as profits available for distribution, and the prohibition on entering into loans or quasi-loans to directors or other connected persons.

Under the SAP rules, a directors’ declaration of solvency and shareholder approval is required, and in some cases a confirmatory auditors’ report is also required. The SAP rules provide that a court may declare a director personally responsible, without any limitation of liability, for all or any liabilities of the company where a declaration is made without having reasonable grounds for the opinion on the solvency of the company as set out in the declaration.

In the context of entering a contract on behalf of a company, a director can be made personally liable where he or she commits a tort or fraud on behalf of the company (or induces the company to do so), where he or she gives a personal guarantee, or where he or she fails to make the other party aware that he or she is acting as an agent for the company.

In the context of insolvency, directors may also face personal liability in a limited number of circumstances: for example, where they engage in fraudulent or reckless trading, misapply company assets or make an incorrect declaration of solvency in the context of a voluntary liquidation. On insolvency, a director may also face restriction for five years or disqualification for up to five years or such other period as the courts think fit.

Appointment, term of office, removal

The appointment and removal of directors is generally governed by the company’s constitution or articles of association. The right to elect directors is generally reserved to shareholders save where a casual vacancy arises. The directors usually have the right to fill a casual vacancy, by a resolution of the directors passed at a board meeting or by unanimous written resolution of the directors, but this appointment might then, particularly with public companies, be subject to shareholders’ confirmation at the next annual general meeting (AGM) after such an election. Under the Companies Act, the directors of a public limited company are required to retire by rotation unless the company’s constitution provides otherwise. For listed companies to which the Corporate Governance Code applies, all of the directors must be reappointed annually.

Apart from the terms of the constitution or articles of association, shareholders also have a statutory right to remove directors by way of resolution passed by simple majority, subject to the director’s right to attend the shareholders’ meeting in question and to make representations.

Conflicts of interest of directors

The area of directors’ conflicts of interest has been the subject of a number of judicial decisions over a number of years, and an extensive body of case law has developed around it. The key principles are, as mentioned, that a director should not place himself or herself in a position where his or her duty to the company conflicts with his or her own personal interests, and
that a director should not gain from his or her fiduciary position. Added to this common law is a host of statutory provisions setting out different checks and balances primarily aimed at the protection of shareholders and creditors.

III DISCLOSURE

i Financial reporting and accountability

Companies are required to disclose details of their accounts at their AGM and in their annual return, which is filed in and publicly available at the Companies Registration Office. Since May 2017, a long-standing non-filing exemption enjoyed by unlimited companies with a particular non-EU/EEA shareholding structure has been removed, by virtue of the Companies (Accounting) Act 2017. Under the Companies Act, related party transactions that are material and have not been concluded under normal market conditions are required to be disclosed in the notes to the company’s accounts.

Company accounts must be audited by a qualified auditor, and the auditor’s report is distributed to shareholders and included in the annual return.

Companies with securities admitted to trading on a regulated market (in Ireland, this is Euronext Dublin) must disclose financial and other information to shareholders on a regular basis. The Transparency Regulations 2007 (as amended, most recently twice in 2015 and once in 2017) (Transparency Regulations) and related rules issued by the Central Bank of Ireland (which implement the EU Transparency Directive7) require the publication of annual and half-yearly financial reports. They also require companies to publish information that is disclosed to them by persons who have acquired or disposed of voting rights in the company.

The Companies Act provides a definition of a traded company for the first time in Irish law. A traded company includes a public limited company that has shares or debentures admitted to trading on a regulated market in an EEA state.

Traded companies are required to include, in the directors’ report, a corporate governance statement in respect of the financial year concerned. This statement must be included as a specific section of the directors’ report and must include the following information:

a a reference to the corporate governance code to which the company is subject, including all relevant information concerning corporate governance practices applied in respect of the company, which are additional to any statutory requirement, and details of where the text of the relevant corporate governance code is publicly available. If the company departs from the corporate governance code, details of this, and of the reasons for the departure, should be included;

b a description of the main features of the company’s internal control and risk management systems in relation to the financial reporting process;

c information already required by the European Communities (Takeover Bids (Directive 2004/25/EC)) Regulations 2006 relating to the company’s share and control structures (where the company is subject to this Directive);

d the operation of the shareholders’ meeting and its key powers, and a description of shareholders’ rights and how they can be exercised; and

e the composition and operation of the board and its committees.

7 Directive 2004/109/EC.
The company’s auditors, when preparing their report to the members to be read at the AGM, must establish that the corporate governance statement addresses the information required under the Companies Act, and provide an opinion on certain aspects of the report. Companies that comply with the CBI Requirements are also required to submit an annual compliance statement to the Central Bank of Ireland.

In June 2016, the European Union (Statutory Audits) Regulations 2016 (2016 Regulations) came into effect in Ireland. The 2016 Regulations give effect to the Statutory Audit Directive,8 which amended the original Statutory Audit Directive9 in various ways. The new regime was designed to enhance the independence of statutory auditors, and the quality and credibility of statutory audits, across the EEA.

Public listed companies are regarded as public interest entities (PIEs) for the purposes of the legislation, and the following provisions apply to them:

a. PIEs are obliged to rotate their auditor firm after a maximum of 10 years (from date of initial appointment);
b. there are tighter restrictions on the provision of non-audit services by auditors to PIEs;
c. the selection and appointment of the statutory auditors must adhere to specified procedures, which must be established by a PIE; and
d. there are detailed requirements regarding the establishment of audit committees in PIEs; however, new legislation has introduced certain exemptions from this obligation in small and medium-sized PIEs. These are discussed in further detail below.

ii Audit committees

The requirement for PIEs to establish an audit committee has been in place in Ireland since the European Communities (Statutory Audits) (Directive 2006/43/EC) Regulations 2010 (2010 Regulations) were published, giving effect to Directive 2006/43/EC on statutory audits.

Under the Companies Act, PIEs are defined as companies whose transferable securities are admitted to trading on a regulated market of any Member State; credit institutions; and insurance and reinsurance undertakings. The Companies Act provides that the directors of a PIE, with a number of exceptions, must establish an audit committee. The majority of members of the audit committee must be non-executive directors, who must have the requisite level of independence to enable them to contribute effectively to the committee’s functions. Irish law provides for an exemption to this obligation for PIEs that are small or medium-sized enterprises and companies listed on an EU regulated market (such as Euronext Dublin) with an average market capitalisation of less than €100 million for the previous three years.10

The responsibilities of the audit committee include:

a. informing the directors of the entity of the outcome of the statutory audit and explaining how the statutory audit contributed to the integrity of the financial reporting;
b. monitoring the financial reporting process;
c. monitoring the effectiveness of the company’s systems of internal control, internal audit and risk management; and

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8 Directive 2014/56/EU.
9 Directive 2006/43/EC.
10 This latter exemption does not apply to any captive insurance or reinsurance undertaking owned by a credit institution or with securities admitted to trading on a regulated market.
d monitoring the statutory audit of the annual and consolidated accounts.

The Companies Act contains provisions on many aspects of auditing that were carried over from the 2016 Regulations (and the 2010 Regulations before that), including:

- the approval of statutory auditors and audit firms;
- the educational standards of auditors;
- the establishment of a public register of auditors;
- the independence of auditors; and
- arrangements regarding third-country auditors.

A notable provision is that statutory auditors or audit firms may only be dismissed where there are proper grounds. Divergences of opinions on accounting treatments or audit procedures are not considered to be proper grounds for dismissal.

Under the Companies Act, large private companies that meet certain financial thresholds are required to have an audit committee on a comply or explain basis.

Listed companies following the UK Corporate Governance Code must additionally comply with the relevant provisions relating to audit committees, or explain why not.

Financial institutions and insurance undertakings must also comply with the relevant provisions on audit committees contained within the CBI Requirements, which operate on a statutory basis rather than a comply or explain basis.

iii Market disclosure

Listed companies must also comply with certain disclosure requirements contained in the Listing Rules, the EU Market Abuse Regulation (MAR) (as implemented in July 2016) and the Takeover Rules. Pursuant to MAR, Irish listed companies are required to release inside information to the market without delay (except where limited circumstances exist for deferring such information). Under the MAR, companies are required to put systems in place to ensure both their initial and their ongoing compliance with market abuse legislation. The MAR also introduces more significant record-keeping and reporting obligations where market disclosure has been delayed.

iv Disclosure of share interests

Under the Companies Act, directors, shadow directors and company secretaries must disclose to the company, in writing, interests they have in shares and debentures in the company, its subsidiary or holding company. Specifically, they must disclose the subsistence of their interest, the number of shares of each class and the amount of debentures of each class of the company, subsidiary or holding company. Under the Companies Act, the threshold at and above which that interest in a public company must be disclosed has been reduced to 3 per cent. The Act also provides that certain transactions and arrangements between directors and persons connected to them, and the company or its subsidiary, must be disclosed in the company's accounts.

In addition, persons discharging managerial responsibilities are obliged to disclose their interests and that of close family members in shares of companies whose shares are admitted to trading on a regulated market, under the MAR. Under the Transparency Regulations and related Central Bank Transparency Rules, major shareholders in issuers whose shares are admitted to trading on a regulated market in Ireland must disclose the voting rights held by them.
v Beneficial ownership

In 2016, the European Union (Anti-Money Laundering: Beneficial Ownership of Corporate Entities) Regulations 2016 came into operation. All corporate and other legal entities, but excluding companies listed on an EU regulated market, must comply with the Regulations. The Regulations require entities incorporated in the state to hold adequate, accurate and current information on the controllers and beneficial owners of more than 25 per cent of their entity.

Listed companies are not required to comply with the Regulations, as they are subject to disclosure requirements that are consistent with this law.

vi Disclosure of non-financial and diversity information

In July 2017, EU Directive 2014/95/EU on disclosure of non-financial and diversity information by certain large undertakings and groups was implemented in Ireland by means of the European Union (Disclosure of non-financial and diversity information by certain large undertakings and groups) Regulations 2017.

The Directive amended the Fourth and Seventh Accounting Directives on Annual and Consolidated Accounts11 by including new provisions on the disclosure of non-financial information, and new provisions on boardroom diversity.

The Regulations provide for two separate reporting requirements as follows:

a the directors of companies that are categorised as public interest entities and large, and that have more than 500 employees, and companies that are ineligible entities (companies that do not qualify for audit exemptions) must include a statement containing specific non-financial information in the company’s directors’ report. The non-financial statement must include information on environmental, social and employee matters, respect for human rights and bribery and corruption. Where a company does not have policies in any of these areas, it must explain why not; and

b large traded companies must include a diversity report in their company’s corporate governance statement. The report must include a description of the company’s diversity policy, and must contain information on the age, gender or educational and professional backgrounds of board members. Where a company does not have a diversity policy, it must explain why not.

The Regulations came into effect in August 2017 and apply to financial years beginning on or after 1 August 2017.

IV CORPORATE RESPONSIBILITY

There are no specific legal requirements or guidance in Ireland regulating corporate social responsibility. However, Irish companies are increasingly aware of corporate social responsibility issues. Most public listed companies acknowledge the need for and benefits of providing information to shareholders and the public on corporate social responsibility.

Legislation exists in Ireland that is designed to protect whistle-blowers. The Protected Disclosures Act 2014 aims to ensure workers are protected from reprisal where, in good faith and in the public interest, they disclose information relating to wrongdoing in the workplace.

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11 Directives 78/660/EEC and 83/349/EEC, respectively.
Employers are required to publish and put in place policies and procedures to deal with whistle-blowing. The Act protects workers in all sectors. For employees who believe that they have been unfairly treated as a result of disclosing company malpractice, there are also remedies under employment law, and in particular unfair dismissals legislation.

V SHAREHOLDERS

Recent years have seen a move internationally towards enhanced rights for shareholders. A significant development in shareholders rights, and one that Ireland shares with its EU neighbours, is the Shareholders Rights Directive,12 implemented in Ireland by the Shareholders’ Rights (Directive 2007/36/EC) Regulations 2009.

An amending Directive, (EU) 2017/828 amending Directive 2007/36/EC, which introduces new provisions in the Shareholder Rights Directive aimed at improving engagement with shareholders, was agreed in May 2017. The basic provisions of the Directive must be implemented into domestic law in Member States by 10 June 2019. Among the provisions of note are the right for companies to be able to identify their shareholders, the transmission of information between companies and shareholders, and provisions relating to remuneration policies of directors. These new provisions substantially reflect current practice in the Irish market, such practice having developed as a result of Irish listed companies that are also listed on the London Stock Exchange opting to comply with the position in the UK on a number of these issues.

i Shareholder rights and powers

Equality of voting rights

Every registered shareholder entitled to attend meetings of an Irish company is also entitled to vote on any shareholder matter, unless the company's constitution or articles of association or the terms of issue of the shares dictate otherwise. Many private companies in Ireland have only one class of ordinary shares in issue, with each share carrying equal rights in relation to voting and dividends, and on a winding-up. However, it is also quite common for an Irish company to introduce different classes of shares, for example voting and non-voting, or a share class that might attach weighted voting rights either generally or on a particular matter.

Rights accrue only to those persons who are registered in the register of members of the company and not to beneficial holders. There is some suggestion that in future direct and indirect holders of shares may be given equal rights, but this has yet to materialise in Ireland.

Other rights of shareholders

Shareholders in Irish companies enjoy all the usual rights associated with membership of a company, for example the right to receive copies of financial information, pre-emption rights and the right to wind up the company.

Shareholders of some Irish listed companies also enjoy certain additional and enhanced rights. For example, under the Companies Act, a general meeting can be called by members representing only 5 per cent of the voting capital of a company listed on Euronext Dublin (10 per cent for companies listed on the smaller Euronext Growth). In addition, members holding 3 per cent of the issued capital of a company listed on Euronext Dublin, representing

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12 Directive 2007/36/EC.
at least 3 per cent of its total voting rights, have the new right to put items on the agenda and table draft resolutions to be adopted at AGMs. Listed companies are allowed to offer members participation in and voting at general meetings by electronic means (although there is likely to be debate about exactly what this means) and will also be allowed to offer the possibility of voting by correspondence in advance. However, neither of the latter provisions is mandatory, and companies are merely permitted to provide these facilities.

**Decisions reserved to shareholders**

Generally, shareholders do not have a role in deciding or approving operational matters, regardless of size or materiality. An exception to this principle arises under the Listing Rules in relation to large transactions.

Under Irish law, there is a list of structural matters that are reserved to be decided by the shareholders by ordinary resolution (or a simple majority) of those who vote. Examples include the consolidation or subdivision of shares, the payment of compensation to former directors and the purchase ‘on market’ of the company’s own shares. Certain other actions are also reserved but require a special resolution (or 75 per cent of the votes). Examples of these matters include the alteration of the memorandum and articles of association of the company, the giving of financial assistance in connection with the purchase of the company’s own shares and the reduction of share capital.

**Rights of dissenting shareholders**

A number of remedies are open to disgruntled shareholders under Irish law. Perhaps the remedy that is most often talked about is the statutory right of minority shareholders to seek potentially far-reaching redress on the grounds of majority shareholder oppression, where shareholders can also apply to court to have a forced sale of the company or to have the company wound up on just and equitable grounds. Here it must be shown that the act or measure complained of has as its primary motive the advancement of the interests of the majority shareholders as opposed to the interests of the company as a whole. Mere dissent by a minority is insufficient to support a claim for redress. The Companies Act permits the courts to award a wide range of remedies, including forced sale, winding up and/or compensation for any loss or damage as a result of oppressive conduct.

**Shareholders’ duties and responsibilities**

**Controlling shareholders**

The Irish company is legally separate from its shareholders, even its controlling shareholder. The powers, rights, duties and responsibilities of the controlling shareholder, like any other shareholder, will be determined by the terms of issue of the shares, the constitution or articles of association of the company and any applicable shareholders’ agreement. However, the actions of a controlling shareholder should always be measured in the context of the various remedies open to minority shareholders.

**Institutional investors**

Corporate governance is currently a key concern for institutional investors, along with so many other interested parties. The UK Stewardship Code sets out good practice for institutional investors when engaging with UK listed companies and will be relevant to how
those institutional investors engage with Irish listed companies. Although there are currently no plans to introduce a similar code in Ireland, it is likely that Irish institutional investors will view this code as a standard of market practice in the area.

### iii Shareholder activism and shareholder remedies

Shareholder activism is relatively underdeveloped in Ireland. However, there are a number of signs of change.

Shareholders can bring proceedings where the directors are exercising their powers or conducting the affairs of the company in a manner oppressive to the shareholders or in disregard of their interests. As indicated above, courts can grant relief where it can be proved by a member that the affairs of the company have been conducted in an oppressive manner against him or her or any of the members of the company, including members who are directors themselves.

Aggrieved members may also take a derivative action (i.e., an action in the name of the company itself) where the company has been wronged, with one shareholder representing the body of shareholders. This typically arises in circumstances where the directors of a company are responsible for taking actions in the company’s name and refuse to take that action. Derivative actions will be permitted where an ultra vires or illegal act has been perpetrated against the company, where more than a bare majority is required to ratify the wrong in question, where members’ personal rights have been infringed or where fraud has been committed on a minority of members.

### iv Takeover defences

Certain takeover defence mechanisms may risk conflicting with the Irish Takeover Panel Rules. As a rule, in any defensive action it is imperative that boards ensure that their actions do not amount to frustrating actions, and that a level playing field is afforded to all potential bidders.

A company that has received a bid is not prevented from seeking alternative bids elsewhere (although this may possibly be subject to any inter-party agreement). The offer of the third party may be announced at any time except where the Takeover Panel directs that the third-party white knight make its intentions clear. In general terms, the directors must provide equality of information to all parties.

### v Contact with shareholders

*Mandatory and best practice reporting to all shareholders*

Under the Transparency Regulations, companies whose securities are admitted to trading on a regulated market are required to publish annual and half-yearly financial reports. The annual report contains audited financial statements, a management report and responsibility statements. The half-yearly report contains a condensed set of financial statements, an interim management report and responsibility statements. Responsibility statements contain certain confirmations, including that the financial statements represent a fair and true view of the financial status of the company.

Members also enjoy the right to access certain information from the company, including the company memorandum and articles of association, resolutions and minutes of general meetings, company registers and the annual financial statements, directors’ reports and auditors’ reports.
Listed companies follow the Corporate Governance Code, which sets out the best practice guidelines for corporate governance. Listed companies must comply with the Code or explain any deviations to shareholders. In addition, the Irish Corporate Governance Annex to the Listing Rules encourages Irish listed companies to provide more detailed explanations of their actions, and in particular any deviation from certain aspects of the Corporate Governance Code to promote dialogue with shareholders.

Twenty-one clear days’ notice must be given for an AGM. Extraordinary general meetings (EGMs) of listed companies may be held on 14 days’ notice, but only where the company offers all members the facility to vote by electronic means at general meetings and the company has passed a special resolution approving the holding of EGMs on 14 days’ notice, at its immediately preceding AGM or at a general meeting held since that meeting. However, if it is proposed to pass a special resolution at the EGM of the listed company, then 21 days’ notice must be given.

Notwithstanding the minimum statutory period, for listed companies, 20 business days is the minimum period recommended under the Corporate Governance Code.

VI OUTLOOK

i New legislation in the pipeline

New prospectus and public offer regime

A phased implementation of the new EU Prospectus Regulation was commenced in July 2017 and shall extend to July 2019. While certain of the changes that the Regulation will introduce to Irish prospectus law came into effect over the course of 2018 with the remainder due to come in effect in July 2019, the Regulation technically entered into force on 20 July 2017, and from that date, companies admitted to trading on Euronext Dublin (or on any other EU regulated market) can issue and admit to trading up to a maximum of less than 20 per cent (up from the existing maximum of less than 10 per cent) of their share capital or debentures that are already admitted to trading (calculated over 12 months), without being obliged to publish a prospectus.

In addition, from 20 July 2017 there has been an exemption from having to publish a prospectus where the company wishes to admit to trading on the regulated market shares resulting from conversion or exchange of other securities or rights where those shares are of the same class as shares already admitted to trading on the same regulated market, and provided that (unless some exceptions apply) the resulting shares are less than 20 per cent of the shares of the same class already admitted to trading on that market.

Annual returns and financial statements

The Companies (Amendment) Bill 2019 proposes to amend the provisions of the Companies Act by extending the time period permitted for the filing of annual returns from 28 days to 56 days from the date of the company’s annual return. The Bill is expected to be passed into law in early 2019. It is anticipated that, on or soon after the enactment of the Bill, the not yet commenced provisions of the Companies (Statutory Audits) Act 2018, including those relating to the introduction of a single step approach for companies when filing their annual return and financial statements, will also be commenced.
Beneficial ownership central register
As outlined earlier, Article 30 of the Fourth EU Anti-Money Laundering Directive (as amended by the Fifth Anti-Money Laundering Directive) requires all EU Member States to implement provisions around beneficial ownership information for corporate and legal entities. The first element of this requirement is already in place, as outlined previously. The second element of this requirement is that corporate and legal entities will be required to file information about their beneficial owners with a central beneficial ownership register. The central register is in the process of being established in Ireland, and it will be maintained by the Companies Registration Office. The implementing legislation is expected to be passed into law during the first quarter of 2019, following which it is anticipated that there will be a grace period of approximately six months for the first filing of information once the register is operational.

Brexit
At the time of writing, the status of the UK’s exit from the European Union remains unclear. A capital markets consequence is that, subject to the continuation of the current system over any transition period, shares of Irish listed companies will no longer be capable of being settled through the London-based CREST system. In the absence of a continuation of CREST post-Brexit, an alternative settlement arrangement to CREST will need to be made available and approved under the EU Central Securities Depositories Regulation.
I OVERVIEW OF GOVERNANCE REGIME

i Sources of law and enforcement

Companies in Japan are generally regulated by the Companies Act. Further, listed companies in Japan are also regulated by the Financial Instruments and Exchange Law (FIEL) and the Securities Listing Regulations published by each securities exchange (SLRs). As the securities exchanges, in publishing their SLRs, generally follow the SLRs published by the Tokyo Stock Exchange (TSE), which is the largest securities exchange in Japan, the information we provide hereafter focuses on the SLRs published by the TSE, and references to ‘SLRs’ are to the SLRs published by the TSE.

In the event that a company violates the Companies Act, depending on the specific provision that is violated, shareholders or creditors of a company are generally entitled to bring a lawsuit against the company. The Financial Services Agency of Japan is responsible for enforcing the FIEL and, depending on the specific provision that is violated, may levy monetary fines, prison sentences, or even both, in connection with certain violations thereof. SLRs are enforced by the specific securities exchange that published the applicable SLR. Violations of the SLRs generally lead to the securities exchange requiring that company to submit an improvement plan. In extreme cases, securities exchanges may even delist the shares of the company.

ii Nature and recent developments in the corporate governance regime

The Companies Act, which has been in effect since 2006, allows a company some flexibility with its governance organisation, such as whether to have a board of directors and whether to have a corporate auditor. Revisions to the SLRs on 30 December 2009, however, require a listed company to have one or more independent directors or corporate auditors (i.e., outside directors or corporate auditors (as defined below) who are not likely to have a conflict of interest with the company’s shareholders). If an independent director or corporate auditor has business or other relationships with the company (e.g., if the director or corporate auditor is a main business partner, consultant or a major shareholder of the company), this relationship must be disclosed, and the reasons the person was appointed as an independent director or corporate auditor must also be provided in the company’s corporate governance reports.

1 Mitsuhiro Harada and Tatsuya Nakayama are partners and Yohei Omata is a senior associate at Nishimura & Asahi.
3 Act No. 25 of 13 April 1948.
under the SLRs. Further, the Companies Act reform bill was enacted on 1 May 2015, and
the Reform Act of 2015 states that if a large public company that is required under the FIEL
to file a securities report does not have an outside director, it must explain the reason for this
in its business report and upon its annual shareholders’ meeting; in addition, the Companies
Act reform bill which passed the Diet on December 2019, but has not yet been put in
force, requires a large public company that is required under the FIEL to file a securities
report to have one or more outside directors. On 5 February 2014, the TSE announced
a revision to the SLRs requesting that listed companies make efforts to elect at least one
independent director because, in practice, most listed companies had elected an independent
corporate auditor. In addition, the TSE released Japan’s Corporate Governance Code (Code)
on 1 June 2015 which was most recently revised on 1 June 2018.5 The Code, which is
applicable to all companies listed on securities exchanges in Japan, establishes fundamental
principles for effective corporate governance, including a structure for transparent, fair,
timely and decisive decision-making by companies, which pay due attention to the needs and
perspectives of shareholders and also customers, employees and local communities. The Code
stipulates that listed companies should appoint at least two independent directors, and that
listed companies should examine whether the purpose of cross-shareholdings is appropriate,
and whether the benefits and risks from each holding cover the company’s cost of capital.

In Japan, roughly speaking, there were two types of governance systems prior to
enactment of the Reform Act of 2015: a company with a corporate auditor and a company with
committees.6 In a company with a corporate auditor, the corporate auditor is an organisation
that audits the directors’ execution of their duties. This type of organisation is the primary
type of company in Japan. On the other hand, in a company with committees (without a
corporate auditor), three stipulated committees perform auditing and monitoring functions:
a nominating committee that decides on the agenda of nominating or dismissing directors at
shareholders’ meetings; an audit committee that audits the execution of duties of executive
officers and directors; and a compensation committee that determines compensation for each
executive officer and director.

A majority of each of these committees must consist of outside directors. In a company
with committees, because a board may delegate substantial parts of its decision-making
authority over the management of the company to the executive officers, the board is expected
to monitor the execution of the executive officers’ duties rather than to make decisions
(although a director can serve concurrently as an executive officer). This type of organisation
was first introduced in 2003 and is used only by a limited number of large companies in
Japan.

The Reform Act of 2015 further introduced another type of governance structure –
a company with an audit committee – anticipating that this structure makes it easier for
Japanese companies to select a monitoring model involving outside directors. A reduction of
costs for selecting the monitoring model is achieved by decreasing the number of outsiders
(i.e., outside directors and outside corporate auditors). A company with an audit committee

4 This Companies Act reform bill will be put into force on the day designated by cabinet order within one
and a half years from the time of promulgation (i.e. December 11, 2019).
6 Following enactment of the Reform Act of 2015, companies with committees are now called companies
with nominating committee, etc., but the meaning of the term is unchanged. As a matter of convenience,
we hereinafter refer to this type of company as a ‘company with committees’.

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is not required to possess a nominating committee or compensation committee. The audit committee must have more than three directors as members, and the majority of them must be outside directors.

The number of companies with an audit committee has reached more than 1,000, which is almost equal to one-third of the total number of listed companies in Japan. This is because, as previously discussed, being a company with an audit committee makes it possible for a listed company with a board of corporate auditors to decrease the number of outsiders. While the Code stipulates that a listed company should appoint at least two independent directors, if a listed company has a board of corporate auditors, half or more of the corporate auditors need to be outside corporate auditors under the Companies Act. If a company with a board of corporate auditors transforms into a company with an audit committee, such requirement to retain outside corporate auditors would not be applicable.

II CORPORATE LEADERSHIP

i Board structure and practices

Structure and composition of the board

Japanese companies generally use a one-tier board structure. Under the Companies Act, although a company may choose not to have a board of directors, the typical form of management structure is a company with a board of directors, where the board has decision-making authority. In a company without a board of directors, while there is no board, unless otherwise provided in the company’s articles of incorporation (articles), a majority of the directors will decide business matters on behalf of the company. As compared with a company with a board of directors, however, shareholders of a company without a board have broader decision-making authority, such as the ability to approve certain competitive activities or to approve activities that result in conflicts of interest of directors.

A company with a board of directors is required to have three or more directors. A company without a board, on the other hand, is required to have only one or more directors. A company with committees must also have a board, and therefore it is required to have three or more directors. A company with an audit committee is required to have a board as well, and therefore to have three or more directors. In addition, in a company with an audit committee, the audit committee must have more than three directors as members, and the majority of them must be outside directors. In Japan, no director is required to be a representative of the employees of the company.

Legal responsibilities of the board

Except for a company with committees and a company with an audit committee, a company with a board of directors generally must have a corporate auditor. In a company with a corporate auditor and a board of directors, the board has decision-making authority over the management of the company, and representative directors and other executive directors are responsible for executing the company management decisions. The corporate auditor generally audits the execution of duties by directors, with a view to compliance with law.

In a company with committees, while the board may have decision-making authority over the management of the company, it usually delegates substantial portions of this authority to executive officers, and executive officers are responsible for executing the company management decisions. Accordingly, for example, executive officers may be delegated the authority to decide on the acquisition of important assets, incurrence of significant debt,
appointment of important employees and establishment of important organisational changes, while those are items that would be determined by a board of directors in a company with a corporate auditor. The board of a company with committees would then, inter alia, determine the agendas of shareholders’ meetings, approve competitive activities and activities that result in conflicts of interests of directors, and appoint committee members. The audit committee audits the execution of duties by directors with a view not only to compliance with the applicable laws, but also the appropriate performance of their duties.

In a company with an audit committee, the core role of the board of directors is to set the basic management policy, develop the internal control system, and supervise the execution of business by other directors, including representative directors and other executive directors. Although important business decisions, such as disposing of or acquiring important assets, are required to be made by the board of directors, its shareholders can, through the company’s articles, enable the board to delegate these decisions to individual directors, such as representative directors or other executive directors. In addition, if the majority of the board is held by outside directors, the board can delegate these decisions to individual directors, such as representative directors or other executive directors.

**Delegation of responsibilities**

In a company with a corporate auditor and a board of directors (which is typical of Japanese companies), the board often delegates decisions on certain matters regarding day-to-day operations to individual directors, such as representative directors or other executive directors. However, the board may not delegate certain important company matters to individual directors, including:

- disposing of or acquiring important assets;
- incurring significant debts;
- electing or dismissing important employees, including managers;
- issuing shares at a fair price; and
- approving audited financial statements.

In a company with committees, the nominating, audit and compensation committees each have their own authority under the Companies Act and cannot further delegate substantial parts of their responsibilities. Apart from the committees’ responsibilities, the board has sole decision-making authority over the management of the company with respect to certain matters, which include basic management policy; matters necessary for the execution of the audit committee’s duties; and if there are two or more executive officers, matters relating to the interrelationship between executive officers.

Similarly, in a company with an audit committee, the audit committee has its own authority and cannot further delegate a substantial part of its responsibility. Apart from the audit committee’s responsibility, the board has sole decision-making authority over the management of the company with respect to certain matters, which include basic management policy; and matters necessary for the execution of the audit committee’s duties.

A board of directors in a company with committees often delegates decision-making authority over the management of the company to the executive officers (as described above). The board may not, however, delegate certain important matters (in addition to the above-mentioned matters) to executive officers (or to individual directors, because each individual director who does not double as an executive officer in a company with committees generally does not have decision-making authority), including:
a approval of share transfers (if the company is a closed company);
b holding of shareholders’ meetings;
c appointment or removal of committee members;
d election or dismissal of executive officers; and
e determining the contents of agreements for mergers, demergers or share exchanges.

In a company with an audit committee, although important business decisions such as disposing of or acquiring important assets are required to be made by the board of directors, its shareholders can, through the articles, enable the board to delegate these decisions to individual directors, such as representative directors or other executive directors. If the majority of the board is held by outside directors, the board can also delegate these decisions to individual directors, such as representative directors or other executive directors.

In Japan, normally the board appoints the CEO or its equivalent from among its representative directors (in the cases of a company with a corporate auditor and a board of directors, and a company with an audit committee) or representative executive officers (in the case of a company with committees). Generally, the CEO will chair the board meeting, and will perform the role of chair of the board in this sense.

**Remuneration of directors and executive officers**

In a company with a corporate auditor and a board of directors, the aggregate amount of remuneration of all directors is determined at a shareholders’ meeting (if not provided in the articles), and the board determines the remuneration of each director within the parameters of this aggregate amount; the board can delegate this authority to an individual director, typically the CEO. The same would apply to a company with an audit committee. In addition, in a company with an audit committee, the audit committee is given the power to express its view on the election, dismissal, resignation and compensation of other directors at the shareholders’ meeting so that the shareholders can make an informed decision on these matters. The Companies Act reform bill, which passed the Diet on December 2019, but has not yet been put in force, requires (1) a large public company that is required under the FIEL to file a securities report; and (2) a company with an audit committee to establish company’s policies for determination of the remuneration for each director, except for in the case where the remuneration for each director is determined by a shareholders’ meeting or the articles.

On the other hand, in a company with committees, the compensation committee determines the remuneration of each director and executive officer in accordance with the remuneration policy prescribed by the committee (therefore, shareholders’ approval is not required).

A public company (i.e., a company, typically listed, whose articles do not require, as a feature of all or part of its shares, the company’s approval for any transfer of those shares, whether it is a company with a corporate auditor, a company with an audit committee or a company with committees) must disclose the aggregate remuneration of all of its directors, corporate auditors and executive officers to its shareholders in its business report. In addition, a listed company must disclose the following information in its securities report: (1) the

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7 Currently, in order to improve the level of disclosure regarding the remuneration of directors, corporate auditors and executive officers, requiring a public company to disclose the following items in its business report is being discussed: (1) an item regarding a policy for determining the remuneration, (2) an item regarding a resolution of shareholders’ meeting for the remuneration, (3) an item regarding a delegation of
amount of remuneration and a breakdown by type of payment (e.g., fixed compensation, performance-based compensation or retirement payment) for each director, corporate auditor and executive officer if his or her remuneration for the relevant fiscal year is ¥100 million or more (out of 2,411 companies listed as of 10 July 2019, there were 570 directors, corporate auditors or executive officers who received ¥100 million or more as remuneration for the fiscal year ending March 2019); (2) an explanation of the company’s policies for determining an amount of or calculation method for remuneration of directors, corporate auditors and executive officers; as for a company that pays directors, corporate auditors or executive officers performance-based compensation, an explanation of the company’s policies on the payment ratio of performance-based compensation and non performance-based compensation (if any), indicators for performance-based compensation and reasons why the company chose such indicators, how the amount of performance-based compensation was determined, and the targets and performance for such indicators in the most recent fiscal year; (3) the name of a person or organisation who has the authority to determine an amount of or calculation method for remuneration of directors, corporate auditors and executive officers, an explanation of such authority including its range of discretion; and (4) as for a company with a committee, including an optional committee, which involves the establishment of company’s policies for determination of an amount of or calculation method for remuneration of directors, corporate auditors or executive officers, an outline of procedures for involvement of such committee and activities of the board and such committee in the course of determination of an amount of remuneration of directors, corporate auditors and executive officers in a most recent fiscal year.

The Code stipulates that, in addition to making information disclosure in compliance with relevant laws and regulations, listed companies should disclose and proactively provide information regarding their boards’ policies and procedures for determining the remuneration of senior management and directors to enhance transparency and fairness in decision-making and ensure effective corporate governance.

**Board and company practice in takeovers**

The typical anti-takeover measure listed companies in Japan use is a ‘precaution-type anti-takeover measure’, whereby a company announces a takeover process rule but does not issue any securities at first. Although there are many variations of this measure, generally a company announces in advance a certain takeover process rule to the effect that a takeover bidder must provide sufficient information to a board of directors about the bidder and the terms of its bid before the beginning of its takeover, and the bidder refrains from purchasing the shares of the company unless the board of the company completes its analysis of the terms of the bid (but the analysis by the board must be completed within a certain period, such as 60 days). If these procedures are respected by the bidder, the board will not implement anti-takeover measures, but where the board decides that the value of the company would be damaged, or maximising value would be difficult under the takeover (including if the bidder

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8 The Code stipulates that anti-takeover measures must not have any objective associated with entrenchment of the management or the board.
does not comply with the procedures), usually based on analysis by a third-party committee, certain anti-takeover measures may be implemented, typically the issuance of share purchase warrants free of charge to all shareholders that cannot be exercised by the bidder.

In Japan, the Bull-Dog Sauce case\(^9\) was the first case where actual share purchase warrants were issued to shareholders as an anti-takeover measure. In this case, the Supreme Court found that the decision regarding whether control by a specific shareholder would harm the value of the company or damage the common interests of shareholders should be ultimately determined by the shareholders who hold its corporate value, and that if, at a shareholders’ meeting, the shareholders decide that the takeover would harm the value of the company or damage the common interests of the shareholders, that decision should be respected. In this case, because the issuance of share purchase warrants was approved by more than 80 per cent of the voting rights, the Supreme Court found that the issuance was valid.

Since this case, we have seen fewer attempts at hostile acquisition.\(^{10}\) In addition, a tender offer regulation under the FIEL was amended in 2007 to the effect that the offeror must disclose more information prior to the tender offer, and that the target company has the right to issue a questionnaire to the offeror. As a result, the total number of listed companies that have adopted anti-takeover measures has decreased for 11 consecutive years (from 570 companies at the end of July 2008 to 327 companies at the end of November 2019).

\[\text{ii Directors}^{}\]

*Appointment, nomination, term of office*

Directors are elected by a resolution at a shareholders’ meeting. In a company with a corporate auditor and a board of directors, the board generally nominates directors to two-year terms of office (maximum; however, in a closed company, the term of office may be extended until the conclusion of the annual shareholders’ meeting for the last fiscal year, which ends within 10 years from the time of its election). On the other hand, in a company with committees, the nominating committee nominates directors with one-year terms of office (maximum). Further, in a company with an audit committee, a director who is a member of the audit committee must be nominated separately from the other directors, and the statutory maximum term of office for a director who is a member of an audit committee is two years, while for other directors it is one year.

Directors can be dismissed at any time by a resolution at a shareholders’ meeting. Directors can seek damages for dismissal from the company if they are dismissed without justifiable grounds.

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\(^9\) Supreme Court, 7 August 2007.

\(^{10}\) For example, in November 2012, PGM Holdings commenced a hostile takeover bid against Accordia Golf, but the tender offer failed to acquire 20 per cent of the shares. In March 2013, Cerberus Capital Management, LP (Cerberus) commenced a hostile takeover bid against Seibu Holdings Inc., but Cerberus only acquired 3.26 per cent (originally it held 32.22 per cent and ended up holding 35.48 per cent) through the tender offer. In December 2014, Prospect Co., Ltd commenced a hostile takeover bid against Yutaka Shoji Co., Ltd, but the tender offer failed to acquire 51 per cent of the shares. In April 2018, Japan Asia Group Limited commenced a hostile takeover bid against Sanyo Homes Corporation, but Japan Asia Group Limited only acquired 8.76 per cent (originally it held 4 per cent and ended up holding 12.76 per cent) through the tender offer. In July 2019, HIS Co., Ltd. commenced a hostile takeover bid against UNIZO Holdings Company, Limited, but HIS Co., Ltd. could not acquire any shares through the tender offer.
**Liability of directors**

Generally, directors must perform their duties with the duty of care of a prudent manager in compliance with all laws and regulations, and the articles and resolutions of shareholders’ meetings, in a loyal manner.

In addition to the foregoing, in Japan the business judgement rule is applied when considering whether a certain decision of a director complies with the director’s duty of care as a prudent manager to the company. Under the business judgement rule, even if a director has made a certain decision that has resulted in damage to the company, the director is, in principle, deemed to have complied with his or her duty of care of a prudent manager, unless the director made important and careless mistakes in the recognition of facts, or the process and content of the director’s decision-making is particularly unreasonable or improper as determined by a management expert. Nevertheless, the courts are not likely to apply the business judgement rule in cases where it can be shown that the director has a conflict of interest.

In the *Apamanshop* case, the business judgement rule was affirmed by the Supreme Court. In this case, Apamanshop Holdings bought out the subsidiary’s minority shareholders at a price per share higher than that set forth in the valuation report to make the subsidiary its wholly owned subsidiary. The Court cited the business judgement rule in finding that the directors of Apamanshop Holdings did not breach their duty of care, because a smooth purchase of the minority shareholders’ shares was beneficial in maintaining good relationships with Apamanshop’s member shops who were shareholders of Apamanshop, the corporate value of the subsidiary after the restructuring was expected to increase and the decision-making process employed by Apamanshop’s directors (i.e., the management committee convened to discuss the purchase and a legal opinion was obtained) was not found to be unreasonable.

**Role and involvement of outside directors**

Outside directors are defined under the Companies Act as directors who are not serving and who have not previously (generally for the past 10 years) served as executive directors, executive officers or employees (including managers) of the relevant company or any of its subsidiaries, its parent companies or its sibling companies. In a company with committees, a majority of the members of each committee must be outside directors, with each committee required to consist of at least three members. In a company with an audit committee, the audit committee must have more than three directors as members, and the majority of them must be outside directors. On the other hand, in a company with a corporate auditor and a board of directors, currently there are no such outside director requirements concerning board composition; however, the Companies Act reform bill, which passed the Diet on December 2019, but has not yet been put in force, requires a large public company that is required under the FIEL to file a securities report to have one or more outside directors.

The TSE requires listed companies to have one or more independent directors or corporate auditors (see Section I). Therefore, it is considered that, for example, persons who work for a company’s parent company or its business partner, or consultants who receive significant fees from a company, cannot be independent directors or corporate auditors of the company. Further, on 5 February 2014, after submission of the Companies Act reform bill (which states that if a large public company that is required under the FIEL to file a securities report has one or more outside directors, it must have one or more independent directors or corporate auditors), the Diet passed the bill, which was put into force on 15 July 2010.
report does not have an outside director, it must explain the reason why in its business report and at its annual shareholders’ meeting), the TSE announced a revision to the SLRs that requests that listed companies make efforts to elect at least one independent director (see Section I).

The Code stipulates that if the organisational structure of a company is either that of a company with a corporate auditor and a board of directors, or a company with an audit committee, and independent directors do not constitute a majority of the board, to strengthen the independence, objectivity and accountability of board functions in matters of nomination and remuneration of the senior management and directors, the company should seek appropriate involvement and advice from independent directors in the consideration of such important matters as nominations and remuneration by establishing independent advisory committees under the board, such as an optional nomination committee and an optional remuneration committee, to which independent directors make significant contributions.

Legal duties and best practice for outside directors
The legal duties of non executive directors including outside directors are generally the same as those of other directors or executive officers. Where provided for in a company’s articles, however, the company may contractually limit the liability (to the company) of its non executive directors, including outside directors who are not aware of the wrongdoing and not grossly negligent in performing their duties to the extent of the larger of both an amount determined in advance, within the range provided in the articles, and an amount equal to double his or her annual remuneration.

Outside directors generally should review the performance of management, conflict of interest issues, the process and propriety of management decisions and general compliance, and work to improve the corporate culture. Although other directors should take on these roles as well, outside directors are expected to do so more effectively because of their objective position.

Recently, many companies in Japan have organised third-party committees to audit or review conflict of interest issues, such as management buyout transactions, internal investigations and anti-takeover measures, and an outside director is often included as a member of the committee.

In a company with a corporate auditor and a board of directors, a company with committees or a company with an audit committee, if a director intends to carry out any transactions involving a conflict of interest, approval must be obtained at a board meeting in which that director may not participate. At the board meeting, the potentially conflicted director must disclose material facts about the transaction. After the transaction, the director must also report material facts about the transaction to the board without delay.

In addition, in a company with an audit committee, an ex ante approval by the audit committee of a self-dealing transaction between a director and the company has the effect of switching the burden of proof regarding the violation of a director’s duty from the director to the plaintiff shareholders.

iii Auditors
In a company with a corporate auditor, the corporate auditor audits the execution of the directors’ duties, including preparation of financial statements. If a company has a board of corporate auditors, the company is required to have three or more corporate auditors, and
half or more of them must be outside corporate auditors. To ensure the independence of the corporate auditor, its term of office must continue until the conclusion of the annual shareholders’ meeting for the last fiscal year, which ends within four years from the time of its election (in a closed company, the term of office may be extended until the conclusion of the annual shareholders’ meeting for the last fiscal year, which ends within 10 years from the time of its election). On the other hand, a company with committees does not have a corporate auditor. Instead, the audit committee, which consists of directors whose terms of office are one year (maximum), audits the execution of directors’ duties, including preparation of financial statements (see Section II). Similarly, a company with an audit committee does not have a corporate auditor. In a company with an audit committee, which consists of directors whose terms of office are two years (maximum), the audit committee is responsible for auditing the execution of directors’ duties, including preparation of financial statements.

In addition, a large company (i.e., a company with either stated capital in the balance sheet at the end of the most recent fiscal year of ¥500 million or more, or total liabilities as of the end of its most recent fiscal year of ¥20 billion or more) and a company with committees are required to have an accounting auditor, which must be either a certified public accountant or an audit firm. An accounting auditor’s terms of office must continue until the conclusion of the annual shareholders’ meeting for the last fiscal year, which ends within one year from the time of their election.

To ensure the independence of corporate auditors, the following are given the power to determine the contents of proposals regarding the election and dismissal of accounting auditors to be submitted to a shareholders’ meeting: a corporate auditor or a board of corporate auditors in a company with a corporate auditor, an audit committee in a company with committees and an audit committee in a company with an audit committee.

III DISCLOSURE

i Financial reporting and accountability

A representative director or representative executive officer must prepare a financial statement within three months from the end of each business year. A large company that is required to file a securities report under the FIEL (e.g., a listed company or a company with at least 1,000 shareholders as of the end of any fiscal year within the past five years is required to file a securities report) must prepare a consolidated financial statement under the Companies Act. However, the FIEL requires all listed companies to prepare a securities report that includes consolidated financial statements (unless they do not have any subsidiaries to be consolidated under the FIEL), as well as a quarterly report. In addition, a representative director or representative executive officer of a listed company must submit a confirmation letter as an attachment to its securities report or other reports, in which he or she confirms that the description of the report is written properly in accordance with the FIEL.

A company with a board of directors must attach financial statements and business reports to the convocation notice of its annual shareholders’ meeting. The company must also keep those documents at its head office for five years, beginning two weeks (one week, in the case of a company without a board) prior to the date of the shareholders’ meeting. Under the FIEL, a listed company is required to file its securities report within three months of the end of its fiscal year.
Communications with shareholders

Under the Companies Act, directors, corporate auditors and executive officers must sufficiently explain the specific issues related to the agenda of the shareholders’ meeting if an enquiry is made by a shareholder. In addition, to improve investor relations, Q&A sessions during shareholders’ meetings are now actively encouraged in Japan. Furthermore, Japanese listed companies often hold informal meetings with investors about financial statements and related issues.

IV CORPORATE RESPONSIBILITY

i Internal control

Boards of large companies must develop internal control systems that ensure that directors comply with the laws and the company articles, and that company operations are appropriate. On the other hand, there is no legal requirement for internal control systems for companies that are not categorised as large companies or companies that do not have a board of directors.

Additionally, in a company with committees, regardless of its size, the board must develop internal control systems that ensure that executive officers comply with the laws and the articles, and that company operations are appropriate. A listed company must file internal control reports that describe the systems that are in place to ensure that the financial reports of the company are properly made in compliance with the laws.

Similarly, in a company with an audit committee, regardless of its size, the board must develop internal control systems that ensure that directors comply with laws and the company articles, and that company operations are appropriate.

Specific contents of internal control systems may be decided at the discretion of companies. In its internal control rules, a company often provides general matters related to the control of information and documents; crisis management systems; necessary internal rules and organisations; and compliance programmes, etcetera.

Under the Whistle-blower Protection Act, the employer of a whistle-blower is prohibited from treating the whistle-blower in any disadvantageous manner, such as by demotion or reducing his or her salary, if this is in response to the employee’s whistle-blowing.

ii Corporate social responsibility to employees and wider society

In Japan, a company is required to hire a certain number of persons with a disability and to take measures to continue to employ elderly persons under affirmative action-related laws. Activities related to corporate social responsibility by some companies involve actions to be taken in the interests of their stakeholders, such as preserving the environment, supporting volunteer work and creating jobs, although these are not generally required by law.

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12 The Code stipulates that listed companies should, proactively and to the extent reasonable, respond to requests from shareholders to engage in dialogue so as to support sustainable growth and increase corporate value over the mid to long term, and that the board should establish, approve and disclose policies concerning the measures and organisational structures aimed at promoting constructive dialogue with shareholders.

13 The Code stipulates that as a part of establishing a framework for whistle-blowing, companies should establish a point of contact that is independent of the management, and that internal rules should be established to ensure the confidentiality of the information provider and prohibit any disadvantageous treatment.
V SHAREHOLDERS

i Shareholder rights and powers

Voting rights
In general, a company must treat its shareholders equally depending on the class and number of shares owned, and therefore each voting share has the same voting right. The Companies Act does, however, allow for the following exceptions: certain minority shareholders’ rights, such as rights to propose an agenda for a shareholders’ meeting, to inspect accounting books and to apply to a court for dissolution of the company; and different treatment for each shareholder in closed companies in terms of rights to dividends or distribution of residual assets, or voting rights at shareholders’ meetings pursuant to the articles.

In a company with a board of directors, matters provided for in the company’s articles and the Companies Act may be resolved at a shareholders’ meeting. In the sense that each director must observe resolutions passed at shareholders’ meetings, shareholders have an influence on the board.

Under the Companies Act, shareholders’ approval is required for certain matters, including the following:

a amending the articles;

b mergers, corporate demergers, statutory share exchanges, statutory share transfers, assignment of business and reduction of stated capital;

c election or dismissal of directors and corporate auditors; and

d decisions regarding dividends of surplus (if a company has an accounting auditor and a board of corporate auditors or committees, however, and the term of office of its directors is no more than one year, the authority to determine the distribution of dividends of surplus can be delegated to the board by the articles).

Rights of dissenting shareholders
Shareholders who object to the proposed agenda specifically listed under the Companies Act, such as certain amendments to the articles and certain mergers and acquisitions, may demand that the company purchase their shares at a fair price. This price will be determined through negotiation between the parties (i.e., the company and the dissenting shareholder) or by court decision. If a demand is made and the parties are able to come to an agreement on the share price, the company must make the payment to the dissenting shareholder within 60 days of the effective date of the transaction contemplated in the proposed agenda to which the dissenting shareholder objected. If the parties are unable to reach an agreement with regards to the share price within 30 days of the effective date, either the dissenting shareholder or the company may file a petition to a court for a determination of a fair price within 30 days of the expiration of that initial 30-day period.

In the ‘Tecmo’ case,14 the Supreme Court presented a framework for determining a fair price under appraisal proceedings in cases where a joint share transfer (where two or more companies form a new holding company under the Companies Act) creates synergies. In this decision, the court found that:

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14 Supreme Court, 29 February 2012.
a fair price should, in general, be the value that the share should have had on the date on which the shareholder made a demand to the company for the repurchase of the share, on the assumption that the share transfer ratio designated in the share transfer plan is fair; and

if a share transfer comes into effect through procedures that are generally recognised as fair, the share transfer ratio should be seen as fair unless special circumstances existed that hindered the shareholders’ ability to make reasonable decisions in the shareholders’ meeting.

ii Shareholders’ duties and responsibilities

Major shareholders’ duties and practice

Under the Companies Act, shareholders do not owe duties to the company other than paying the required share capital contribution for the shares to which they have subscribed. However, under the SLRs, if a listed company conducts certain transactions with its controlling shareholder, such as issuing shares or conducting mergers or business alliances, the company must obtain an opinion from a third party who is independent from its controlling shareholder that the transaction would not undermine the interests of minority shareholders of the company.

There are no specific duties of controlling shareholders to the company or other minority shareholders under the Companies Act. In an extreme case where a controlling shareholder abuses the company or other minority shareholders (e.g., a transaction with the company involving extremely unfair consideration or a squeeze-out of minority shareholders at an extremely low price), it may be liable for the abusive acts under the Civil Code or other laws, although there are no clear-cut standards for such cases.

iii Shareholder activism

Derivative actions

Under the Companies Act, a shareholder can demand that the company file an action to pursue, inter alia, directors or corporate auditors for their liabilities to the company if the shareholder has held shares of the company for the preceding six consecutive months or more. If the company does not file an action within 60 days of receipt of the demand from the relevant shareholder, the shareholder can file an action on behalf of the company.

Further, multiple derivative actions are allowed, subject to certain conditions, where, inter alia, a director or corporate auditor of a company might be sued by a shareholder of the company’s ultimate wholly owning parent company as long as, inter alia, the shareholder owns 1 per cent or more of the total voting rights or outstanding shares of the ultimate parent company, and the book value of the shares of the company constitutes more than 20 per cent of the total assets of the ultimate parent company as of the date of occurrence of the underlying events that gave rise to relevant obligations of the director or corporate auditor.

The company that directly or indirectly owns 100 per cent of the shares of the ‘subsidiary’ company, but that is itself not a wholly owned subsidiary of any other company.
**Proxy battles**

The FIEL stipulates the rules for proxy fights in listed companies. Under the FIEL, a shareholder or the company that solicits a proxy must provide the other shareholders with a certain set of documents (including a proxy and reference materials that set forth the agenda). It is generally considered to be difficult for a shareholder to embark on and succeed in such a proxy fight, mainly because the shareholder does not know the agenda of the shareholders’ meeting until the convocation notice is sent by the company. In the past, because the Companies Act could be interpreted as allowing companies to refuse to provide the names, addresses and other information of other shareholders to a shareholder who wishes to solicit the proxy if the bidder is or works for a competitor of the company, the bidder could encounter even more difficulties. However, under the current Companies Act, even if the bidder is a competitor of the company, the company may not refuse to provide the information about other shareholders for that reason. In this sense, one of the hurdles to a shareholder embarking on a proxy fight would be alleviated.

**iv  Takeover defences**

As described above, the typical anti-takeover measure used by listed companies in Japan is a precaution-type anti-takeover measure. However, since the *Bull-Dog Sauce* case in August 2007, we have seen fewer attempts at hostile acquisition. In addition, the tender offer regulations under the FIEL were amended so that an offeror must now disclose more information prior to a tender offer and a target company has the right to issue a questionnaire to the offeror. In consequence, the number of listed companies that adopt anti-takeover measures has slightly decreased for 11 consecutive years.

**v  Contact with shareholders**

Under the Companies Act, directors, corporate auditors and executive officers must sufficiently explain the specific issues related to the agenda of the shareholders’ meeting if an enquiry is made by a shareholder. In addition, to improve investor relations, Q&A sessions during shareholders’ meetings are now actively encouraged in Japan. Furthermore, Japanese listed companies often hold informal meetings with investors about financial statements and related issues.

**VI OUTLOOK**

The Reform Companies Act enacted in May 2015 has improved corporate governance (e.g., the comply or explain rule for the appointment of outside directors), and regulates the relationship between parent companies and their subsidiaries (e.g., clarifying the liabilities and rights of parent companies with respect to their subsidiaries (including derivative actions by shareholders of a parent company against the directors of its subsidiary)). In addition, the TSE formulated the Code in June 2015, which was revised in June 2018. The Code has established fundamental principles for effective corporate governance, including a structure for transparent, fair, timely and decisive decision-making by companies, which pays due attention to the needs and perspectives of shareholders and also customers, employees and local communities. Further, the Reform Cabinet Office Ordinance on the Disclosure of Corporate Affairs, etc. enacted in January 2019 has improved the level of disclosure regarding the corporate governance of the listed companies including the remuneration of such companies’ directors.
Furthermore, the Reform Companies Act, which passed the Diet in December 2019, but has not yet been put in force, has further improved the corporate governance (e.g., requiring a large public company that is required under the FIEL to file a securities report: (1) to have one or more outside director; and (2) to establish company's policies for determination of the remuneration for each director). Corporate governance will continue to be a hot issue in Japan.
Chapter 13

LUXEMBOURG

Margaretha Wilkenhuysen and Anke Geppert-Luciani

I OVERVIEW OF GOVERNANCE REGIME

i Statutory framework

Luxembourg’s main statutes on corporate governance include the Companies Act, the EU Market Abuse Regulation and the Securitisation Act. The Companies Act was revamped in 2016 to modernise Luxembourg corporate law, and a consolidated version of the Act was published in December 2017, following the renumbering of its articles.

Other notable statutory instruments regulating corporate governance in Luxembourg include:

a the Act of 30 May 2018 on Markets in Financial Instruments, introducing specific provisions on transparency for shares and transaction reporting, together with the EU Regulation on Markets in Financial Instruments (MiFIR);

b the Takeover Bid Act, providing for minority shareholder protection, rules of mandatory offers and disclosure requirements for companies whose shares are admitted to trading on a regulated market in a Member State of the EU;

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1 Margaretha Wilkenhuysen is a partner and Anke Geppert-Luciani is a professional support lawyer at NautaDutilh Avocats Luxembourg SARL.
2 Act of 10 August 1915 on Commercial Companies.
4 Act of 22 March 2004 on Securitisation, as last amended by the Act of 27 May 2016.
5 Act of 10 August 2016 amending the Act of 10 August 1915 on Commercial Companies. Following the renumbering of the articles of this Act, a new consolidated version of the Commercial Companies Act was published on 15 December 2017 by the Grand-Ducal Regulation of 5 December 2017.
the Prospectus Act,\textsuperscript{9} which requires the publication of prospectuses from companies intending to admit their shares to trading on a regulated market or to make a public offer;

d the Transparency Act of 11 January 2008,\textsuperscript{10} as amended; and

e the Shareholder Act of 24 May 2011,\textsuperscript{11} as amended by the Act of 1 August 2019 setting out a number of shareholders’ rights and aiming to increase long-term shareholder engagement, transposing the Second Shareholders’ Rights Directive\textsuperscript{12} into Luxembourg law.

Furthermore, the Act of 21 July 2012\textsuperscript{13} introduced a squeeze-out right in favour of dominant shareholders and a sell-out right in favour of minority shareholders in companies whose shares are admitted to trading on a regulated market,\textsuperscript{14} and a year later, the Act of 6 April 2013 introduced a legal regime for dematerialised securities, and the Act of 12 July 2013,\textsuperscript{15} as amended, introduced into Luxembourg law a new structure: the special limited partnership. In 2013 and 2015, the accounting standards commission was reformed and certain rules regarding the annual accounts and consolidated accounts of companies were modified.\textsuperscript{16}

Furthermore, in 2014, the Act on the Immobilisation of Bearer Shares\textsuperscript{17} instituted the requirement to deposit bearer shares with a recognised depositary and allowed access by judicial and tax authorities to information on the identity of bearer shares holders.

Also worth mentioning is the Act of 10 March 2014\textsuperscript{18} providing for the possibility of forming a European Cooperative Society in conformity with the provisions of Council Regulation (EC) No. 1435/2003 of 22 July 2003. As a supplement to the general statutory law, the Luxembourg Stock Exchange (LuxSE) 10 Principles of Corporate Governance (LuxSE Principles)\textsuperscript{19} provide general principles, recommendations and guidelines on best

\begin{itemize}
\item Act of 16 July 2019 on prospectuses for securities.
\item Act of 24 May 2011 on shareholders rights in listed companies, as last amended by the Act of 1st August 2019.
\item Act of 21 July 2012 on Mandatory Squeeze-Out and Sell-Out of Securities of companies currently admitted or previously admitted to trading on a regulated market or having been offered to the public.
\item Until the Squeeze-out Act came into force, a squeeze-out and a sell-out right existed only in the context of a public takeover under the Act dated 19 May 2006 implementing Directive 2004/25/EC on takeover bids.
\item Act of 12 July 2013 on Alternative Investment Fund Managers, as last amended by the Act of 8 April 2019.
\item Act of 30 July 2013 reforming the commission of accounting principles and modifying certain rules regarding the annual accounts and consolidated accounts of companies and Act of 18 December 2015 modifying several Acts in view of the transposition of Directive 2013/34/EU. The main modifications introduced by this Act is discussed in Section III.
\item Act of 28 July 2014 on the Immobilisation of Bearer Shares.
\item Act of 10 March 2014 amending the Act of 10 August 1915 on Commercial Companies.
\item Available at www.bourse.lu/corporate-governance.
\end{itemize}
practices relating to general corporate governance issues for all companies listed on the LuxSE and all Luxembourg companies whose shares are admitted to trading on a regulated market operated by the LuxSE.  

ii  Regulatory authorities

In Luxembourg listed companies are often controlled by one or more major shareholders, rendering it impossible to rely solely on market monitoring to ensure that listed companies comply with the LuxSE Principles. Therefore, a system of monitoring involving the shareholders, the board and the LuxSE, at a minimum, is required to ensure proper observance of the principles of corporate governance.

The other main regulatory authority is the Luxembourg Supervisory Commission of the Financial Sector (CSSF), which is in charge of promoting transparency, simplicity and fairness on the markets of financial products and services. The CSSF has jurisdiction regarding matters for which the laws or regulations in force require disclosure, whether or not the information is dealt with in the LuxSE Principles, and also has the authority to impose sanctions. The LuxSE’s role in the external monitoring of compliance with the principles of corporate governance does not affect the CSSF’s legal responsibility as a regulator.

As an operationally independent body, the CSSF has sufficient powers to conduct effective supervision and regulation of the Luxembourg securities market. It is funded by taxes levied from entities under its supervision. To conduct its tasks effectively, the CSSF has broad powers, including the authority to attend meetings of LuxSE entities, suspend rulings, or suspend market intermediaries’ decision-makers if they fail to observe legal, regulatory or statutory provisions.

Other professionals in the financial sector and private sector companies also have an indirect regulatory role through their consultative participation with the government and the legislator in the field of regulation.

II  CORPORATE LEADERSHIP

i  Board structure and practices

Structure

Although public limited liability companies may choose between a two-tier board structure and a one-tier board structure, the latter one remains by far the preferred option in Luxembourg, with a company being managed exclusively by a board invested with the broadest powers to act in the name and on behalf of the company.

In a two-tier system, a company is managed by two bodies: the management board, charged with the day-to-day management of the company, and a supervisory board. The supervisory board’s responsibilities include the appointment and permanent supervision of

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20 As an exception, the 10 Principles do not apply to regulated investment companies with variable capital and funds, to which specific regulations apply. The fourth version of the LuxSE Principles entered into effect on 1 January 2018, and applies to annual reports for financial years as from that date. The main provisions of the LuxSE Principles are discussed in Section IV.


22 Article 442-1 of the Companies Act.

23 Articles 441-1 to 441-13 of the Companies Act.
the management board members, as well as the right to inspect all company transactions.\textsuperscript{24} No person may at the same time be a member of both the management board and the supervisory board.\textsuperscript{25} Members of the supervisory board are liable towards the company and any third party in accordance with general law.\textsuperscript{26} However, there is no specific guidance relating to the exercise by members of the supervisory board of their duties.

**Composition of the board in a one-tier board structure**

The board is composed of appointed members (the company’s directors). A public limited-liability company can be managed by one director as long as it has a sole shareholder.\textsuperscript{27} Otherwise, the Companies Act requires a minimum of three directors;\textsuperscript{28} the maximum number of directors is undefined (the LuxSE Principles advise 16 directors as a reasonable limit).\textsuperscript{29} While the directors are appointed by the shareholders of the company,\textsuperscript{30} the directors choose a chair from among their members.\textsuperscript{31} The Companies Act does not provide any specific powers to the chair of the board, although companies may choose, for example, to grant a power of representation to the chair in the articles of association. However, unlike in other civil law jurisdictions, the chair of the board does not act on behalf of the company in his or her position as chair, but rather on the basis of his or her position as director of the company.

The Companies Act provides that where a legal entity is appointed as director of a public limited liability company, it shall designate a permanent representative to exercise that duty in the name and for the account of the legal entity.\textsuperscript{32}

As for the representation of the company, most articles of association provide that any two directors can represent the company without evidence of a board resolution (although in practice, the board may ratify actions taken previously by directors acting individually).

In this respect, the Companies Act provides for three mechanisms: first, the board can adopt a decision and give specific mandates (limited in time and scope) to one or more of its members, or other individuals, to act on its behalf;\textsuperscript{33} second, the articles of association may entitle one or more directors to represent the company for the purposes of any instrument or in any legal proceedings, either individually or jointly;\textsuperscript{34} or, third, the board may designate a director as a general representative of the company charged with its day-to-day business (the day-to-day manager), and representing the company, individually or jointly, towards third parties for that business.\textsuperscript{35}

Under the third option, power may be delegated to one or more directors, managers or other agents, who may but are not required to be shareholders, acting either individually or

\textsuperscript{24} Article 442-1 et seq. of the Companies Act, in particular, Articles 442-2, Paragraph 3, 442-3, Paragraph 1, 442-7, Paragraph 1 and Articles 442-11 to 442-16.

\textsuperscript{25} Article 442-17, Paragraph 1 of the Companies Act.

\textsuperscript{26} Article 442-16 of the Companies Act.

\textsuperscript{27} Article 441-2, Paragraph 1 of the Companies Act.

\textsuperscript{28} Article 441-2, Paragraph 1 of the Companies Act.

\textsuperscript{29} LuxSE Principle 3, Guideline to Recommendation 3.3.

\textsuperscript{30} Article 441-2, Paragraph 3 of the Companies Act.

\textsuperscript{31} Article 444-3, Paragraph 2 of the Companies Act.

\textsuperscript{32} Article 441-3 of the Companies Act.

\textsuperscript{33} Article 1984 et seq. of the Luxembourg Civil Code.

\textsuperscript{34} Article 441-5, Paragraph 4 of the Companies Act.

\textsuperscript{35} Article 441-10 of the Companies Act.
jointly. While their appointment, removal from office and powers may be specified, limited or extended by the articles of association or the competent corporate body, the Companies Act states that no restrictions to their representative powers may be validly opposed in relation to third parties, even if their appointment is published. The liability of the day-to-day manager is based on the general rules relating to mandates. When a member of the board is appointed as the day-to-day manager, the Companies Act requires the board to report annually to the shareholders on the salary, fees and any benefits granted to that director.

A company will generally be bound by the acts of its directors or by the person entrusted with its day-to-day management, even if those acts exceed the company’s corporate object, unless the company proves that the third party knew that the relevant acts exceeded the company’s corporate object or could not, in view of the circumstances, have been unaware of it. The publication of a restriction to a director’s powers in the company’s articles of association is deemed insufficient to constitute such proof.

Regarding listed companies, the LuxSE Principles distinguish between executive and non-executive managers: executive managers are defined as senior managers who are not board directors but who are members of a body of executives charged with the day-to-day management of the company. There is no other distinction under Luxembourg law, with all board members having the same rights and obligations. A more permanent division of tasks and responsibilities between board members is possible (e.g., by providing for different classes of directors), but any such division is purely internal and is unenforceable towards third parties. It is, however, possible for the board to delegate certain specific powers to individual board members or non-board members in the framework of a specific delegation of power.

**Separation of CEO and chair roles: chair’s role and responsibilities**

While the roles of CEO and chair tend to be separated in practice, there are no legal provisions or guidelines pertaining to a separation of roles or responsibilities.

For listed companies, the LuxSE Principles requires that the chair prepares the board meeting agendas after consulting the CEO, and ensures that the procedures for preparing meetings, deliberations, decision-making and the implementation of decisions are correctly applied. Under this non-compulsory guideline, the chair should ensure the proper application of the rules of governance and provide advice to the board.

Luxembourg law does currently not provide for a specific procedure for direct communication between the CEO or the chair and the shareholders.

For listed companies, according to the LuxSE Principles, companies should ‘establish a policy of active communication with the shareholders’ and allow shareholder dialogue with the board and the executive management.

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36 Article 441-10, Paragraph 1 of the Companies Act.
37 Article 441-10, Paragraph 2 of the Companies Act.
38 Article 441-10, Paragraph 5 of the Companies Act.
39 Article 441-10, Paragraph 4 the Companies Act.
40 Article 441-10, Paragraph 2 of the Companies Act.
41 LuxSE Principle 4.
42 LuxSE Principle 2, Recommendation 2.4.
43 LuxSE Principle 10.
Remuneration of directors and senior management

Directors are not employees of the company as such, and their remuneration falls under the general rules on mandates and corporate law. Generally, and unless otherwise provided by the articles of association, services rendered by the company directors are considered to be provided remuneration-free. If the articles of association authorise remuneration, the global amount to be paid to the directors will be fixed by the general meeting of shareholders, and the board will allocate that amount between board members as it deems fit. The rules on conflicts of interest forbid directors from taking part in or voting on resolutions relating to their own remuneration.

Senior managers are generally employees of the company, and the Luxembourg Labour Code will be applicable as regards their relationship with the company.

The LuxSE Principles recommend establishing a remuneration committee to deal with these issues. The LuxSE Principles state that the company must ‘secure the services of qualified directors and executive managers by means of a fair remuneration policy that is compatible with the long-term interests of the company’, thereby introducing a sustainable aspect rather than concentrating on short-term gains.

Concerning listed companies, following the transposition of the Shareholder Directive II, shareholders must now be informed in detail of the remuneration of directors and the company’s remuneration policy. Companies must prepare a management remuneration policy describing all components, criteria, methods and modalities applied to determine the fixed and variable remuneration of the directors. Shareholders have an advisory vote on this policy, unless the company’s articles of association provide for a binding vote. The remuneration policy must be submitted to the general meeting of shareholders for approval each time there is a significant change thereto and at least every four years. In addition, companies must prepare a report for the annual general meeting on the remuneration and benefits granted to directors.

Committees

The company’s articles of association may allow for the creation of committees appointed by the board to ensure that the directors’ obligations are fulfilled. The LuxSE Principles advise listed companies to establish, from among the board’s members, inter alia:

a. a committee to assist the board in relation to corporate policies, internal controls, financial and regulatory reporting, and risk management;
b. an audit committee;
c. a nomination committee to nominate suitable candidates as directors; and
d. a corporate governance committee to ensure compliance with corporate governance practice.

The articles of association will outline the number of members of each committee, their function and the scope of their powers, and the committees themselves will be appointed by and under the supervision of the board.

44 Article 442-19 of the Companies Act.
45 LuxSE Principle 7.
46 Articles 7 a) and b) of the Shareholder Act of 24 May 2011, as amended by the Law of 1st August.
47 Should the company not have an audit committee, LuxSE Principle 8, Recommendation 8.1 requires that the board reassess the need to create an audit committee regularly.
The LuxSE Principles require listed companies and their boards to establish such committees as are necessary for the proper performance of the company’s tasks. The Principles also recommend that the board appoints as many special committees as are needed to examine specific topics and to advise the board.48 The board itself shall remain responsible for decision-taking.

ii Directors

Although no general legal obligations are in place, the LuxSE Principles require that listed companies’ boards have a sufficient number of independent directors (the number depends on the nature of the company’s activities and share ownership structure), defining independent directors as not having ‘any significant business relationship with the company, close family relationship with any executive, or any other relationship with the company, its controlling shareholders or executive managers which is liable to impair the independence of the director’s judgement’.49 While there are no specific legal provisions regarding independent directors, it is generally understood that all directors, including independent directors, should be provided with timely information for the proper performance of their duties.

Liability of directors

Directors must act in the best corporate interests of the company, and are obliged to comply with the Companies Act and with the company’s articles of association. This includes the obligation to act as reasonably prudent businesspersons. They must manage the company’s business in good faith, with reasonable care, in a competent, prudent and active manner, at all times in the company’s best interests, and must refrain from doing anything that does not fall within the scope of the company’s corporate objectives. The Companies Act also imposes certain general duties on directors, including the general management of the company, representation of the company towards third parties and upholding their duty to avoid any conflicts of interest.50

The Luxembourg legislator has remained silent on what should be considered a company’s best corporate interest. In a judgment delivered in 2015,51 the Luxembourg District Court made some observations on this notion. It explained that it is an adaptable concept, the exact interpretation of which depends on the company concerned and the nature of its activities. For some companies, the corporate interest is aligned to the interests of a company’s shareholders. For other companies, it includes the interest of the legal entity as a whole, including the interests of shareholders but also those of employees and creditors. The Court remarked that for companies that are used for purposes of financing and pure holding companies, the interest of the company’s shareholders will be of overriding importance as the focus of the company’s activities is on the rate of return of its investments.

However, it should be noted that directors of listed companies are held to a number of more specific duties under the Transparency Act and the Market Abuse Regulation, in addition to the LuxSE regulations and principles. According to the LuxSE Principles, the

49 LuxSE Principle 3, Recommendation 3.5.
50 Articles 441-7 and 441-12 of the Companies Act.
51 Luxembourg District Court, 23 December 2015, Nos. 145 724 and 145 725.
board of a listed company is bound by a fiduciary duty to its company and shareholders, and ‘shall act in the corporate interest, and shall serve all the shareholders by ensuring the long-term success of the company’.52

The directors’ duties are owed to the company, and as such they may be held liable towards the company both on civil and criminal grounds.

They are jointly and severally liable in accordance with the general provisions on civil liability53 and the provisions of the Companies Act,54 both towards the company and towards all third parties, for any damage resulting from a violation of the Companies Act or of the articles of association of the company. To elude collective liability, a director must prove that he or she has not taken part in the breach of the Companies Act or of the articles of association of the company, that no misconduct is attributable to him or her, and that he or she reported the breach at the first shareholders’ meeting following his or her discovery or knowledge of the breach.

With regard to mismanagement every director is individually liable.55 In the event of misconduct, according to prevailing doctrine and case law, the shareholders’ meeting must decide whether to make any claim against a director in connection with faults committed by the director in the performance of his or her functions. Creditors of a company may, under certain circumstances, institute action on behalf of the company if the latter fails to do so and if that failure harms the company’s creditors.56 Besides, each director is individually liable in accordance with the general provisions on tort liability.57

The company as well as third parties (including any shareholder or creditor with a legitimate interest) may bring an action against a director. Shareholders may, however, only seek compensation for a prejudice that is distinct from the company’s collective damage, and that can be defined as an individual and personal damage. The possibility for a (minority) shareholder to sue a director has recently been given an explicit legal basis in Luxembourg law.58

If the shareholders have suffered collective damage, it is up to the shareholders’ meeting to demand compensation, in which case an action must be brought by the shareholders’ meeting on behalf of the company (an action initiated by a single shareholder will be dismissed). The legal basis for the action differs depending on whether the proceedings are invoked by the company or by third parties.

Any action by the company has a contractual basis, whereas an action by third parties will be brought on the grounds of tort liability. Whereas, under contractual liability, only reasonably foreseeable damage is to be repaired (except in cases of fraud), under tort liability all damage caused by the misconduct must be repaired. For listed companies, the LuxSE rules and regulations59 provide a series of sanctions in the event its rules are breached, including fines or compensation for damage caused to the stock market.

52 LuxSE Principle 2.
53 Articles 1382 and 1383 of the Luxembourg Civil Code.
54 Article 441-9 of the Companies Act.
55 Article 441-9, Paragraph 1 of the Companies Act.
56 Article 1166 of the Civil Code.
57 Articles 1382 and 1383 of the Luxembourg Civil Code.
58 See Section V.
59 LuxSE rules and regulations have been substantially updated in January 2020 in order to take into account recent developments, in particular the Act of 16 July 2019 in prospectuses for securities, see www.bourse.lu/regulations.
Directors’ liability towards the company is exonerated further to cover the discharge granted to the board by the annual shareholders’ meeting approving the annual accounts. This discharge is only valid for the period covered by the accounts presented to and approved by the general meeting of shareholders, provided that they do not contain any omission or false statement of a material fact. Although a discharge given by the general meeting of shareholders extinguishes the board members’ liability towards the company, it is important to note that proceedings initiated by third parties are not affected by such a discharge.

The directors of a public limited liability company are appointed for a period that cannot exceed six years, although they can be re-elected if the company’s articles of association do not provide otherwise. They may at any time be removed from office by the general meeting of shareholders without cause, by simple majority. It is also possible to provide for stricter conditions in the articles of association via a supermajority vote to appoint or revoke the directors. Another possibility is to authorise each category of shareholders to nominate candidates, among which the general meeting of shareholders will elect the directors.

**Conflicts of interest of directors**

Regarding the rules relating to conflicts of interest, any director who has, either directly or indirectly, a financial interest that is contrary to that of the company in a transaction submitted for approval to the board is obliged to inform the board of his or her conflict, refrain from taking part in the deliberations, abstain from voting and record his or her statement in the minutes of the meeting. A special report regarding the transactions in which one of the directors had a (potential) conflict of interest is then to be prepared and submitted at the next general meeting before voting on any resolutions. If, because of a conflict of interest, the number that is required by virtue of a company’s articles of association to deliberate and vote on a certain matter is not reached, the board of directors can – unless otherwise provided by the company’s articles of association – decide to defer the decision to the company’s general meeting of shareholders. The above-mentioned obligations do not apply when a decision to be taken by the board relates to the company’s normal course of business and is taken under normal conditions.

For listed companies, the LuxSE Principles require directors to show integrity and commitment. It is recommended that directors of LuxSE-listed companies:

- inform the board of any possible conflict of interest and any other directorship, office or responsibility, including executive positions taken up outside the company during the term of the directorship;
- take decisions in the best interests of the company;
- warn the board of possible conflicts between their direct or indirect personal interests and those of the company or an entity controlled by it; and

60 Article 441-2, Paragraph 4, of the Companies Act.
61 Article 2004 of the Luxembourg Civil Code.
62 Article 441-7 of the Companies Act. The same conflict of interest regime applies, in addition to directors, members of the management board and supervisory board of public limited companies, to managers of private limited companies, delegates entrusted with day-to-day management, members of executive committees and liquidators of public limited liability companies.
d refrain from taking part in any deliberation or decision involving such a conflict (unless they relate to current operations concluded under normal conditions). 63

III DISCLOSURE

i Trade and Companies Register and the ultimate beneficial owner register
The Articles of Association and amendments are filed and are published, in principle, in full in the Electronic Digest of Companies and Associations. 64

On 1 March 2019, the law establishing a Luxembourg register of beneficial owners (RBE Act), transposing Article 30 of the 4th AML Directive 65 entered into force. 66 Entities that fall within its scope had to comply with the Act’s provisions until 30 November 2019. The RBE Act applies to entities registered with the Luxembourg Trade and Companies Register, including civil and commercial companies, branches of foreign companies, Luxembourg common investment funds, and other types of investment funds such as the UCITS, SICAR, RAIF and SIF. There is, nevertheless, an exception for companies whose securities are admitted to trading on a qualifying regulated market (qualifying listed entities). The information to be provided includes the ultimate beneficial owner’s first and last name, nationality, date and place of birth, country of residence and national identification or registration number, and the nature and scope of the interest held in the entity. Qualifying listed entities are only required to provide the name of the market on which their securities are traded.

ii Financial reporting and accountability
Every company must file all company accounts annually under the Companies Act, which imposes consolidated accounting for all Luxembourg-based companies where the company has a majority of the shareholding or voting rights in another entity; is a shareholder or member in another entity and has the right to approve or appoint a majority of the members to the administrative, management or supervisory body of the entity; or is a shareholder or member of another entity and solely controls a majority of shareholders’ or members’ voting rights in the entity, further to a shareholder or member agreement. 67

On 18 December 2015, Parliament passed an act implementing Directive 2013/34/EU. 68 This act made various changes to the preparation of the annual accounts of Luxembourg companies. Among other things, it changed the rules that are used to determine the size of a company. Depending on whether a company can be categorised as small, medium or large, various financial reporting obligations apply to it, such as the obligation to draw up consolidated annual accounts or the obligation to use a certain structure of balance sheet and

63 LuxSE Principle 5, Recommendations 5.1 and 5.2. For further recommendations, see Recommendations 5.3 to 5.8.
64 Article 100-10 of the Companies Act. By derogation from this, extracts of the instruments or the deeds establishing société en nom collectif, SCSs and special limited partnerships shall be published.
66 The law is complemented by the Grand Ducal Regulation on registration requirements, administrative fees and access to information in the Luxembourg register of beneficial owners (RBE Regulation) adopted on 15 February 2019.
67 Article 1711-1 of the Companies Act.
68 Act of 18 December 2015 modifying several Acts in the view of the transposition of Directive 2013/34/EU.
profit and loss account. In addition, the disclosure requirements for small companies was changed, and a principle of materiality was introduced, as a result of which information that is considered immaterial may be omitted from the annual accounts.

The LuxSE Principles additionally require that a set of rules be drawn up to regulate the behaviour and the notification obligations relating to transactions of a company’s securities, and to specify which transaction information should be made public. These rules should also place the appointment of a compliance officer, charged with monitoring compliance to the rules, under the responsibility of the board. Principle 8 requires directors to ‘establish strict rules, designed to protect the company’s interests, in the areas of financial reporting, internal control and risk management’. This includes creating, where relevant, an audit committee to discharge the board from its responsibilities of risk management, internal control and financial reporting. The effectiveness of the company’s financial reporting, internal control and risk management system must also undergo regular scrutiny.

LuxSE-listed and Euro MTF-traded companies are additionally subject to the internal LuxSE rules and regulations, which contain a number of disclosure rules primarily derived from the Transparency Act as well as the Market Abuse Regulation. Legal obligations do not specifically include impacts outside the jurisdiction, unless the impacts influence the financial reporting obligations, in which case they must be reported.

The CSSF is responsible for verifying LuxSE-listed companies’ reports and may issue administrative and criminal sanctions in cases of failure to report or misrepresentation, in particular under the Transparency Act. The company’s corporate governance charter should also be made available on its website. In practice, companies publish press releases and past information in addition to regulated information.

However, since reporting on non-listed companies’ social impacts remains on a soft-law basis, there are few legal consequences in cases of misrepresentation or failure to report. Some companies have put internal procedures in place to address complaints that an employee failed to comply with an internal code of conduct. It cannot be excluded that a violation of a CSR obligation may potentially be alleged by a third party if a company does not respect one of its CSR engagements, the publication of which is now mandatory under the LuxSE Principles. However, so far there is no case law or doctrine in the field, and such a claim would depend on the third party being able to prove its personal interest or damage in the claim.

iii Auditors’ role and authority, and independence

The Audit Act and Luxembourg legislation exclusively reserve statutory audits to statutory auditors and to audit firms that have been approved by the CSSF. Access to the auditing profession is regulated by the Audit Act, and the titles ‘auditor’ and ‘audit firm’ are exclusively granted by the CSSF to applicants upon fulfilment of certain criteria. The CSSF also administers a database of statutory auditors, approved statutory auditors, audit firms, approved audit firms, trainee statutory auditors and candidates to the audit profession.

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69 See fn 59.
70 See Section I.ii.
71 See, for example, PricewaterhouseCoopers’ corporate governance procedure at www.pwc.lu.
73 Act of 23 July 2016 on the Auditing Profession, as last amended by the Act of 13 February 2018.
74 Article 7 of the Act of 23 July 2016 on the Auditing Profession.
including third-country auditors and audit entities registered pursuant to Article 12 of the Audit Act. Registered auditors and registered auditing firms must also be members of the Luxembourg national auditing organisation, the Institute of Registered Auditors, which is charged with enforcing the strict application of the rules of the auditing profession and members' respect of their professional obligations.75

The question and definition of the independence of auditors remain unresolved. Under the Luxembourg definition, the requirement for registered auditors and registered auditing firms to be independent from the entity they are reviewing translates as auditors being prevented from being directly or indirectly associated with the decision-making process of the entity reviewed. The auditor is also prevented from auditing the accounts if there is any form of direct or indirect relationship, be it financial, business, employment or other, including the provision of additional services other than audit, between the registered auditor, the registered auditing firm or its network and the entity under review.76

iv The comply or explain model and mandatory disclosure

The comply or explain approach, recommended by the Organisation for Economic Co-operation and Development and the European Commission, is favourably received by company boards and investors.

In Luxembourg, the LuxSE Principles were drafted to be highly flexible and adaptable to the size, structure, exposure to risks and specific activities of each company. The LuxSE Principles consist of three sets of rules: general principles (comply), recommendations (comply or explain) and guidelines. The general principles form the structure upon which good corporate governance should be based and are drafted in a sufficiently broad manner to enable all companies to be able to adhere to them, whatever their particular features. Without exception, all Luxembourg-based listed companies must apply the principles.

At the same time, the comply or explain system allows companies to deviate from the recommendations when justified by companies' specific circumstances, provided that adequate explanation is provided. Given this flexible comply or explain approach, shareholders, and in particular institutional investors, have a paramount role in the thorough evaluation of a company's corporate governance. They should carefully examine the reasons provided by a company whenever it is found to have departed from the recommendations or failed to comply with them, and make a reasoned judgement in each case.

The possibility of one-on-one meetings of directors with shareholders is not regulated by Luxembourg legislation. While possible, in practice, such meetings will depend on, inter alia, the size of the company, its structure, and the number and geographic location of shareholders and directors.
IV CORPORATE RESPONSIBILITY

Corporate responsibility and CSR becomes more and more important for Luxembourg companies. After the National Action Plan on the implementation of the United Nations Guiding Principles on Business and Human Rights, Luxembourg is now working on a National Action Plan on CSR and aims at raising awareness on the importance of CSR.

The Directive 2014/95/EU on disclosure of non-financial and diversity information by certain large undertakings and groups was transposed into national legislation by the law of 23 July 2016. It imposes an obligation on certain companies identified by national authorities as ‘public interest entities’ exceeding an average number of 500 employees during the financial year, including listed companies, banks, insurance companies and other companies, to include information in their annual management report with respect to human rights. The goal is to help investors, consumers and policymakers to assess the non-financial performance of these companies and encourage them to develop responsible business conduct.

Furthermore, when publishing its revised LuxSE Principles in December 2017, the LuxSE added a new Principle on CSR to this document, introducing mandatory disclosure of companies’ CSR commitments. This new LuxSE Principle forces companies to define their policy on CSR aspects. It specifies the measures for the implementation of policies and how to give them adequate publicity. In particular, companies will have to integrate CSR aspects into their long-term value creation strategy and describe how the CSR approach contributes to this goal. In this regard, companies are to present the CSR-related information in a report that assesses the sustainability of the activities and that provides clear and transparent non-financial information in support thereof. Moreover, the board of directors will have to regularly address and review the non-financial risks of companies, including social and environmental risks.

Besides the LuxSE Principles, the Act of 5 December 2007 implementing, among others, the Directive on annual and consolidated accounts, includes a provision on corporate governance practices that listed insurance companies should apply. This provision requires listed companies in the insurance field to dedicate a specific section in their management report to their obligatory and voluntary adhesion to corporate governance codes, as well as all other information purporting to their corporate governance practice.

Moreover, the Transparency Act requires listed companies to publish information regarding their share capital and all regulated information (including financial reporting and shareholding) on their websites, and the Market Abuse Regulation stipulates that complete and effective public disclosure of any inside information must be published on both the

78 See LuxSE Principle 9. This fourth version of the LuxSE’s Principles entered into effect on 1 January 2018, and applies to annual reports for financial years as from that date.
80 Article 85-1 et seq. of the Act of 5 December 2007.
company’s and the LuxSE’s websites. Listed companies must also publish their corporate governance charters on their websites. In practice, listed companies tend to publish not only regulated information, but also all past and present press releases and corporate information.

While CSR commitments displayed on participating companies’ websites have no legal basis and are, therefore, not subject to legal enforcement, the unique nature and size of the Luxembourg marketplace has increased the effect of peer pressure on companies. The importance of CSR is gathering momentum, as demonstrated by the increasing number of companies opting to follow institutional CSR recommendations or drawing up and publishing their own guidelines.

i Whistle-blowing

Luxembourg companies do not have a legal obligation to put a whistle-blowing policy in place. Currently, whistle-blowing policy are in place only for some specific sectors, but with the transposition of the Directive on the protection of whistle-blowers the protection will be substantially extended.

The Labour Code encourages whistle-blowing and provides that no disciplinary action may be taken against employees on the mere grounds of their protest against or refusal of something that they consider in good faith to constitute an unlawful taking of interest, corruption or undue influence as defined under the Luxembourg Criminal Code, whether committed by their employer, any other person senior in rank to them, their colleagues or any third party in relation to the employer.

ii CSR for other stakeholders and employees

Non-shareholders

Under Luxembourg law, directors are neither legally required to take the company’s impact on non-shareholders into account; nor are they prevented from doing so. One of the guidelines in the LuxSE Principles suggests that the board draws up a code of business ethics and defines the values of the company. It is also recommended for a company to show its CSR performance indicators in the form of a comparison over time. For example, the significant indicators could include subcontracting and relations with suppliers.

In practice, an increasing number of private companies are taking social criteria into account in their decision-making and disclosing such information to the marketplace (e.g., the CSR commitments published on the websites of several major Luxembourg-established companies, such as SES and ArcelorMittal, which publicly declare that they will take the social and environmental impacts of their operations into account, both on a national and international level). This consideration may extend to other companies or business partners, but on a voluntary basis only.

81 This means whenever an issuer, or a person acting on its behalf, discloses any inside information to a third party in the normal exercise of business (simultaneously in the event of intentional disclosure, promptly in the event of unintentional disclosure).
83 Articles 245 to 252, 310 and 310-1 of the Luxembourg Criminal Code.
85 LuxSE Principle 2, Guideline 3 to Recommendation 2.3.
86 LuxSE Principle 9, Guideline to Recommendation 9.4.
Employees

The Labour Code\textsuperscript{87} introduced a legal requirement for employee representatives on certain company boards. This legal obligation is limited to public limited liability companies fulfilling two criteria: all companies established in Luxembourg and employing over 1,000 employees over a three-year period; and all companies established in Luxembourg in which the state retains a financial participation of over 25 per cent, or that exercise a state-awarded concession.

Despite the lack of a more general legal requirement concerning representation on company boards, it should be noted that employees in Luxembourg workplaces with more than 15 employees have a legal right to representation at work.\textsuperscript{88} The central element of workplace representation is the workers’ representatives concerned with workers’ everyday concerns and directly elected by all employees. As a result of the adoption of the Act of 23 July 2015,\textsuperscript{89} workers’ representatives saw their duties increased and were given a larger say in certain decision-making processes. The scope of their right to information was also enlarged.

In larger companies employing an average of 150 or more workers over a three-year period, the Labour Code provides for a common decision-taking process of the employer and the workers’ representatives, for example with regard to decisions relating to the introduction or running of technical equipment intended to monitor the behaviour and performance of employees at work.

Unlike in some other European countries, there is no legally backed trade union workplace presence in Luxembourg, although trade unions have a substantial range of rights in the election and operation of employee delegations. Unions also have important rights in joint company committees, and to our knowledge the majority of employee representatives are union members.

Despite an increasing number of non-discrimination laws, including a new equal treatment chapter in the Labour Code\textsuperscript{90} implementing Directive 2000/78/EC, there is no binding anti-discrimination legislation currently in place specifically targeting non-discrimination on company boards.

V SHAREHOLDERS

Shareholder rights and powers

Shareholder’s meetings and equality of voting rights

The Shareholder Act came into force on 1 July 2011 aiming, inter alia, at strengthening the exercise of minority shareholders’ voting rights in listed companies to improve the corporate governance of such companies. The Shareholder Act explicitly refers to a principle of equal treatment of shareholders.\textsuperscript{91}

\textsuperscript{87} Article L426-1 of the Labour Code.
\textsuperscript{88} Article L411-1 of the Labour Code.
\textsuperscript{90} Chapter V (equal treatment), Articles L241-1 to L254-1 of the Labour Code.
\textsuperscript{91} Article 2 of the Shareholder Act, as amended.
In addition, the LuxSE Principles provide that ‘the company shall respect the rights of its shareholders and shall ensure that they receive equal treatment. The company shall define a policy of active communication with its shareholders and shall establish a related structured set of practices’.92

Pursuant to the Shareholder Act, listed companies must give at least 30 calendar days’ notice before holding a meeting (notwithstanding particular requirements under the Takeover Bid Act). Should the quorum not be met at the first meeting, a second meeting must be convened at least 17 calendar days before the meeting is held.95 The convening notice must be published in the Electronic Digest of Companies and Associations, a Luxembourg newspaper and other media in a manner that ensures the effective distribution of the information to the public throughout the European Economic Area.96 In the event that all the shares are registered, convening notices may be sent by registered letter to the shareholders, members of the board (or the management board and the supervisory board) and the statutory auditors. The Shareholder Act requires that, in addition to the agenda, date and place of the general meeting to be held, convening notices must also include:

\[ \text{a) a clear description of the shareholders’ rights to put items on the agenda and to table draft resolutions, the procedure for voting by proxy and a form to be used for that purpose and, if provided for in the company’s article of association, the procedure to vote by electronic means;} \]

\[ \text{b) postal and email addresses that can be used to obtain documents in relation to the meeting;} \]

\[ \text{c) where applicable, a copy of the record date as defined by the Shareholder Act (i.e., the date by which shareholders must register their shares to participate and vote at the general meeting). The date for listed companies is set at midnight Central European Time on the 14th calendar day before the meeting. The shareholder must notify the company at the latest by this date of its intention to participate in the meeting; and} \]

\[ \text{d) the company’s website address, which must contain all of the above information, as well as a full copy of the draft resolutions.} \]

The Shareholder Act allows distance voting by shareholders in advance of the meeting, provided that the company has expressly recognised this possibility and has outlined the related requirements in its articles of association.98 The Shareholder Act details the content of the ballot paper, which must include, inter alia, the full identity of the shareholder, the content of the vote cast in advance, the agenda of the meeting and the deadline before which the ballot paper must be received.99 From now on, when votes are cast electronically a confirmation of receipt of the vote must be sent within a maximum of two months after the vote.100

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93 By doing so, Luxembourg’s Parliament has imposed a longer notice period than the 21-day notice period required under Directive 2007/36/EC.
94 Article 3(1) of the Shareholder Act as amended.
95 Article 3(1), Paragraph 2 of the Shareholder Act as amended.
96 Article 3(1), Paragraph 2 of the Shareholder Act as amended.
97 Article 3(3) of the Shareholder Act as amended.
98 Article 6 of the Shareholder Act as amended.
99 Article 1 (6), 5 Shareholder Act, as amended.
100 Article 1 c) of the Shareholder Act.
The Shareholder Act requires proxy voting to be offered to shareholders under certain conditions, with the proxy holder having the same rights as the shareholder. The company has no obligation to verify that the proxy holder votes in accordance with the shareholders’ instructions.  

The powers of shareholders to influence the board

The Companies Act reserves the management of a company, in principle, to its board. Should a shareholder be directly involved in the management of the company, he or she may be deemed a de facto director and face civil or criminal liability, or both, and generally be liable under the same circumstances as the appointed directors.

Shareholders do, however, control the appointment of the board (and, therefore, its composition) via a majority decision of over 50 per cent to appoint a new director. In addition, shareholders representing 10 per cent of a company’s share capital may force the board to postpone a general meeting of shareholders for a period of up to four weeks and may request the addition of items to the agenda of the shareholders meeting.

As for listed companies, the Shareholders Act acknowledges the right of any shareholder or group of shareholders holding at least 5 per cent of the capital to ask for items to be included in the agenda for the general meeting, and to lodge draft resolutions concerning the items on the agenda of the meeting.

Furthermore, during the annual general meeting, the shareholders can question the board on all aspects of a company’s management, accounting and so forth throughout the year, and may withhold the granting of discharge. The right of shareholders to ask questions during the meeting and to receive answers to their questions is legally enshrined.

Under the Shareholder Act, in addition to the right to ask questions orally during a meeting, shareholders may have the right to pose written questions about the items on the agenda before the meeting is held. If provided for in a company’s articles of association, questions may be asked as soon as the convening notice for the general meeting is published. The company’s articles of association will furthermore provide the cut-off time by which the company should have received the written questions.

Apart from several specific circumstances (e.g., in the case of confidential information), the company must answer any questions addressed to it. Should several questions relate to the same topic, the company may publish a detailed questions and answers document on its website, in which case the chair should draw the shareholders’ attention to the publication.

The Companies Act also allows shareholders to submit questions to management outside a meeting. Any shareholder representing at least 10 per cent of the company’s share capital or voting rights, or both, can ask the board of directors or management body

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101 Article 8 of the Shareholder Act.
102 Article 441-5 of the Companies Act. Since 2016 according to Article 441-11 of the Companies Act, the articles of association can authorise the directors to delegate their powers of management to an executive committee or chief executive officer.
103 Article 441-2, Paragraph 3 of the Companies Act.
104 Article 450-1(6) of the Companies Act.
105 Article 4 of the Shareholder Act as amended.
106 Article 7 of the Shareholder Act as amended.
107 Article 7 (2) of the Shareholder Act.
108 Article 1400-3 of the Companies Act. This new management evaluation procedure, inspired by French law, was introduced to the Companies Act by the Act of 10 August 2016.
questions about the management and operations of the company or one of its affiliates, without the need for extraordinary circumstances. If the company’s board or management body fails to answer these questions within one month, the shareholders may petition, as in summary proceedings, the president of the district court responsible for commercial matters to appoint one or more independent experts to draw up a report on the issues to which the questions relate.  

Certain matters must also be reported to the shareholders, such as any director’s conflict of interest relating to voting on a resolution.  

Furthermore, if a minority shareholder of a public limited liability company finds that directors and members of its management and supervisory boards are negligent or simply not diligent in the performance of their duties, it may sue them. Such an action may be brought by one or more shareholders, the holders of founders’ shares, or both, representing 10 per cent or more of the company’s voting rights.  

**Decisions reserved to shareholders and approval of material transactions with related parties**

The Companies Act provides that a company’s management board has the most extensive powers to perform all actions necessary or appropriate to fulfil the company’s corporate objective, with the exception of the actions specifically reserved by law to the shareholders’ meeting. Such actions include, inter alia, any amendments to the company’s articles of association, the approval of annual accounts and the allocation of the company’s results, which are reserved to the company’s shareholders.

While the Companies Act does not set out any specific areas in which board decisions must be approved by the shareholders, the articles of association of a company may provide that all or certain board decisions must be ratified by the shareholders.

Besides, shareholders must approve material transactions with related parties. With regard to the definition of ‘material transaction’, Luxembourg Law takes into account the nature of the transaction as well as the position of the related party.

**Rights of dissenting shareholders**

The Companies Act currently recognises only a few rights of action on behalf of the company in favour of individual shareholders.

Seeking invalidation of a shareholder decision by dissenting shareholders is only possible on the basis of five grounds specified in the Companies Act:

- a procedural irregularity that influenced or could have influenced the outcome of the decision;
- a violation with fraudulent intent of the rules governing general meetings;
- an ultra vires act or abuse of power affecting the decision;

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109 Luxembourg District Court, 18 November 2016, No. 1809/2016. This judgment clarified the scope of application of this provisions, and, in particular, the questions that can be asked by the shareholders, and the answers provided by the management that are to be considered satisfactory.
110 Article 441-7, Paragraph 2 of the Companies Act.
111 Article 444-2 of the Companies Act.
112 Article 441-5 of the Companies Act.
113 Article 7 c) of the Shareholder Act as amended.
the exercise at a general meeting of voting rights that have been suspended by legislation other than the Companies Act, provided the quorum or majority required to adopt the decision would not have been met but for the unlawful exercise of these voting rights; and

e any other cause provided for by the Companies Act.\(^\text{114}\)

In addition, minority shareholders enjoy a sell-out right under certain conditions. According to the Squeeze-out Act, in the event of an individual or legal entity acquiring at least 95 per cent of the share capital of the company and subject to certain conditions, the remaining minority shareholders are entitled to exercise a sell-out right within three months of the required notification and publication of the acquisition.\(^\text{115}\)

Nevertheless, the extension of the protection of minority shareholders by stipulating provisions in the company’s articles of association (e.g., the right of a minority coalition to propose directors, provisions for a more stringent majority for certain decisions, approval clauses or share transfer restrictions) is well recognised insofar as the arrangement does not conflict with Luxembourg’s public order rules. Providing such additional protection in favour of minority shareholders, whether in the articles of association or otherwise, is common in Luxembourg, particularly among international joint ventures and groupings that use a Luxembourg company structure to promote mutual business activities.\(^\text{116}\)

In this respect, the use of shareholders’ voting agreements of a purely contractual nature is far more common than providing for relevant provisions in the articles of association. Since the amendment of the Companies Act in 2016, the use of shareholders’ agreements has been explicitly recognised in Luxembourg law. The Companies Act does not state that these type of arrangements need to be limited in time. However, it does set out three types of voting arrangements that are null and void: a shareholders’ agreement that violates the provisions of the Companies Act or that is contrary to a company’s corporate interest; an undertaking by a shareholder to vote in accordance with instructions given by the company itself, a subsidiary or any corporate organ of those entities; and an undertaking by a shareholder to those same companies or corporate organs to approve proposals made by the company’s corporate bodies.\(^\text{117}\) If votes are cast at a general meeting of shareholders pursuant to an invalid voting arrangement, the votes shall be considered null and void along with any resolutions taken, unless the votes did not affect the final outcome.\(^\text{118}\) While the use of shareholders’ agreements does allow for discretion and flexibility, any compulsory implementation of this type of arrangement remains at risk.

Benefits for long-term shareholders

The Companies Act does not provide for any specific benefits (e.g., extra votes or dividends) for long-term shareholders, although such facilities may be agreed upon in a shareholders’ agreement or incorporated into the articles of association, or both.

\(^{114}\) Article 100-22 of the Companies Act.

\(^{115}\) Article 5 of the Squeeze-out Act.

\(^{116}\) For further analysis on minority shareholders rights, see also Marc Elvinger, ‘Les minorités en droit des affaires: rapport luxembourgeois’, Annales du droit luxembourgeois, No. 15 (2005).

\(^{117}\) Article 450-2(1) of the Companies Act.

\(^{118}\) Article 450-2(2) of the Companies Act.
Identification of and contact with shareholders

One of the main objectives of the Directive 2017/828 is to give listed companies the right to identify their shareholders and, in the end, to improve the communication between the companies and their shareholders. Intermediaries, even those in third countries, are required to provide the company with information on shareholders identity. They must also provide the shareholders with information in order to facilitate the exercise of shareholder rights.

Shareholders’ duties and responsibilities

Controlling shareholders’ duties and liability

All shareholders have certain obligations by law, including the payment of shares, a proportional contribution to any losses suffered by the company and an obligation of loyalty.

In addition, the controlling shareholders are notably prevented from dictating or imposing an increase of the other shareholders’ obligations without their prior consent, although this principle has been considerably attenuated by the Squeeze-out Act, which grants the right to force the acquisition of shares held by minority shareholders by shareholders controlling at least 95 per cent of the share capital.

Institutional investors’ duties and best practice

Institutional investors as well as asset managers shall develop and publicly disclose an engagement policy that describes how they integrate shareholder engagement in their investment strategy. They shall also on an annual basis, publicly disclose how this policy has been implemented. Institutional investors as well as asset managers and proxy advisers are now bound by accrued transparency obligations.

Besides, it is to note that a number of Luxembourg-based investors have signed the United Nations-supported Principles for Responsible Investment. The first of these six principles is to incorporate environmental, social and corporate governance considerations into investment analysis and decision-making processes. Furthermore, a growing number of investors – while not being signatories to the Principles for Responsible Investment – are taking the private initiative to take such risks into account.

Code of best practice for shareholders

Luxembourg has no official code of best practice for shareholders, although companies may draw up internal codes of best practice for their shareholders.

Shareholder activism

Shareholder activism is not a defined notion under Luxembourg law, and neither derivative actions nor proxy battles are common practice in Luxembourg.

119 Article 1 a) of the Shareholder Act as amended.
120 Article 1b) of the Shareholder Act as amended.
121 Article 5 of the Squeeze-out Act.
122 Article 1e) of the Shareholder Act.
123 For further information, see www.unpri.org. The principles are an investor initiative in partnership with the United Nations Environmental Programme Finance Initiative and the United Nations Global Compact.
v Takeover defences

Takeover bids are covered by the Luxembourg Takeover Bid Act.124 The scope of this Act is limited to companies whose shares are traded on a regulated market in one or more Member State of the European Union. Although Luxembourg law admits the principle of defensive measures, there has been no case law specifically covering this question as yet. In implementing any defensive measures, the board has an obligation to act in good faith with respect to the shareholders’ interest.

In the absence of a specific provision in a company’s articles of association requiring shareholder approval, the board may adopt defensive measures (e.g., issuing new shares within the limits of authorised capital or selling key assets) without the approval of the shareholders, provided that these measures are taken in the best interests of the company. The board may not prohibit the shareholders from accepting an offer. It should be noted, however, that measures aimed at frustrating bids in the long term are not generally deemed to be admissible under Luxembourg legislation. It would, therefore, not be possible to repeat defensive measures whenever the bid is repeated or to take defensive measures that have a long-term effect.

Shareholder and voting rights plans, and similar measures

As a general rule, any increase of a Luxembourg company’s share capital is decided upon by the general meeting of shareholders. However, the articles of association of a Luxembourg public limited liability company may authorise the board of directors to increase the share capital up to a designated amount in one or more instalments.125 The authorisation to do so is only valid for a period of five years, but may be renewed by the general meeting of shareholders.126 As an inducement for an existing shareholder to purchase more shares, it may be decided to abandon any payment of share premium. Beyond that, there is no possibility for a company to offer a discount on the par value of shares to be issued.

White-knight defence

In Luxembourg practice, the board of any company that is the subject of a takeover bid may seek out a third party with the purpose of the third party making a counter-offer that is more favourable to the company. It can do so without the need for approval by the company’s shareholders.


125 As a result of the entry into force of the Luxembourg Act of 10 August 2016, the articles of association of Luxembourg private limited liability companies may now also include an authorisation to the board of managers to issue shares, provided that the shares so issued are either issued to existing shareholders or to a third party that has been approved in accordance with the law.

126 Article 420-22 of the Companies Act.
Staggered boards
Directors of a Luxembourg public limited liability company shall be appointed for a term of office that may not exceed six years. However, directors may be removed from office by the general meeting of shareholders at any time and without stating reasons. As a result, a staggered board does not constitute a major obstacle for a hostile acquirer holding sufficient shares to make changes to the composition of the board.

VI OUTLOOK
While some fundamental elements of corporate governance such as board responsibilities or directors’ liability have not evolved that much over the past years, Corporate (Social) Responsibility as well as disclosure obligations become more and more important. The transposition of the Shareholder Directive II into Luxembourg Law and its implementation in practise will also be interesting to follow in the light of enhanced long-term shareholder engagement and more sustainability.

127 Article 441-2, Paragraph 4 of the Companies Act.
I OVERVIEW OF GOVERNANCE REGIME

In the Netherlands, the general rules of civil law relating to the governance of companies and listed companies are laid down in Book 2 of the Dutch Civil Code (DCC). This sets out the duties and powers of the various corporate bodies, as well as rules on representation, conflicts of interest and the liability of management board members. The DCC also contains rules regarding financial reporting and disclosure. Compliance with the rules in the DCC can, if necessary, be forced through the courts. Furthermore, shareholders with a specific capital interest (in some cases even former shareholders) have the right to request an inquiry into the company’s policy and affairs, at a court specially designated for this purpose – the Enterprise Chamber of the Amsterdam Court of Appeal. Upon a showing of mismanagement, the Enterprise Chamber can intervene by, inter alia, suspending or nullifying a management board decision, suspending or removing management or supervisory board members and appointing temporary board members. In practice, inquiry proceedings have played an important role in the development of law in the area of corporate governance; for example with regard to the issue of the respective roles of the management board and the shareholders in determining the strategy of the relevant company.

In addition, the Netherlands has rules on the supervision of the business conduct of listed companies, laid down in Chapter 5 of the Financial Supervision Act (FSA). The FSA contains rules on, inter alia, the disclosure of major holdings, financial reporting, the prevention of market abuse and the obligations of institutional investors. Supervision of compliance with these rules is carried out by a specially designated body, the Authority for the Financial Markets (AFM).

Alongside these statutory rules, there is a system of self-regulation consisting of codes of conduct containing principles and best-practice provisions drawn up by the sector itself. The first Dutch Corporate Governance Code containing governance rules for listed companies entered into effect in 2004. In December 2016, a revised version was published, with more attention being paid to long-term value creation, culture, reporting of misconduct and risk management.

Since the introduction of the first Corporate Governance Code, several sectors have set up their own specific codes, such as the Code of the Dutch Pension Funds and the Housing Corporations Code. In 2010, the Banking Code was introduced to govern Dutch banks. This mirrors the Corporate Governance Code in many respects, but also contains rules specifically
targeted at banks (specific expertise of certain committee or board members, the treatment and interests of clients). The Banking Code (updated in 2015) applies to both listed and unlisted banks. Listed banks fall under the Corporate Governance Code, as well as the Banking Code. Both codes adopt a 'comply or explain' system: on their websites. Companies must state how they applied the principles and best-practice provisions and, if applicable, provide a reasoned explanation of why a provision has not been applied.

As from January 2019 the first Dutch Stewardship Code entered into force, a form of self-regulation that does not have a statutory basis. Pension funds, insurers and asset managers have developed this Stewardship Code to emphasise the increasing importance of engaged and responsible share-ownership and the role that institutional investors play in promoting long-term value creation at Dutch listed companies. The principles of the Stewardship Code offer pension funds, insurers and asset managers the opportunity to inform their beneficiaries and clients about how they have used their shareholder rights. All institutional investors holding shares in Dutch listed companies are expected to aim for meaningful implementation of the principles of the Stewardship Code and to report on compliance with the Stewardship Code.

II CORPORATE LEADERSHIP

i Board structure and practices

Dutch corporate law has traditionally provided for a two-tier board structure, consisting of a management board and a separate supervisory board (each of which is governed by different statutory provisions); however, the institution of a supervisory board is only mandatory for companies subject to the 'structure regime'. A company is subject to this regime if, for a period of three consecutive years:

a its issued capital and reserves amount to not less than €16 million;
b it has a works council instituted pursuant to a statutory requirement; and
c it regularly employs at least 100 employees in the Netherlands.

Since 2013, Dutch corporate law has also provided a statutory basis for the one-tier board structure. However, through the influence of international developments, the one-tier board structure had made its way into Dutch corporate practice prior to this legislation. Therefore, the Corporate Governance Code of 2008 already contained provisions relating to listed companies with a one-tier board structure. In 2016, the new Code clarified how companies with a one-tier board must apply the Code by, inter alia, specifying that the current rules for supervisory board members also apply to non-executive directors.

Generally, the one-tier model is considered to be suited to companies in a highly dynamic environment such as companies in the technology sector, complex companies that need to act quickly in crisis situations, companies that are in the process of being listed and in which a major shareholder is closely involved in the company's management or supervision (family businesses) and companies that form part of an international group or have an international group of shareholders. In practice, the one-tier model and the two-tier model appear to be growing closer to one another: in companies with a two-tier board structure the supervisory

3 Book 2, Title 4, Part 6 of the DCC.
board is now expected to play a more active role, while in those with a one-tier structure it is often required that the majority of board members consist of independent non-executives. According to the new Code, the latter is also mandatory. For this reason, some commentators speak of a convergence towards a 1.5-tier structure.5

**Management board**

The management board is charged by law with the duty to manage the company, subject to restrictions imposed in the articles of association.6 It is generally accepted that management in any event includes directing the company’s day-to-day affairs and setting out its strategy. It should be borne in mind that in accordance with the Dutch stakeholder model, the board must take into account various interests, not only those of the enterprise and shareholders, but also those of other interested parties, such as employees and creditors.

In recent years the average size of the boards of Dutch listed companies has declined; a significant number of companies even have two-member boards. The rise of this ‘CEO–CFO model’ can be explained by a number of factors, one of which is the popularity of the executive committee (Exco), in which board members, as well as senior managers, have seats; in these setups a larger management board makes less sense. Although clearly desirable in terms of efficiency, Excos also raise several governance issues that require due consideration. The new Corporate Governance Code Committee does embrace the Exco; however, it requires companies to render account of governance issues such as how the interaction between the Exco and the supervisory board will be structured. Furthermore, the Exco’s role, duties and composition must be set out in the management report.

**Supervisory board**

The function of the supervisory board is to supervise and advise the management board and oversee the general state of affairs within the company.7 Like the management board, the supervisory board must take into account the interests of the company and its enterprise, as well as those of all other stakeholders.

The supervisory board of a structure-regime company has a number of important rights, including the right to appoint, suspend and remove management board members, and the right to approve (or refuse to approve) certain management board decisions, such as a decision to issue shares, enter into a joint venture, make a major acquisition or large investment, amend the articles of association or dissolve the company.8

To enable the supervisory board to perform its supervisory duties, the DCC requires the management board to provide the supervisory board at least once a year with information about the company’s strategic policy, its general and financial risks and its internal control system. The Corporate Governance Code expands upon the supervisory duties: if the

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6  Article 2:129 of the DCC.
7  Article 2:140(2) of the DCC.
8  Article 2:164 of the DCC.
supervisory board consists of more than four members, it must appoint from among its members an audit committee, a remuneration committee and a selection and appointment committee, whose duties are also specified.

ii Directors (both management and supervisory board)

Appointment and removal

As previously stated, management board members of structure-regime companies are appointed and removed by the supervisory board. In companies not governed by this regime, the general meeting of shareholders has this power. Under the Corporate Governance Code, directors are in principle appointed for a maximum term of four years, but reappointment for successive four-year terms is permitted. However, this is limited to only one additional four year term for supervisory board members with a possible third and fourth term of two year. In the event of a reappointment after an eight-year period, reasons should be given in the report of the supervisory board.

Each management board member who has been employed for two years or more, is entitled to claim a transition payment when the contract is (1) terminated by the employer; (2) dissolved in court at the employer’s request; or (3) has ended by operation of law. Only in exceptional circumstances, such as in the event of any seriously culpable act or omission on the employer’s part, or other extraordinary circumstances, could the board member be eligible for additional severance pay, referred to as ‘fair compensation’. Under the Code no remuneration is justified if the board member ended the contract on his or her own initiative or in the case of seriously culpable or imputable acts.

 Supervisory board members of structure-regime companies are appointed by the general meeting of shareholders based on a nomination by the supervisory board. The general meeting of shareholders may, however, overrule such a nomination. The general meeting of shareholders and the works council may recommend persons for nomination. An individual supervisory board member of a structure-regime company may only be removed by the Enterprise Chamber of the Amsterdam Court of Appeal, at the request of the company, the general meeting of shareholders or the works council. However, the general meeting of shareholders may pass a vote of no confidence in the supervisory board as a whole, which results in the immediate removal of all board members.

Independence and expertise

The DCC and the codes contain several provisions intended to safeguard the independence of supervisory board members, such as the absence of family ties and business interests. The Dutch Central Bank (DNB) has developed its own policy rules. It requires that supervisory board members are independent ‘in mind’ (independent with respect to partial interests), ‘in state’ (formal independence) and ‘in appearance’ (no conflicts of interest).

A great deal of attention is being paid to the expertise of supervisory board members. For example, under the Banking Code supervisory board members are expected to have

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9 As a result of recently adopted EU legislation the responsibilities of the audit committee will increase in the future; see Section III.ii.
10 Best Practice 3.2.3 of the Corporate Governance Code 2016.
11 Article 2:158 of the DCC.
12 Article 2:161 of the DCC.
knowledge of the risks of the banking business and of the bank’s public functions. Moreover, banks are expected to introduce a permanent education programme, while legislation has also been enacted; since 1 July 2012 management and supervisory board members of financial institutions have been subjected to a stricter ‘fit and proper’ test, to be applied by the AFM or the DNB.

Additionally, in 2017 the guidelines on suitability assessments of the European Banking Authority (EBA) and the European Securities and Markets Authority (ESMA) and the ECB’s 2017 guide to assessments of board members were introduced. The AFM and DNB support this development. As shown in 2015 by the EBA Peer Review Report on suitability, Dutch assessment procedures are considered as good practice, and the European assessment procedures are largely in line with the current Dutch take on assessments.14

Caps on the holding of multiple supervisory board memberships

The number of supervisory positions a management board member or supervisory board member is allowed to hold at ‘large’ legal entities is limited by the DCC. In principle, a management board member may hold a maximum of two positions as a supervisory board member in addition to his or her management board position; for a supervisory board member the limit is a total of five supervisory positions, with a position as a management board or supervisory board chairperson counting double.

Under the Code, the approval of the supervisory board is required for a management board member of the company intending to accept a supervisory board membership elsewhere.15

For banks and certain types of investment firms, the CRD IV Directive has introduced limitations for ‘significant institutions’.16 As a rule, a management board member is limited to two directorships whereas for a director a maximum of four directorships (in total) or one management board position combined with one other directorship applies. The Dutch implementing rules, which stay very close to the CRD IV regime, entered into force in August 2014.17

Diversity

Over and above these measures to improve the quality of management and supervision, rules to promote gender diversity within the management boards and supervisory boards of large companies have applied in the Netherlands since 1 January 2013, the target being that the board is at least 30 per cent female and 30 per cent male. The rules are of a ‘comply or explain’ nature: if the target is not met this will not lead to the imposition of sanctions, but an explanation must be given in the management report as to why the target was not met and what steps will be taken towards meeting it. In November 2019, a motion was carried asking the government to require listed companies to have at least 30 per cent female members

15 Best Practice 2.4.2 of the Corporate Governance Code 2016.
16 Directive 2013/36/EU of the European Parliament and of the Council of 26 June 2013 on access to the activity of credit institutions and the prudential supervision of credit institutions and investment firms.
on their supervisory board. If the government decides to introduce the quota, a bill will be prepared. Since legislative processes may be rather lengthy, entry into force is not expected before the end of 2020, at the earliest.

Narrower in scope but still relevant, EU Directive 2014/95 requires ‘large’ companies to have a description of the diversity policy applied in relation to the undertaking’s administrative, management and supervisory bodies. This Directive was implemented in Dutch law and entered into force on 1 January 2017. Diversity under this Directive has a wider significance than gender alone, but also includes, inter alia, background, expertise, nationality and experience.

**Conflicts of interest**

Neither a management board member nor a supervisory board member will be permitted to take part in any discussion or decision-making that involves a subject or transaction in relation to which he or she has a conflict of interest. The DCC provides subsequently that if the board member nevertheless does take part, he or she may be liable towards the company, but the transaction with the third party will in principle remain valid.

**Internal liability**

A management board member or supervisory board member who has performed his or her duties improperly may be held personally liable to the company. In principle, each board member is liable for the company’s general affairs and for the entire damage resulting from mismanagement by any other board member (principle of collective responsibility). A board member may, however, avoid liability by proving that he or she cannot be blamed for the mismanagement. The allocation of duties between the board member and his or her fellow board members is one of the relevant factors in that respect. With respect to the one-tier board model an internal allocation of duties among the board members is permitted, but that this does not change the directors’ collective responsibility for the company’s management. The non-executive board members (i.e., those not charged with attending to the company’s day-to-day affairs) may therefore be held liable for the mismanagement of an executive board member. For that reason it is advisable that board members keep each other informed of their actions and actively inform each other, sometimes also referred to as a monitoring duty.

It is a well-established concept of Dutch law that personal liability should only arise in situations of apparent mistakes or negligence. In this context, the concepts of, for example, ‘severe fault’ or ‘apparent mismanagement’ are developed in case law or are part of statutory provisions. Recent case law, however, reminds us that this does not imply immunity.

The Supreme Court has held that only the company, or a bankruptcy trustee in cases of insolvency, may sue a board member for mismanagement under Article 2:9 of the DCC; there is no shareholder derivative action under Dutch law. However, in certain situations,

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19 Directive 2014/95/EU amending Directive 2013/34/EU as regards disclosure of non-financial and diversity information by certain large undertakings and groups.

20 *Fairstar*, 30 September 2015.

directors may incur personal liability as regards third parties, such as shareholders or creditors of the company on account of tort or on account of specific provisions in the law, such as in the case of insolvency caused by apparent mismanagement.

External liability
As a general rule, management board members will not be personally liable for the company’s debts or other obligations as regards creditors or other third parties. Liability might only ensue if that board member: (1) can be seriously blamed for having conducted a wrongful act on the company’s behalf towards a third party; (2) is subject to liability pursuant to certain specific statutory grounds; or (3) is penalised pursuant to criminal or administrative law. A parent company or its directors may, under certain circumstances, also be liable for the debts of a subsidiary.

If a company is declared bankrupt, special rules – including certain evidentiary presumptions – apply. Under these rules, each management board member is personally liable for debts that cannot be satisfied from the assets of the bankruptcy estate if the management board was guilty of clear mismanagement during the three-year period preceding the bankruptcy and it is likely that this was an important cause of the bankruptcy. Besides failure of the management board to comply with its accounting obligations and its obligation to file the annual accounts, clear mismanagement constitutes conduct that is seriously irresponsible, reckless or rash; the trustee in bankruptcy must show that no reasonably thinking board member would have acted in this way under the same circumstances. Case law shows that supervisory board members are not immune in this respect.22

III DISCLOSURE
Listed companies are subject to various disclosure obligations. The general rules on financial reporting can be found in Book 2 of the DCC, while the FSA contains additional rules applicable to listed companies. The Corporate Governance Code also lays down several specific financial disclosure obligations for listed companies.

The DCC contains rules with regard to the composition of the annual accounts and management report, the auditor’s opinion, the adoption of the annual accounts and the publication requirement. Listed companies are required to send their annual accounts to the AFM after adoption. If the AFM believes that annual accounts do not comply with the relevant rules, it may initiate special ‘annual accounts proceedings’ before the Enterprise Chamber of the Amsterdam Court of Appeal. Shareholders and employees may also initiate such proceedings. In these proceedings, the Court may order the company to amend the annual accounts and management report in accordance with its instructions.

The transparency requirements can, in general terms, be divided into two categories: ad hoc disclosure obligations and periodic disclosure obligations.

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22 Landis, 19 June 2013, Van der Moolen, 15 February 2013 and Meavita, November 2015.
i  Ad hoc

The main example in this first category is the obligation for issuers of securities in regulated markets to disclose inside information that directly concerns the issuer as soon as possible. Disclosure may be delayed if the following conditions are met: (1) the immediate disclosure is likely to prejudice the legitimate interests of the issuer or emission allowance market participant; (2) the delay of disclosure is not likely to mislead the public; and (3) the issuer or emission allowance market participant is able to ensure the confidentiality of that information. When the issuer or emission allowance market participant has delayed the disclosure of inside information it shall, immediately after the information is disclosed to the public: (1) inform the competent authority that the disclosure of the information was delayed; and (2) provide a written explanation of how the conditions set out above were met. The Netherlands has ‘opted in’ for the requirement of a written explanation (2) to be given only upon request of the competent authority. An issuer that is a financial institution or credit institution has additional grounds for delaying public disclosure of inside information where disclosure would risk undermining the financial stability of the issuer and of the financial system, the delay is in the public interest, confidentiality can be ensured, and the competent authority consents. 24

Another relevant disclosure obligation concerns shareholders of listed companies. They are required to notify the AFM if their holdings of voting rights or capital in listed companies reach, exceed or fall below particular thresholds. Gross short positions in excess of a certain threshold (3 per cent) must also be disclosed; this obligation is intended to give an insight into the shareholder’s true economic interest and, at the same time, to shed light on ‘empty voting’. Moreover, shareholders are obliged to disclose the loss or acquisition of predominant control (30 per cent shareholding or voting rights). The issuer is required to disclose certain information as well, such as changes in its issued capital or in the number of voting rights on its shares. Management and supervisory board members of listed companies are also required to notify the AFM of their holdings of shares or voting rights in the company and of any transactions in these shares or changes in the voting rights.

ii  Periodic

The periodic disclosure obligations consist mainly of the annual and half-yearly financial reporting requirements. With regard to the auditing of financial disclosure, statutory auditors are required to enact an extensive, supplementary control statement for the audit committee of the board of directors. Audit committees have to explain how the audit contributed to the integrity of the financial reporting, what the audit committee’s role has been in the process, and bear responsibility for the selection procedure regarding the auditor.

24  Section 17(5) MAR.
25  Section 5:38-44 of the FSA.
26  The absence of any economic interest with the party legally entitled to exercise the voting right at the general meeting of shareholders.
27  Section 5:25c et seq. of the FSA.
28  Audit Firms (Supervision) Decree.
The Corporate Governance Code also contains provisions on the auditing of the financial reports and the position of the internal audit function and the external auditor. These provisions cover subjects such as the role, appointment, remuneration and assessment of the functioning of the external auditor, as well as the relationship and communication of the external auditor with the management board, supervisory board and audit committee.

IV CORPORATE RESPONSIBILITY

The Netherlands has traditionally followed the stakeholder model, under which management and supervisory board members are required to take into account the interests of all stakeholders when making decisions and performing their duties. The Corporate Governance Code is based on the principle that a company is a long-term alliance between the various parties involved in the company, such as employees, shareholders and other investors, suppliers, customers, the public sector and public interest groups. The Dutch Stewardship Code also confirms the duty of asset owners and asset managers to take the interests of stakeholders into account, such as banks, creditors, customers, suppliers, the works council and non-governmental organisations.

With regard to the scope of the responsibility, the Dutch Stewardship Code states that in assessing the Dutch listed investee companies’ long-term value creation opportunities, risks, strategy and performance, it is critical to consider environmental (including climate change risks and opportunities), social and governance information (including board composition and diversity) besides financial information. This is in line with the Corporate Governance Code. The Code requires the management board to draw up a view and strategy on long-term value creation setting out, inter alia, any aspects relevant to the company, such as the environment, social and employee-related matters, the chain within which the enterprise operates, respect for human rights, and fighting corruption and bribery.29

In light of the call for action on climate change, corporate responsibility is climbing up the agenda of governments all over the world, as well as regulatory authorities such as the DNB.30 Another relevant development is the adopted Dutch Child Labour Due Diligence Act, which will enter into force in 2020. This Act is aimed at all companies selling goods or serviced to Dutch end-users and imposes an affirmative due diligence obligation to investigate whether there is a reasonable suspicion that goods or serviced supplied have been produced using child labour and if suspicion is found, adopt and implement a plan of action. It also introduces serious penalties for companies and their directors. On an international level, large public-interest entities – in short: listed companies, banks and insurers – are required to include in their management reports a non-financial statement containing certain CSR-related information.

Risk management

Not surprisingly, post-crisis governance reforms focus on risk management. As a result of the financial crisis in The Netherlands (2007-2011), risk management gained prominence in the Corporate Governance Code. The 2016 Code contains several best practices to further strengthen risk management and disclosure related to risk. For instance, the position

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29 Best Practice 1.1.1 of the Corporate Governance Code 2016.
30 Supervision Outlook 2019 of 29 November 2018, on the website of DNB: www.dnb.nl.
of the internal auditor and the role of the audit committee regarding staffing, work plan and functioning of the internal auditor are strengthened. Furthermore, the chief financial officer, the internal auditor and the external auditor should attend the audit committee meetings, unless the audit committee determines otherwise. In practice, the Code also turns out to have a knock-on effect on other sectors. Often the rules of the Code are used by non-listed companies, serving as a model for codes of conduct in all sorts of sectors, including semi-public sectors such as healthcare and education.

In addition, Article 2:391 of the DCC requires the management board to describe in the management report the main risks to which the enterprise is exposed. If necessary, to properly understand the results or position of the company and its group companies, the management report should also contain an analysis of both financial and non-financial performance indicators, including environmental and employment-related issues.

ii Client focus

The ‘client-focus’ principle forms part of the Banking Code and is regarded as a necessary precondition for the continuity of the undertaking. Complementary to the Banking Code, the Dutch Banking Association introduced a ‘social statute’ setting out the sector’s core values, a banking oath and disciplinary measures, in which the importance of client focus is stressed. Alongside the efforts of the sector itself, both the Dutch Central Bank and the AFM, within their respective areas of competence, continuously monitor progress on client focus and press for further change.

iii Remuneration

According to the Corporate Governance Code the purpose of the remuneration structure should be to focus on long-term value creation for the company and its affiliated enterprise. The remuneration must not encourage management board members to act in their own interests nor to take risks that are not in keeping with the strategy formulated and the risk appetite that has been established.31 The Banking Code also contains a section on remuneration policy.

The variable remuneration of management board members of banks is maximised to 100 per cent of the fixed salary and subjected to strict conditions: if breached, the rate of a newly introduced bank tax will be increased by 10 per cent.32 Moreover, there is a maximum of variable remuneration within the whole of the financial sector of 20 per cent of the fixed salary.33

Financial companies as well as Dutch public limited companies (NVs) have the power to claw back bonuses from management board members.34 The relevant Act that introduced this rule was the subject of extensive parliamentary debate because of a controversial provision requiring listed companies, in merger and takeover situations, to deduct from a management board member’s salary any increase in the value of the company’s shares following the merger or takeover; a management board member with shares in the company is therefore precluded from profiting from the transaction. The – understandable – rationale behind this provision is to eliminate personal gain as the driving force behind the decision-making in such situations.

32 Banking Tax Act (Bulletin of Acts and Decrees 2012, 325); the Act entered into force on 1 October 2012.
33 Bulletin of Acts and Decrees 2015, 45.
34 The Clawback Act (Bulletin of Acts and Decrees 2013, 563).
This ‘skimming off’ rule expired, pursuant to a sunset clause, on 1 July 2017. The Minister of Finance has announced to draw up a draft bill for consultation purposes regarding this subject, but nothing has been submitted to Parliament thus far.

Furthermore, ‘say on pay’ has been at issue, partly in the context of the revised Shareholders Rights Directive (see Section V.i) and in part following the adoption of a law that introduced a say-on-pay right for the works council as of January 2019. Since the Bill implementing the Shareholders Rights Directive entered into force on 1 December 2019, the works council also has the right to render an opinion on the proposed remuneration policy adopted by the AGM at least every four years. Besides the new requirements for the content of the remuneration policy that are introduced by the Shareholders Rights Directive, the Dutch government added an additional requirement, namely that, henceforth, the remuneration policy must explain how the identity, mission and values of the company and its affiliated companies, the company’s internal remuneration ratios and those of its affiliates, and public consensus have been taken into account. Furthermore, a majority of at least 75 per cent is required to approve a change to the company’s remuneration policy, unless the articles of association provide for a lower majority. Finally, another new rule introduced by this bill affects companies that are subject to the structure regime. Within these companies, the works council has by law a strengthened right to recommend a third of the members of the supervisory board. According to the new rule, if the supervisory board establishes an incentives or remuneration committee from among its members, the board members appointed further to the works council’s recommendation will automatically sit on this committee.

Of course, although the discussion specifically focuses on remuneration, it is in fact a general behavioural and cultural change that is expected.

V SHAREHOLDERS

i Shareholder rights and powers

The general meeting of shareholders has important powers within the company, such as the power to amend the articles of association, dissolve the company, approve a merger, adopt the annual accounts and appoint supervisory board members. In addition to these specific powers, article 2:107 of the DCC assigns all residual powers (i.e., those not assigned to the management board or other corporate bodies) to the general meeting of shareholders. The general meeting of shareholders of a Dutch public limited liability company is not, however, entitled to give the management board binding instructions regarding the manner in which the board carries out its duties. Management board decisions resulting in an important change in the company’s identity or character require the approval of the general meeting of shareholders. This applies, for example, to decisions to transfer the enterprise or almost the entire enterprise, enter into or terminate a significant long-term cooperation, or acquire or divest a significant holding. The provision only applies to decisions that are so fundamental

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35 Act amending the Works Councils Act regarding the competences of the Works Council on directors’ remuneration, Stb. 2018, 221.
36 Article 2:107a of the DCC.
that they change the nature of share ownership, in the sense that the shareholder will, as a result of the decision, in effect have provided capital to and hold an interest in a substantially different enterprise.37

Another important shareholder right is the right to have items placed on the agenda of a general meeting.38 The threshold is 3 per cent. The consequences in practice of the right to have an item placed on the agenda of a general meeting are discussed further in Section V.iv.

In 2017, the revised Shareholders Rights Directive entered into force.39 Some of the rules are new to the Netherlands; others already apply under Dutch law, although these are generally the ones that have attracted the most media attention. For example, listed companies throughout the EU will have the right to identify their shareholders; in the Netherlands this is already possible under the Securities Book-Entry Transfers Act.40 Similarly, the ‘new’ right for shareholders to vote on the remuneration policy is already laid down in Section 2:135(1) of the DCC. The Bill implementing the revised Shareholders Rights Directive entered into force, for the most part, on 1 December 2019.

ii Equality of voting rights

The most fundamental right of a shareholder is the right to vote at meetings. In principle, Dutch corporate law adheres to the principle of equality of voting rights: all shares carry equal rights and obligations in proportion to their nominal value and all shareholders whose circumstances are equal must be treated in the same manner.41 The articles of association may, however, provide otherwise. The principle of one share, one vote also applies.42 There are, however, important exceptions to these principles, a few of which are mentioned below.

The first exception is the use of ‘loyalty shares’, to which extra voting rights or extra dividends are attached as a reward for long-term shareholders.43 A second exception to the principle of equality of voting rights is the issuance of protective preference shares: listed companies may protect themselves against hostile takeovers or shareholder activism by issuing preference shares to an independent foundation set up in advance for this purpose (see Section V.v). A third exception to the principle of equality of voting rights is financial preference shares, which are used as a financing instrument. In respect of these shares, too, there is a disproportionate relationship between the voting rights acquired and the capital invested. With respect to the issuance of financing preference shares, the Corporate Governance Code provides that the voting rights attached to such shares must be based on the fair value of the capital contribution.44 This represents an attempt to return to the one-share, one-vote principle.

37 ABN-AMRO, 13 July 2007.
38 Article 2:114a of the DCC was introduced by means of the Corporate Governance Act; see Section V.iv.
40 Wet giraal effectenverkeer.
41 Article 2:92 of the DCC.
42 Article 2:118(2) of the DCC.
44 Best Practice 4.3.4 of the Corporate Governance Code 2016.
iii Shareholders’ duties and responsibilities

Under Dutch law, shareholders – unlike management and supervisory boards – are in principle not required to be guided by the interests of the company and its affiliated enterprise. Shareholders may, therefore, in principle give priority to their own interests, with due regard for the principles of reasonableness and fairness. Based on these principles, however, larger shareholders are considered to have a certain responsibility towards other parties. The Corporate Governance Code’s preamble states: ‘The greater the interest which the shareholder has in a company, the greater is his or her responsibility to the company, the minority shareholders and other stakeholders.’ Institutional investors in particular are therefore being called upon to accept greater responsibility.

In this regard, the Corporate Governance Code seeks to increase the transparency of voting behaviour. Institutional investors must publish their voting policy on their website and report annually on how that policy has been executed in the preceding year. They must also report quarterly to the general meeting of shareholders on how they have exercised their voting rights. Furthermore, Eumedion adopted a set of ‘Best Practices for Engaged Share-ownership’ in June 2011, which, inter alia, call on institutional investors to inform clients of conflicts of interest if, in relation to a particular matter, the investors have divergent roles that could affect their voting behaviour.

At the European level, similar developments have taken place. In this regard, the ESMA updated its guidelines in 2014 on ‘acting in concert’ in the Directive on Takeover Bids (see Section V.v). In addition, the revised Shareholder Rights Directive requires institutional investors to be more transparent about their voting policies, as this would lead to better investment decisions and could also facilitate dialogue with the relevant company.

iv Shareholder activism

In practice, the shareholder rights described in Section V.i have also been actively exercised by hedge funds, most notably the right to have an item placed on the agenda of a general meeting. Although the aim of the new rights was to increase shareholder participation and strengthen the monitoring of management boards, the actions of hedge funds have also revealed a dark side to participation. In particular, the focus on short-term profits has had adverse effects in some cases.

A number of situations in which activist investors targeted companies with similar proposals caused both government and parliament to reconsider the desirability of shareholder activism. To this end, the Corporate Governance Act was introduced in 2013. The idea behind the Act is to enable the management board, through the introduction of disclosure obligations, to learn the identity and intentions of its shareholders at an early stage, so that it can enter into a dialogue with them. The minimum threshold for the obligation to disclose substantial holdings of capital or voting rights in listed companies has therefore been reduced from 5 per cent to 3 per cent. In addition, the threshold for the right of shareholders to have items placed on the agenda for a general meeting has been substantially raised, from a capital
interest of 1 per cent to a capital interest of 3 per cent; the alternative threshold in the case of
an interest of €50 million for listed companies has been cancelled. Finally, the Act contains a
mechanism enabling a listed company to identify its ‘ultimate investors’.

The issues of empty voting or securities lending, both of which have appeared to be
important instruments for activists, have not been directly provided for in the Act. Hedge funds
can use these devices to influence decision-making in the general meeting of shareholders,
without bearing any economic risk. Furthermore, shareholders of listed companies are not
only obliged to disclose their long positions in excess of a certain threshold, but also their
gross short positions (see Section III.i) and should, when exercising the right to place an item
on the agenda disclose their full economic interests (both long and short). As a result, the
shareholder’s true motives for placing an item on the agenda should be revealed, which is
supposed to discourage the practice of empty voting as well.

In limiting the right to have items placed on the agenda the Corporate Governance
Code goes further than the Act. The Code provides that a shareholder of a listed company
may exercise this right only after having consulted the management board about this. If the
item to be placed on the agenda may possibly result in a change in the company's strategy,
the management board must be given a period of a maximum of 180 days to respond (the
response time). The management board should use this period to confer with the relevant
shareholder. The statutory period for such requests, however, is 60 days before the meeting –
even for items relating to the company’s strategy – and may, therefore, clash with the response
time. The response time is an elaboration of the statutory principles of reasonableness and
fairness that shareholders are required to adhere to in their relations with the company, and
must, therefore, be respected by an activist large shareholder. It may only be disregarded
on compelling grounds. Furthermore, on 19 December 2019, a bill was submitted to the
Lower House of Parliament, introducing a statutory cooling-off period of up to 250 days
during which the shareholders meeting would not be able to dismiss, suspend or appoint
board members of a listed Dutch company under attack. The cooling-off period may also be
invoked in case of unwanted shareholder activism.

The trend towards limiting shareholder rights can also be discerned in Dutch case law.
For example, the Supreme Court, in the summer of 2010, held that it is up to the management
board to determine corporate strategy. Decisions of this nature need not be submitted to
the shareholders for approval or consultation, not even on the grounds of reasonableness
and fairness or non-statutory governance rules. This judgment limits the possibility for
shareholders to demand strategic changes. This is echoed in a more recent judgment, in
which a large investor was denied the right to add a strategic item to the agenda.

v Takeover defences and other protective measures

In Dutch practice, various (structural and ad hoc) defensive measures have been developed
against the threat of hostile takeovers, shareholder activism, etc., among others:

- the incorporation of a protective foundation with a call option to acquire preferred
  shares;

49 Best Practices 4.1.5 and 4.1.6 of the Corporate Governance Code 2016.
50 Cryo-Save, 6 September 2013.
51 ASMI, 9 July 2010.
52 Boskalis/Fugro, 12 January 2018.
a binding nomination right for the company’s board or another body regarding the appointment of directors;

a proposal right for the board or another body in respect of certain resolutions of the general meeting of shareholders;

imposing an ownership limitation on shareholders; and

listing of depositary receipts instead of shares.

The most common takeover defence is the incorporation of a protective foundation with a call option to acquire preferred shares. The shares, which are issued when a threat materialises, change the balance of control within the general meeting of shareholders and make it possible to pass certain resolutions desired by management or in some cases block certain undesired resolutions. The Supreme Court permits the issuance of protective preference shares provided they are necessary with a view to the continuity of the enterprise, and are adequate and proportional. The construction must be temporary in nature and intended to promote further dialogue.53

Shareholder and voting rights plans, and similar measures

As mentioned before, Dutch law accepts a number of deviations from the one-share-one-vote principle (Section V.ii). Instruments that are typically used as a defensive tool are dual-class structures, ownership limitations and — to a lesser extent — loyalty shares. The listing of depositary receipts instead of the shares themselves is not allowed as a defensive measure under the Corporate Governance Code54 and its use by listed companies has slowly declined.

White-knight defence and staggered boards

White-knight defences only occur occasionally in the Netherlands, probably because of the availability of preferable alternatives. Directors are typically appointed and re-appointed on the basis of a rotation scheme, as required under the Corporate Governance Code.55 The concept of staggered boards, as far as we are aware, is not applied by Dutch listed companies.

vi Contact with shareholders

Although the general meeting of shareholders has a statutory right to obtain information, based on which it is accepted that shareholders have the right to ask questions at a general meeting, it is unclear from the relevant DCC provisions whether the management board can itself take the initiative to discuss its intentions with individual shareholders outside a meeting. In practice, such one-on-one meetings do take place. According to the Corporate Governance Code, the company should formulate a policy on bilateral contacts with shareholders and publish this policy on its website. It is important that particular shareholders are not favoured and given more information than others, however, as this would violate the principle that shareholders in the same circumstances must be treated equally. It goes without saying that price-sensitive information may not be disclosed. The fear of violating the market abuse rules causes some shareholders and companies to be hesitant about participating in one-on-ones.

55 Best Practice 2.2.4 of the Corporate Governance Code 2016.
Shareholders among themselves may, in addition, be afraid of being regarded as parties ‘acting in concert’, because under the provisions of the Directive on Takeover Bids\(^{56}\) such parties are obliged to make an offer for the listed shares of a company if they collectively acquire dominant control (30 per cent or more of the voting rights in that company’s general meeting of shareholders). At the end of 2013 ESMA drew up a white list of activities on which shareholders can cooperate without being presumed to be acting in concert, which was updated in 2014 and again in 2019.\(^{57}\) However, if shareholders engaging in an activity on the white list in fact turn out to be cooperating with the aim of acquiring control over the company, they will be regarded as persons acting in concert and may have to make a mandatory bid. The sensitive subject of cooperation with regard to board appointments has been acknowledged, but was nevertheless left off the white list.

VI OUTLOOK

Several legislative plans are currently at the forefront of corporate governance in the Netherlands, some of which originated from before 2017. For different reasons, many of these plans got delayed for the past two years, such as the proposal for new legislation regarding partnerships. Other bills containing corporate legislation have been at a standstill for most of 2018, such as the Management and Supervision Legal Entities Bill. Both remain firmly on the 2020 legislative programme.

Looking at the rest of the 2020 legislative programme, modernisation and simplification of corporate law, together with transparency and the prevention of fraud remains key. All legislative proposals seem to strike a proper balance between the interests of the various stakeholders within an enterprise, without losing sight of the interests of society as a whole. In the end, a model will have to be found whereby risky conduct is discouraged and public confidence in the management boards of banks and companies is restored.

\(^{56}\) Directive 2004/25/EC.

Chapter 15

NORWAY

Gudmund Knudsen and Erik Langseth

I  OVERVIEW OF GOVERNANCE REGIME

i  Sources of law and other regulations

Norwegian public limited companies are governed by the Public Companies Act, which regards important areas (e.g., information requirements, investor protection and accounting) supplemented by other mandatory laws such as the Securities Trading Act, the Stock Exchange Act and the Accounting Act. Companies listed in Oslo are also subject to the continuing obligations of listed companies as adopted by Oslo Stock Exchange.

In addition, important guidelines for corporate governance in listed companies have been established in the Norwegian Code of Practice for Corporate Governance (NCCG). The NCCG provides Norwegian listed companies with guidelines for governing the relationship between the shareholders, the board of directors and executive management more comprehensively than applicable legislation. The NCCG consists of 15 recommended principles of corporate governance, each of which is coupled with explanatory commentaries.

Several provisions of the Public Companies Act have been introduced or amended owing to EU regulations, including Directive 2007/36/EC on shareholder rights with amendment by Directive 2017/828. This directives was implemented in Norway in 2009 and 2019, and applies to listed companies only. The purpose of the directive is generally to improve the shareholders’ opportunities to exercise influence in listed companies.

ii  Enforcement

A shareholder who believes that a resolution by the general meeting violates mandatory law or the company’s articles of association, can take legal action to have the resolution rendered void. An illegally adopted resolution or other forms of non-compliance with mandatory laws can also give rise to claims for compensation.

The NCCG is, on the other side, not directly legally binding. Nevertheless, the NCCG has to some extent gained legal anchoring through the Accounting Act, which requires that listed companies account for their principles and practice of corporate governance in their annual directors’ report on a ‘comply or explain’ basis. This requirement is also established in the continuing obligations of listed companies published by the Oslo Stock Exchange. In addition, companies applying for listing on the Oslo Stock Exchange must report on

1 Gudmund Knudsen is a Norwegian-qualified lawyer and Erik Langseth is a partner at Advokatfirmaet BAHR AS.
the company’s corporate-governance principles in their listing application. By connecting the NCCG to mandatory legislation and stock exchange regulations, the NCCG has been established as guidelines with which companies are generally expected to comply.

II CORPORATE LEADERSHIP

i Governance regime

The Norwegian governance regime draws a fundamental line between a company’s management and its owners. The shareholders exercise the highest authority in the company through the general meeting and may, through the general meeting, decide on any matter provided that it has not expressly been made subject to the exclusive authority of another corporate body (e.g., the board of directors).

A company’s management is divided into two corporate bodies: a board of directors (consisting in practice only of non-executive directors), who have the overall responsibility for the management of the company and a CEO, who is in charge of day-to-day management.

A special feature of the Norwegian governance model is the obligation to appoint a corporate assembly in companies with more than 200 employees. The principal tasks of the corporate assembly consist of board elections and, following a recommendation from the board of directors, to resolve on matters regarding significant investments in relation to the company’s resources, and any rationalisation or alteration of the company’s operations that may cause extensive changes or a re-allocation of the company’s work force. The Public Companies Act does, however, allow the company to agree with a majority of its employees (or unions representing two-thirds of the employees) that a corporate assembly should not be established in exchange for extended employee representation on the company’s board of directors. It is common practice to enter into such agreements.

Another fundamental characteristic of the Norwegian governance regime is the rules in Norwegian companies’ legislation that grant company’s employees the right to elect members to the board of directors and the corporate assembly. The main rule regarding employee representation is that one-third of the members of the board of directors or one-third of the members of the corporate assembly or both are elected by and among the employees. The employee representatives act as ordinary members of the board or corporate assembly and have the same authority and responsibility as the members elected by the general meeting.

ii Board structure and practices

Size and composition of the board of directors

The board of directors must consist of at least three members (five in companies with a corporate assembly). In practice, the boards of Norwegian listed companies tend to consist of between six and 10 directors, of which one-third is elected by and among the employees.

As regards the composition of the board of directors, at least half of the directors must be resident within the EEA and citizens of an EEA country. Since 2006, Norwegian companies’ legislation has also contained requirements relating to gender representation on the board of directors of public limited companies. These rules provide that each gender must, at a minimum, be represented by approximately 40 per cent of the total number of directors elected by the general meeting. According to the Public Companies Act, the CEO cannot be a director.

The Oslo Stock Exchange Listing Rules contains further requirements for listed companies. Pursuant to these rules, at least two of the shareholder-elected directors must
be independent of the company’s executive management, material business contacts and the company’s ‘larger’ shareholders (meaning shareholders who own more than 10 per cent of the company’s voting capital or share capital). No members of executive management may be represented on the board, unless warranted by special circumstances. Finally, all directors must be fit and proper and have satisfactory knowledge of the rules applicable to listed companies on the Oslo Stock Exchange.

Further guidelines and recommendations regarding the composition of the board of directors are set out in the NCCG relating to, inter alia, independence and expertise of the directors.

The chair of the board of directors

The chair of the board is the leader of the board of directors and carries a particular responsibility for ensuring that the work of the board is well organised and that it functions effectively. The chair normally has the casting vote in the event of a parity of votes on the board. The chair shall ensure that matters of current interest are presented to the board. This rule indirectly implies that the chair has a duty to keep him or herself continuously up to date on material matters regarding the company.

Responsibilities of the board

The board of directors has the principal responsibility for the management of the company and for supervising the company’s day-to-day management and activities in general. This includes ensuring that the company’s activities are soundly organised, drawing up plans and budgets for the activities of the company, staying informed of the company’s financial position and ensuring that its activities, accounts and asset management are subject to adequate control.

The principal task of the board of directors, as well as of the other managing corporate bodies (i.e., the CEO and the corporate assembly), is to promote the company’s commercial interest, facilitate value creation and, as a consequence thereof, safeguard the shareholders’ general interest in gains and dividends on the capital invested in the company. However, the managing bodies of a Norwegian company are also entitled – and sometimes obliged – to consider non-shareholder interests (e.g., the interests of the company’s employees, creditors and contract parties), as well as the company’s obligations towards society and the environment. The common view is that the board of directors of Norwegian companies must to some extent have a broader perspective than the sole economic interest of the shareholders. This particular point is reflected in the NCCG, which recommends that the board of directors ‘should define the company’s basic corporate values and formulate ethical guidelines and guidelines for corporate social responsibility in accordance with these values’.

The liability of directors is several and not joint, meaning that each individual director may be held responsible for his or her actions or inactions as a director on the board.

Board committees

The Public Companies Act requires that listed companies of a certain size appoint an audit committee (Section III). Apart from this requirement, the Public Companies Act neither requires nor prohibits the establishment of specialised board committees.

The NCCG further recommends that the board of directors of listed companies consider appointing a remuneration committee consisting of independent directors, to help ensure thorough and independent preparation of matters relating to executive compensation. Many
listed companies also choose to appoint other specialised board committees dealing with particular matters of interest (e.g., corporate social responsibility and social responsibility, HR and workplace environment issues, and so forth).

To the extent board committees are established, such committees cannot be granted authority that is vested in specified corporate bodies according to law. Thus, the principal responsibility for tasks delegated by the board of directors to a board committee will always remain with the board and its individual directors. The work being carried out by a board committee must therefore only be viewed as preparatory or advisory for the board’s discussions.

**Remuneration of directors and the CEO**

Except in cases where the company has a corporate assembly, the remuneration of the directors shall be determined by the general meeting. The Public Companies Act does not contain rules or guidelines with respect to the size of the remuneration to the directors, but further guidelines are provided in the NCCG, which states that the ‘remuneration of the board of directors should reflect the board’s responsibility, expertise, time commitment and the complexity of the company’s activities’ and that the ‘remuneration . . . should not be linked to the company’s performance’. The NCCG also states that share options should not be granted to directors. The size of the remuneration paid to directors in Norwegian companies varies in practice, but historically has been seen as modest when compared with other industrial countries.

The remuneration of the CEO is determined by the board of directors. The board of directors is obligated to produce an annual statement setting out guidelines for the determination of salaries and other remuneration to the company’s executive personnel, including the CEO, for the next financial year. This statement is subject to the consideration of the annual general meeting each year.

### Directors

**Election of directors**

The directors are elected by the general meeting, which also determines whether deputy directors shall be elected. In companies with a corporate assembly, this body is responsible for electing the directors. A decision to remove directors may be taken by the same corporate body authorised to elect the directors, which means that removal of directors is normally resolved by the general meeting. A characteristic feature of the Norwegian corporate law is that a majority of the shareholders, acting through the general meeting, may replace one or several directors at any time during his or her term without cause. This grants the majority shareholders authority to determine and alter the composition of the board of directors at any time. ‘Staggered boards’, where directors cannot be removed until the end of their term, are not permitted according to Norwegian law. An important caveat is that directors who are elected by the employees cannot be removed by the general meeting, but may only be replaced pursuant to a decision by the employees.

The NCCG recommends that the task of proposing eligible candidates for the board of directors, as well as proposing the directors’ remuneration, is prepared by a nomination committee. This recommendation is followed by a majority of the Norwegian listed companies, even though there is no legal requirement to appoint a nomination committee. Whether or not a company shall have a nomination committee is usually (but not necessarily) governed by the company’s articles of association.
The starting point of the Public Companies Act is that the directors are elected for a period of two years, provided the company’s articles of association do not state otherwise. The term cannot, however, exceed four years. The NCCG recommends that directors are not elected for a period of more than two years.

**CEO**

All Norwegian public limited companies must have one or several CEOs. In practice, Norwegian listed companies have only one CEO. The CEO is normally appointed and dismissed by the board of directors.

The CEO is in charge of the day-to-day operations of the company and responsible for executing the board’s resolutions and addressing external relations. The authority of the CEO is generally limited with respect to matters of an unusual nature or major importance to the company. The CEO is subordinate and reports to the board of directors while the board, in turn, has a duty to supervise the CEO. The board of directors may also instruct the CEO on the day-to-day operations of the company.

### III DISCLOSURE

**i  Internal control and financial reporting**

The Public Companies Act requires that listed companies of a certain size appoint an audit committee to advice on and prepare certain matters for the board of directors. At least one of the members of the audit committee must be independent of the company’s operations and have qualifications from accounting or auditing.

Listed companies are subject to a financial reporting scheme as set out in the Securities Trading Act, Securities Trading Regulation and the Continuing Obligations of the Oslo Stock Exchange. This entails, among other things, that all listed companies must publish semi-annual and annual financial reports to the market within certain deadlines. The financial reports must be prepared in accordance with recognised accounting standards, such as IFRS or US GAAP. The company must ensure that no unauthorised persons gain access to accounting information before any such financial report is published.

**ii  Reporting on corporate governance**

The NCCG is based on a principle of ‘comply or explain’ and is thus not directly legally binding upon its target companies. However, pursuant to the Accounting Act, listed companies are required to account for their principles and practice of corporate governance in their annual directors’ report. This requirement is also established in the continuing obligations of listed companies. In addition, companies applying for listing on the Oslo Stock Exchange must report on the company’s corporate-governance principles in their listing application or in an appendix to this.

**iii  Audit**

All public limited companies are required to appoint an authorised auditor. The auditor is elected by the general meeting and serves as auditor until replaced.
The primary task of the auditor is to verify that the company's annual report including its annual accounts is in accordance with applicable legislation. The auditor shall also verify that the company has undertaken satisfactory management of its assets and that proper control mechanisms are in place.

The auditor shall have at least one annual meeting with the board of directors without the CEO being present. In listed companies, the auditor shall liaise with the audit committee, and give the committee a description of the main elements of the audit.

The audit is an important part of the shareholders’ monitoring of the board of directors’ management of the company. The auditor shall present a report concerning the audit to the general meeting. In the event the auditor finds circumstances that may give rise to liability on the part of a member of the board of directors, a member of the corporate assembly or the CEO, the auditor must make a note of this in the report.

The auditor shall attend any general meeting where the matters to be dealt with are of such a character that the auditor’s attendance is deemed necessary. Otherwise, the auditor has, according to law, the right (but no obligation) to be present at the general meeting. However, the NCCG recommends that the auditor attends all general meetings of the company.

IV CORPORATE RESPONSIBILITY

The Public Companies Act confers the ultimate responsibility for the management of the company on the board of directors. The board shall also keep itself informed on the company’s financial position and ensure that the operations, accounts and asset management are subject to adequate control. In performing its duties, the board shall initiate such investigations as it finds necessary, as well as those investigations that may be required by one or more of the directors.

The responsibility of the board of directors is also addressed in the NCCG, which makes it clear that it is also the board’s responsibility to define and perform internal controls with respect to the company’s corporate values, ethical guidelines and guidelines for corporate social responsibility. It is common for listed companies to appoint a special risk committee to the board of directors to monitor risks and report any issues on an ongoing basis.

V SHAREHOLDERS

i Shareholder rights and powers

Norwegian companies’ legislation is based on a majority principle that grants controlling influence to the shareholders controlling the majority of votes at the general meeting. This majority principle provides for a secure and flexible governance system in which an important element is the majority shareholder’s control over the company’s board of directors. However, an important feature of the Norwegian governance model is the balancing of the majority principle against a set of rules relating to minority protection. These rules limit the majority’s authority over individual shareholders (or minority groups of shareholders) and equip the minority shareholders with legal tools to enforce the limitations to the majority’s authority.
Shareholders’ duties and responsibilities

General

The shareholders exercise supreme authority in the company through the general meeting in which they can instruct and control other corporate bodies, including the board of directors and its composition. The general meeting can also, as a main rule, reverse resolutions adopted by other corporate bodies and directly resolve on all company matters to the extent there are no third parties (e.g., contracting parties) who have rights as regards the company that prevent the general meeting from making decisions.

The general meeting is obliged to resolve on matters that are expressly made subject to its authority pursuant to the Public Companies Act, such as adoption of the annual accounts, approval of the board’s statement on remuneration to executive personnel and election of directors to the board. Matters concerning the company’s capital are also generally subject to the general meeting’s authority (i.e., increases and reductions in share capital, mergers, demergers and dividend distributions).

Protection of minority rights

The Public Companies Act has several provisions that balance the majority principle against the interests of the minority shareholders. These minority-protection provisions reflect the fundamental principle of equality in Norwegian company legislation.

The minority-protection rules consists of provisions of various nature, such as general provisions concerning, among other things, abuse of authority, conflict of interests and related-party transactions, as well as provisions regarding majority requirements and procedural requirements for certain resolutions made by the general meeting.

General provision against abuse of authority

The main material limitation on the majority’s authority over the other shareholders is set out in the general anti-abuse provisions in Sections 5-21 and 6-28 of the Public Companies Act. These provisions prohibit the shareholders, the directors and the CEO from adopting any resolution that may provide certain shareholders or others with an unreasonable advantage at the expense of the other shareholders or the company. Further, these provisions prohibit the board of directors and the CEO from effecting resolutions made by superior corporate bodies that would violate mandatory laws or the company’s articles of association.

For listed companies, the anti-abuse provision in the Public Companies Act is supplemented by a provision on equal treatment in the Securities Trading Act and in the Continuing Obligations of the Oslo Stock Exchange.

The anti-abuse provisions are limited in scope to ‘unreasonable’ abuse of majority power that results in unequal treatment. This implies that unequal treatment per se is not prohibited, and that majority shareholders as well as the board and the CEO can pass resolutions that provide for de facto unequal treatment as long as there is a good and valid reason for passing such a resolution.

Shareholder activism

The Public Companies Act opens up for various methods of exercising shareholder activism in Norwegian companies, such as:

A right for shareholders holding more than 5 per cent of the share capital of the company to demand that an extraordinary general meeting is held to discuss any specific matter.
b A right to request that the district court initiates an investigation of the company if a proposal to investigate the company’s ‘establishment, management or certain specified matters regarding the management or the accounts’ is supported by at least 10 per cent of the share capital represented at the general meeting.

c A right for shareholders who own at least 5 per cent of the share capital to request that the district court resolves a dividend that is higher than that approved by the general meeting, thus giving minority shareholders a protection against being ‘starved out’ of the company by a dominant shareholder who is keeping the dividend distributions ‘unreasonably low’.

d An unconditional right for all shareholders to be present (either personally or by proxy) at the company’s general meetings.

e A right for all shareholders to have specified matters addressed by the general meeting.

The Public Companies Act also provides each shareholder with a right to information, including a right to receive the annual accounts, the board’s statement and the auditors’ statement and the statement from the corporate assembly. At the general meeting, each shareholder can also demand information regarding circumstances that may be significant for the approval of the annual accounts and the annual report, matters that are presented to the general meeting and information on the company’s economic situation. The shareholders’ right to information is far-reaching and can only be denied to the extent the information demanded cannot be provided without disproportionate harm to the company.

**Proxy advisers**

With respect to the actual voting at the general meeting, a practice of using ‘proxy advisers’ has been increasingly adopted during the past decade, most commonly by institutional shareholders. The proxy advisers are professional analysts who provide advice on how the shareholders should exercise their voting powers at the general meeting. The advice can either be provided based on the shareholders’ expressed ownership principles, or be of a more general nature. The proxy advisers help the shareholders stay up to date on their investments by taking on the task of analysing the consequences of the matters that are presented to the general meeting. However, critics are concerned that extensive use of proxy advisers causes unwanted harmonisation of the governance of Norwegian companies, which does not always take into consideration the specific needs of a company’s business and operations.

**Proxy battles, shareholder campaigns, etc.**

Prominent proxy battles and shareholder campaigns in relation to Norwegian companies listed on Oslo Stock Exchange are rarely seen. Occasionally such campaigns and battles ensue in the context of a hostile takeover bid, or more recently in relation to companies in financial distress, where creditors of a distressed company may try to influence shareholders and management to agree to a particular proposal for the financial restructuring of the company.

iv **Takeover defences**

Takeover defences in the form of ‘poison pills’ and similar measures are rarely seen in the Norwegian market.

As a starting point, the Securities Trading Act, the NCCG and the Listing Rules of Oslo Stock Exchange builds on a principle that the shares of a listed company should be freely transferable and carry equal rights in the company, and that it should be up to
the shareholders – not the board of directors – to consider any bid made for the shares of
the company by a third party. Consequently, Section 6-17 of the Securities Trading Act
restricts the board’s ability to take defensive measures against a third party tender offer for
the company’s shares, including by issuing new shares, selling or buying significant assets,
purchasing own shares and resolving mergers. These prohibitions can, however, be set aside
by a vote of the shareholders in a general meeting.

The NCCG goes even further and states, among other things, that the board of
directors should publicly announce how it will act in the event of a tender offer for the
company’s shares, and that the company should not take any measures to prevent such an
offer from being made. In the event that the board has been authorised by the shareholders to
take defensive measures in such a situation, the NCCG recommends that the authorisation
should only be acted on if it has been given after the relevant offer has become publicly
known.

Hostile takeovers are rare in the Norwegian market, but there have been examples of
such transactions in recent years where the board of the target company has implemented a
variety of defensive measures to secure a more competitive offer.

As an alternative to active, defensive measures against tender offers, it is possible to
implement ‘structural defences’ in the form of voting restrictions, multiple share classes and
similar means. The Oslo Stock Exchange has historically been reluctant to accept the listing
of companies with such structural defence mechanisms, but there have been several examples
in recent years of companies with restrictions on voting rights or dual share classes having
been accepted for listing. It is difficult to say whether these cases are rare exceptions to the
main rule or if they can be seen as precedents and indications of a less restrictive approach
being taken by the Oslo Stock Exchange in recent years and going forward.

v Contact with shareholders

Outside the general meeting, the shareholders do not have formal authority to govern the
company or to instruct the board of directors or to influence the company affairs. This does
not, however, prevent the shareholders and management from having contact outside the
general meeting when it comes to matters unrelated to the exercise of the shareholders’ legal
authority. Oppositely, such contact is rather common in companies with one dominant
shareholder and is often also seen in companies with dispersed ownership, as the main
shareholder or main shareholders will have a need to be kept informed and up-to-date
on important matters related to the company's operations and development. In addition,
main shareholders may also wish to give their input regarding the company's operations to
management, and management may need to discuss matters with the main shareholder or
main shareholders to avoid falling out of step with them on important matters regarding the
company. In matters in respect of which the general meeting has the final authority, such as
resolutions on share issues, share buy-backs, mergers and demergers, the management will
usually have discussed the matter with the main shareholder or main shareholders before
a reasoned proposal is presented to all shareholders (which needs to occur at least 21 days
before the general meeting is held).

The extent and substance of the contact between management and the shareholders
vary to a great extent from one company to another. In any case, it is important that informal
contact between management and the company's shareholders is kept within certain limits
to make clear that it is the company's management, namely its board of directors and CEO,
which has the responsibility and authority to manage the company's operations. Contact with
the shareholders should thus principally be of an informative nature and with the company’s best interests in mind. To the extent that shareholders present comments or proposals to the management outside of the general meeting, such comments or proposals cannot be of an instructive character. It is also important to ensure that the contact between management and the main shareholders does not violate the other shareholders’ rights in the company and that the contact is kept within the framework of, among other things, the principle of equal treatment of shareholders. To this end, the board and management must be particularly cautious not to disclose information to the main or dominant shareholders without providing the same to the minority shareholders.

The NCCG recommends that the board of directors of listed companies establish guidelines for the company’s contact with shareholders other than through general meetings. Such guidelines will typically specify how the company communicates to its shareholders and stakeholders in the public domain (for instance, by hosting webcasts or telephone conferences in connection with the publication of annual or interim accounts), the frequency of such communications, and the person or persons responsible for the communications (for instance, an investor relations manager).

It is not per se unlawful for a listed company to disclose confidential inside information to one or a select few of its shareholders outside of a general meeting. Depending on the circumstances, there may be good and valid reasons for sharing inside information with a major shareholder, for instance in cases of financial distress. It is, however, important to note that, if a shareholder receives inside information, the shareholder will become an ‘insider’ pursuant to the Securities Trading Act. This means, among other things, that the shareholder will be prohibited from trading in the shares and will be obliged not to disclose the information. A shareholder with inside information must be added to the company’s list of insiders, and the company must inform the shareholder of this fact as well as the consequences of receiving inside information.

VI  OUTLOOK

The Norwegian corporate governance structure has been rather stable for some time, and legislative amendments that will materially affect the corporate governance regime are not expected.

The Norwegian governance model is broadly drafted and flexible and thus caters for many different ownership models. This means that it can be suitable for both companies with a dominant shareholder and companies with dispersed ownership.

In recent years, the actions of directors and management of publicly listed companies in Norway have become subject to increased scrutiny by regulators and the general public, in particular as allegations of corruption and unlawful business practices have been made against several large Norwegian corporations. Statistics also show that director liability lawsuits by aggrieved shareholders and third parties have increased in recent years, prompting an increased focus on directors’ responsibilities and potential liability in general.
I OVERVIEW OF GOVERNANCE REGIME

i Legal framework: sources of law

In Poland, general corporate governance rules applicable to companies, including listed companies, are laid down in the Commercial Companies Code of 2000 (CCC), which replaced the former Commercial Code of 1934. The CCC sets out the general duties and powers of the various corporate bodies, as well as rules on representation, conflicts of interest and the liability of management board members.

As regards listed companies, further rules are contained in the following acts:

a the Act on Public Offering and Conditions for Introducing Financial Instruments to the Organised Trading System and Public Companies, which includes rules regarding takeover offers and general duties of listed companies;

b the Act on Trading in Financial Instruments, which contains provisions on disclosure of non-public information that could affect the market in respect of a listed company’s shares and a prohibition on insider trading;

c the Accounting Act, which contains rules regarding financial reporting and disclosure; and

d the National Court Register Act, which contains rules on filings with the public register of companies.

Compliance with the above rules can, if necessary, be enforced through the courts and, with respect to the capital market regulations, by the Financial Supervision Authority. The significant role of registry courts in respect of the National Court Register goes far beyond the mere authority to maintain the public registers. Under certain circumstances, the registry courts may decide to dissolve a company (although this is very rare in practice). Companies with state participation fall additionally under special regime introduced by the Act on the Management of State Property, which entered into force on 1 January 2017.

ii Legal framework: best practice relating to the governance of listed companies

Alongside the above statutory rules, companies listed on the Warsaw Stock Exchange (WSE) are also expected to follow corporate governance rules adopted by the WSE. The first formal document containing these rules was adopted by the WSE in early 2000 and entered into force in 2002. Since then, it has been revised regularly and adapted to the needs of the
growing Polish capital market. The most recently adopted Best Practice of WSE Listed Companies 2016 (Best Practice Code) came into force on 1 January 2016. These rules apply on a voluntary basis (i.e., as soft law).

In contrast to the version that was in force from 2008 to 2015, the latest Best Practice Code uses a legislative approach adopted in the UK Corporate Governance Code (formerly the Combined Code) and repeated in the EU model of corporate governance rules, consisting of general principles followed by detailed guidelines. The absence of such general principles in the earlier Best Practice Code was heavily criticised. In particular, it was emphasised that without general principles, the Best Practice Code was essentially just a manual providing a set of technical rules. Apart from seeking to protect shareholders’ interests, the current version permits the rules to be better understood and properly applied, which serves the interests of all members of a company’s governing bodies.2

Compliance with the Best Practice Code is monitored by the WSE, and listed companies have certain disclosure obligations in this regard based on the comply or explain model.

There are separate best practice rules that apply to companies listed on New Connect, a stock exchange for smaller companies that is generally subject to less stringent rules and oversight.

Financial institutions are also obliged to implement the current Corporate Governance Rules for Supervised Institutions issued by the Financial Supervision Authority, which have been in force since 2014.

II CORPORATE LEADERSHIP

In Poland, only joint-stock companies can be listed. The relevant regulations of the CCC provide for a mandatory two-tier board structure for joint-stock companies that consists of a management board and a supervisory board.

i Board structure and practices

Composition, appointment and dismissal

Management board

The management board of a company must have at least one member (with no applicable maximum number of members unless otherwise specified in the articles of association). Only individuals can be members. In particular, another company may not be appointed to the management board.

If a fixed or a minimum number of management board members is provided in the articles of association and that number of members is not appointed, even temporarily, then the ability of the management board to validly represent the company may be compromised. To avoid any such issues, most companies have articles of association specifying that the management board consists of one or more members.

The competence to appoint, remove or suspend a management board member is vested in the supervisory board, unless the articles of association of the relevant company provide otherwise (e.g., by stipulating that the management board members are appointed

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by way of a shareholders’ resolution or by conferring rights on a certain shareholder to make nominations). Management board members may always be removed or suspended by the shareholders at a general meeting.

Following the amendment of the CCC, which entered into force on 1 January 2017, the articles of association or a resolution of a general meeting may stipulate certain criteria that should be met by a management board candidate, or may provide a detailed qualification procedure.

It is possible to temporarily appoint one member of the supervisory board to the management board. Such an appointment (which is an exception to the general division of functions between company bodies and the non-compatibility rule described below) is only allowed for up to three months and is only used in exceptional circumstances (e.g., after the resignation of a management board member and before the appointment of a new candidate).

The Best Practice Code provides that management board members should be of high quality and experienced, and the overall composition of the board should ensure diversity as regards matters such as gender, age, education and professional background.

Generally, no minimum term applies to the appointment of management board members, although a single term of office cannot exceed five years. Reappointment for a subsequent term cannot be made earlier than one year before the end of the current term of office. If the articles of association do not provide any specific term of office, the mandate of a management board member automatically expires, at the latest, on the date of the general meeting approving the financial statements for the final full financial year of service of the relevant management board member. Similarly, if a term of office is specified in the articles of association, the mandate of a management board member expires upon approval of the financial statements for the final full financial year of that term. In 2016, the Supreme Court ruled that, for these purposes, the final full financial year is the final financial year that commenced during the term of office.³ The ruling brought an end to debate in the legal doctrine with regard to that aspect of the interpretation of the regulation. This is an important development because miscalculation of the expiry of mandates of management board members could have significant consequences. In particular, a management board member without a valid mandate cannot validly represent the company, and as such, the effectiveness of any acts undertaken by a management board member after the expiry of the mandate could potentially be brought into question, sometimes years later. Following the amendment of the Civil Code adopted in 2018, from 1 March 2019 onwards it will be possible for a company to confirm legal acts undertaken by the member or members of its management board without a valid mandate (similar to acts of a falsus procurator). This brings an end to a discussion regarding the controversies regarding whether such a possibility exists with respect to acts undertaken by a company’s organs.

The articles of association may provide for a joint term of office of the management board members. In such cases, the mandates of all members generally expire at the same time, even if a particular management board member was appointed during the term of office.

A management board member may generally be removed without reason at the discretion of the general meeting or other nominating body. However, the articles of association may limit this right to circumstances in which there are valid reasons for removal.

³ Resolution of the Supreme Court dated 24 November 2016, III CZP 72/16; although it concerns members of the supervisory board, the ruling is also relevant to management board members because of the similar statutory regulations in respect of the terms of office.
Supervisory board

The supervisory board of a listed company must consist of at least five members, and there is no maximum unless otherwise specified in the articles of association. Because of the division of functions between the management board and the supervisory board, it is not possible for a management board member to be a supervisory board member at the same time. The same restrictions apply to a commercial proxy, a liquidator, a manager of a branch office of the company and certain other persons employed by the company.

Members of the supervisory board are generally appointed and dismissed by way of resolutions at a general meeting. Irrespective of the appointment rules specified in the articles of association, the regulations of the CCC provide a special appointment procedure designed to protect the interests of minority shareholders. Shareholders representing at least one-fifth of the share capital may request that the election of the supervisory board at a general meeting take place by voting in separate groups. Shareholders may create groups by division of the total number of shares represented at the general meeting by the number of supervisory board members to be appointed. Each group may then elect one supervisory board member.

The recommendations of the Best Practice Code regarding the composition of the management board and diversity are equally applicable to the supervisory board. Additionally, at least two members have to fulfil the independence criteria described in the Commission Recommendation on the role of non-executive or supervisory directors of listed companies and on the committees of the (supervisory) board. Neither an employee of the company, a subsidiary or an affiliated company, nor a person holding at least 5 per cent of the shares in the company, can be regarded as independent for these purposes. The new Act on auditors and auditors’ firms that entered into force 2017 introduced further criteria for part of the supervisory board members in listed companies. Under this Act, an audit committee appointed by the supervisory board from its own members is obligatory in such companies. The audit committee members (there must be at least three of them), being supervisory board members at the same time, apart from fulfilment of the independence criteria must have knowledge and skills in the scope of the industry in which the company is operating, whereby at least one of them must have knowledge and skills in the scope of accounting or examination of financial statements.

The rules regarding the term of office and expiry of the mandate of a supervisory board member are the same as for the management board members as described above.

Legal responsibilities and representation

Management board

The competence to represent a company in relation to third parties generally lies with the company’s management board. Specifically, management board members are entitled to represent the company in relation to third parties in all judicial and extrajudicial matters. The representation rules specified in the articles of association may provide for either joint or

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4 2005/162/EC.
5 Act on Statutory Auditors, Audit Firms and Public Oversight of 11 May 2017.
6 Articles 128 Section 1 and 129 Sections 1, 3 and 5 of the Act on Statutory Auditors, Audit Firms and Public Oversight of 11 May 2017.
individual representation. The rules on joint representation may provide that the company can be represented by a management board member acting jointly with a commercial proxy. The notion of commercial proxy in Poland is similar to that of Prokura in Germany.

As a general rule, each management board member is responsible for the day-to-day management of the company.

The competence of the management board to manage the company’s business may, to a certain extent, be limited. In particular, it may be subject to a list of reserved matters for which the consent of the supervisory board or the shareholders by way of resolution at a general meeting is required. In such situations, the supervisory board role is strengthened or the shareholders in general meeting are more involved in crucial decisions concerning the management of the company. However, exceptionally detailed or exhaustive catalogues of reserved matters for the supervisory board may not be permissible because, in practice, the need for the approval of the supervisory board may be tantamount to it giving binding instructions to the management board, which is prohibited.

In the course of performing their duties, the management board members are obliged to act with due care necessitated by the professional nature of their activity. In 2012, the Court of Appeal in Poznan emphasised7 that a management board decision can be made based on analyses prepared by the company’s employees or opinions of external persons who have the required special knowledge. However, simply entrusting other persons with an issue is not on its own sufficient to fulfil the obligations of due care of a management board member. In particular, the responsibility for decision-making cannot be shifted to a subordinate.

The management board members have fiduciary duties towards the company and are obliged to act in the interests of the company. Following a resolution of the Supreme Court in 2009, it is clear that the interests of the company are not independent and abstract from the interests of the shareholders, but the interests of the shareholders should be taken as a whole.8

Supervisory board

The supervisory board exercises ongoing supervision of all the company’s activities. For that purpose, the supervisory board members may inspect all the company’s documentation and request information from the management board and the company’s employees.

The specific responsibilities of the supervisory board include, in particular, evaluating annual financial statements, annual management board reports and motions from management concerning decisions on the company’s profits or losses. The supervisory board provides the shareholders with an annual written report on the results of the evaluation. The basic scope of supervisory board responsibilities may be extended and include, among other things, reserved matters for which management is obliged to get supervisory board approval.

The powers of the supervisory board also include suspending (but only for significant reasons) an individual or all management board members from their duties and temporarily appointing supervisory board members to the management board (for a period no longer than three months) to perform the duties of management board members who were dismissed, who resigned or who are incapable of performing their duties for other reasons. The supervisory board is not entitled to issue binding instructions to a management board member and the supervisory board members cannot represent the company in relation to third parties, except in relation to agreements or disputes with the management board members.

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7 Judgment of the Court of Appeal in Poznan – I Civil Division dated 11 October 2012, I ACa 336/12.
8 Resolution of the Supreme Court – Civil Chamber dated 22 October 2009, III CZP 63/09.
Supervisory board and management board

Delegation of board responsibilities

The supervisory board members generally act jointly. Indeed, the regulations of the CCC explicitly apply a collectivity principle to the activities of the supervisory board. In accordance with this principle, a supervisory board member cannot act individually without the prior authorisation of the entire supervisory board. However, the supervisory board may delegate an individual supervisory board member to undertake certain specific supervision activities.

As a general rule, and unlike the supervisory board members, each management board member is responsible for the day-to-day management of the company. The management board is entitled to issue its own by-laws regulating its internal operation, unless the authority to issue the by-laws is granted under the articles of association to the supervisory board or to the shareholders in a general meeting.

The by-laws may provide for the delegation of certain areas of the company’s operations to individual management board members. However, the delegation of functions within the management board does not relieve the other management board members of their responsibility for those functions. Management board members are obliged to control each other and prevent a negative outcome for the company (horizontal control). According to the Best Practice Code, such an internal division of responsibilities should be clear and unambiguous and published on companies’ websites.

Roles of the chair

There is the possibility to appoint one of the management board members as the president of the management board. However, unless provided otherwise in any management board by-laws or the articles of association, no particular duties or powers apply to the president. As such, this function is not necessarily the same as or comparable to the position of a CEO or president of a US corporation.

In the case of a supervisory board, there is often a chair and a deputy chair. Unless explicitly granted additional powers (e.g., a decisive vote if there is no majority on a supervisory board decision), the main power of the chair is basically to open general meetings. Usually, the chair has administrative functions with respect to the supervisory board, such as preparing agendas for and chairing its meetings.

Remuneration

The shareholders should determine the general remuneration policy of the company including, among other things, caps and remuneration systems, as well as any rights of the management board members to participate in the company’s profits. However, the specific remuneration of the management board members is usually determined by the supervisory board.

According to the Best Practice Code, the level of remuneration of management and supervisory board members and key managers of the company should be sufficient for the acquisition, retention and motivation of persons with the qualities and range of competences generally required by the company, as well as being adequate with regard to the specific tasks and any additional functions discharged by the relevant individual.
III DISCLOSURE

According to accounting rules, a listed company is obliged to include a separate statement on corporate governance in its annual management board report. These statements are subject to review by an external auditor. Matters referred to in the Best Practice Code and marked with ‘R’ are recommendations for disclosure in these statements. Instances of non-compliance with matters marked with ‘Z’ fall under the comply or explain principle. Specifically, a listed company has to report cases of non-compliance with matters marked with ‘Z’, whether permanent or incidental, including information on the reasons for non-compliance and the steps to be undertaken to ensure future compliance. The report has to be published on the company’s websites, as well as by the same method employed for ongoing reporting and disclosure. The report has to be published immediately after the non-compliance occurred. Similarly, a report has to be published immediately if the company decides not to apply a relevant recommendation. The Best Practice Code requires that a company explicitly explain the reasons for any non-compliance.

As emphasised by commentators, it cannot be excluded that in certain cases a failure to report non-compliance with a particular recommendation of the Best Practice Code may infringe the obligation to disclose confidential information provided in Article 17 of the Market Abuse Regulation (MAR), which means that such an infringement may potentially be subject to criminal, administrative and civil liability. A failure to report non-compliance with the recommendation to disclose transactions with a shareholder representing 5 per cent of the votes in the company or an affiliated company without supervisory board consent is an example of a situation in which such liability might apply.

IV CORPORATE RESPONSIBILITY

i Risk management and compliance

Polish listed companies are not obliged to adopt any risk management regulations, or to appoint a risk officer or establish a risk committee. Polish law is quite traditional in this respect, making management board members liable for their decisions that exceed the permitted risk doctrine. Responsibilities are usually divided among management board members. According to the Best Practice Code, which is not binding, the internal division of responsibilities for individual areas of a company’s activity among management board members should be clear and transparent, and a chart describing that division should be available on the company’s website.

However, at the same time, according to the Best Practice Code, a company should maintain efficient internal control, risk management and compliance systems, and an efficient internal audit function adequate for the size of the company and the type and scale of its activity. Responsibility for the implementation and maintenance of the above rests with the management board. The staff working in particular units responsible for risk management,
internal audit and compliance should report directly to the president or another member of the management board, and should be allowed to report directly to the supervisory board or the audit committee. A supervisory board, which is obligatory in joint-stock companies, is generally responsible for exercising supervision over a company’s activity. However, listed companies are also required to appoint an audit committee. The audit committee should consist of at least three members appointed by the supervisory board to monitor, among other things:

- the financial reporting process;
- the effectiveness of internal control systems, internal audit systems and risk management;
- the performance of financial audits; and
- the independence of the auditor and the entity authorised to audit financial statements.  

Polish law does not provide for any specific whistle-blowing regulations for listed companies (although provisions regarding whistle-blowing procedures mitigating anti-bribery risks are currently subject to parliamentary works). Obviously, auditors responsible for examining a company’s financial statements and books play an important gatekeeping role. Nonetheless, there is a general trend towards implementing internal whistle-blowing systems in line with the compliance regulations introduced by corporations internally. At present, almost every listed company has such internal procedures in place, or is in the process of adopting the same.

The implementation of internal compliance and risk management regulations is also becoming increasingly common in the market because of new laws that allow the imposition of very high penalties on corporations and their managers, while at the same time extending their corporate liability. For instance, EU Regulation 2016/679 on the protection of natural persons with regard to the processing of personal data and on the free movement of such data allows corporations to be penalised for infringements with administrative fines of up to €20 million, or, in the case of an undertaking, up to 4 per cent of the total worldwide annual turnover of the preceding financial year, whichever is higher; 14 and the MAR, 15 which, in certain circumstances described therein, allows the imposition on legal persons of a penalty of €15 million or 15 per cent of the total annual turnover of the legal person according to the most recent available accounts approved by the management body. In certain cases, EU regulations are transposed into Polish law, for example, in relation to liability in cases of unintentional infringement of competition and consumer protection law, which may be penalised with an administrative fine of up to 10 per cent of the turnover achieved in the financial year preceding the year in which the fine is imposed. 16

The visible practice of the implementation of risk management and internal compliance regulations is a sign that the tone from the top (i.e., ethical business standards set by top

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13 See Article 130 Section 7 of the Act on Statutory Auditors, Audit Firms and Public Oversight of 11 May 2017.
15 See footnote 8.
management) is slowly but steadily breaking through to Polish corporate society. However, as usual, reality is different from theory, since it is created by managers who are not always appointed as a result of a contest.

**ii Corporate social responsibility**

We observe a general tendency for higher expectations among corporations: increasingly, more businesses and their top management focus not only on gaining financial profit, but also on supporting values and goals promoted and supported worldwide. An example of these values and goals is described in the UN 2030 Agenda for Sustainable Development, raising such issues as affordable, decent work and economic growth, and partnerships between governments, the private sector and civil society. A more detailed example of cooperation between the private and public sectors and their joint cooperation is the Paris Agreement on climate change adopted during the UN conference held in 2015 in Paris.

These trends are also visible from the Polish perspective, and Polish corporations are expected to live up to a set of general social, economic and climate expectations. However, no general corporate responsibility rules are implemented in this respect, especially in corporate law. What is being introduced internally for all company’s employees, managers and members of supervisory boards are certain ethical and business conduct standards.

**V SHAREHOLDERS**

**i Shareholder rights and powers**

**Equality of voting rights**

A company may issue either registered or bearer shares. By definition, a listed company is a company in which at least one share is dematerialised. Currently, only bearer shares may be dematerialised. In this context, it should be noted that in light of recent amendments to the CCC and the Act on Public Offering and Conditions for Introducing Financial Instruments to the Organised Trading System and Public Companies, entering into force on 1 January 2021, all issued shares, including shares in non-listed joint stock companies and partnerships limited by shares, will be subject to obligatory dematerialisation due to the introduction of the shareholders’ register.

Except for silent shares (non-voting shares), only registered shares may be preference shares. As a rule, the preference may concern in particular the voting right the right to dividends; or the distribution of a company’s assets in the event of its liquidation.

A single share may carry no more than two votes. In the event that such a share is changed into a bearer share or disposed of in breach of certain reserved conditions, the privilege expires. While the voting preference does not apply to listed companies, before the CCC was adopted listed companies were also allowed to issue preference shares, and therefore they may still exist in the Polish market.

17 Article 334 Section 1 of the CCC.
20 Article 351 Section 2 of the CCC.
The powers of shareholders to influence the board

The general meeting and the supervisory board may not give binding instructions to the management board concerning the running of the company’s affairs.\(^{21}\) (This regulation is limited only to internal relations within the company since, from the point of view of outside relationships, the right of management board members to represent the company may not be restricted with a legal effect with respect to third parties.\(^{22}\)

The above reflects the principles governing joint-stock companies, such as the principle of separation of capital from management and the principle of the presumption of competence of the management board. This also supports the principle that liability is related to those who make decisions.\(^{23}\) The discussed regulation does not preclude the right of the general meeting or the supervisory board to give non-binding guidelines and advice (i.e., suggestions on taking a position or other recommendations). However, a board’s failure to comply with such guidelines does not render board members liable for damages and should not constitute a valid reason to dismiss a board member if the articles of association limit the right of dismissal only to valid reasons.\(^{24}\) In practice, articles of association rarely make such provision, and therefore board members must take into account that they can be dismissed in such cases. Furthermore, there is a general rule that, in relationships with the company, members of the management board shall be subject to restrictions set forth in the CCC, articles of association, management board by-laws, and resolutions of the supervisory board and the general meeting.\(^{25}\) Thus, the general meeting may actually influence the management board if competence for this is included in the articles of association.

It is noted, however, that the above-mentioned right is reserved for the shareholders’ meeting and not individual shareholders. The rights of individual shareholders are limited to the right to information, and not the right to influence the board.

Decisions reserved to shareholders and subject to shareholder approval

Pursuant to the CCC, the shareholders’ consent is required for the following:

\(a\) examination and approval of a management board report on the company’s operations, financial statements for the previous financial year, and granting a vote of approval to members of the company’s bodies for the discharge of their duties;

\(b\) decisions concerning claims for redressing damage inflicted upon the formation of the company or exercising management or supervision;

\(c\) disposal or lease of the enterprise or an organised part thereof, and establishment of a limited right \(\text{in rem}\) thereon;

\(d\) acquisition and disposal of real property, perpetual usufruct or an interest in real property, unless the articles of association provide otherwise;

\(e\) issue of convertible bonds or senior bonds and issue of subscription warrants;

\(f\) acquisition of own shares and authorisation to acquire the same under the circumstances set forth in the CCC; and

\(^{21}\) Article 3751 of the CCC.

\(^{22}\) Article 372 Section 2 of the CCC.


\(^{24}\) Ibidem.

\(^{25}\) Article 375 of the CCC.
The following also require a resolution of the general meeting: contracts for the acquisition of any assets for the benefit of the company (including the acquisition of property from the controlling company or from a subsidiary company or cooperative), for a price higher than one-tenth of the paid-up share capital, from the company’s founder or shareholder, or for a subsidiary company or cooperative from the company’s founder or shareholder, executed prior to the lapse of two years from the company registration.

The foregoing does not apply to the acquisition of assets on the basis of the provisions of law concerning public procurement, liquidation, bankruptcy and execution proceedings, and to the acquisition of securities and commodities on the regulated market.

The articles of association may specify other matters reserved to the competence of the shareholders’ meeting. While the absence of a shareholders’ resolution required by the articles of association does not make a particular action invalid, neither does it preclude the liability of members of the management board towards the company for violation of the articles of association. Furthermore, the absence of a shareholders’ resolution required by the provisions of the CCC (which may be granted two months after the action at the latest) does entail the invalidity of an action.

**Rights of dissenting shareholders**

The CCC and other regulations applicable to listed companies provide for the principle of majority rule. Nonetheless, minority shareholders are to some extent protected and are vested with rights aimed at guaranteeing them a certain influence in company matters.

For instance, at the request of a shareholder or shareholders in a public company holding at least 5 per cent of the total vote, the general meeting may resolve to mandate an expert to review, at the company’s expense, a specific issue relating to the company’s incorporation or the conduct of its business (a special-purpose auditor). To this end, the shareholders may request that an extraordinary general meeting be convened or that the adoption of such a resolution be placed on the agenda of the next general meeting. The management board and the supervisory board of the public company shall provide the special-purpose auditor with the documents specified in the resolution of the general meeting or in the court’s decision to appoint the special-purpose auditor, and shall also provide all the explanations necessary for the performance of the review.

Furthermore, minority shareholders have the right to appoint members of the supervisory board by a vote in separate groups, which may be executed at the request of shareholders representing at least one-fifth of the share capital, even if the company’s articles of association provide for a different manner of appointing the supervisory board. As a result of the aforementioned regulation, the minority shareholders representing at least 20 per cent of votes may have their representative appointed to the supervisory board.

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26 Article 393 Section 1 of the CCC.
27 Article 394 Section 1, 2 and 4 of the CCC.
29 Article 385 Section 3 and 9 of the CCC.
Facilities for long-term shareholders

Polish law does not provide for any specific facilities (such as extra votes or extra dividends) for long-term shareholders, except for the option to obtain preference shares incorporating a right to a dividend on advantageous terms compared with other shareholders. For example, shares carrying special dividend rights may entitle the holder to a dividend that exceeds by no more than one-half the dividend to be distributed to holders of non-preference shares. Shares carrying special dividend rights do not enjoy priority of satisfaction over other shares and may be deprived of voting rights (non-voting shares).\(^{30}\)

ii Shareholders’ duties and responsibilities

Controlling shareholders’ duties and liability

Polish law does not impose any special requirements on controlling shareholders apart from the obligation (which applies to all shareholders) to notify the Financial Supervision Authority and the company about reaching or exceeding a particular percentage of the total votes in a company or a change in the share of votes held in excess of 10 per cent of the total votes by at least:

- a 2 per cent of the total votes in a public company, the shares of which have been admitted to trading on the official stock exchange listings; and
- b 5 per cent of the total votes in a public company, the shares of which are admitted to trading on another regulated market, or a change in the share of votes held in excess of 33 per cent of the total votes by at least 1 per cent of the total votes.

Furthermore, the majority shareholder is obliged to purchase shares of the minority shareholders under the buyout procedure.\(^ {31}\) A shareholder or shareholders representing not more than 5 per cent of the share capital may demand that the agenda of the next general meeting include the issue of adoption of a resolution on the compulsory buyout of their shares by no more than five shareholders holding, in aggregate, no less than 95 per cent of the share capital, where each of them holds no less than 5 per cent of the share capital (majority shareholders).

Institutional investors’ duties and best practice

Neither the CCC nor the Act on Public Offering and Conditions for Introducing Financial Instruments to the Organised Trading System and Public Companies provide for any regulation specifically relating to institutional investors; nor is there any specific best practice code for such investors or other shareholders besides the Best Practice Code.

According to the Best Practice Code, the general meeting should deliberate with respect to the rights of shareholders and make sure that the resolutions do not infringe upon legitimate interests of various groups of shareholders. Moreover, the shareholders participating in the general meeting are obliged to exercise their powers in a manner not prejudicial to good practice.

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\(^{30}\) Article 353 Section 1-3 of the CCC.

\(^{31}\) Article 418(1) of the CCC.
iii  Shareholder activism

Say on pay

There is no general rule that a company’s shareholders have the right to vote on the remuneration of executives. Save as otherwise provided in the company’s articles of association, according to the general rules provided in the CCC, the supervisory board sets the remuneration of management board members employed under employment contracts or other contracts, and the general meeting may authorise the supervisory board to establish that the remuneration of members of the management board shall also include the right to participate, in a specified manner, in the company’s annual profit allocated for distribution among the shareholders. Obviously, the company’s articles of association may provide that the rules of the remuneration are determined by the shareholders.

The Best Practice Code specifies only that companies have a remuneration policy at least for management board members and key managers. The remuneration policy should specify, in particular, the form, structure and method of determining the remuneration of members of a company’s bodies and its key managers.

Derivative actions

Under Polish law, if a company fails to file a statement of claim for redressing damage within one year of the disclosure of the act resulting in the damage caused to the company, each shareholder or person otherwise entitled to participate in profit or in distribution of assets may file a statement of claim for redressing the damage suffered by the company (actio pro socio).32

Furthermore, a shareholder has the right to file a statement of claim to repeal or declare a resolution of the general meeting invalid if:

a  the shareholder voted against the resolution and, upon the adoption thereof, requested that his or her objection be recorded in the minutes. The voting requirement does not apply to shareholders holding a non-voting share;

b  the shareholder was prevented from participating in the general meeting without a sound reason; and

c  the shareholder was absent from the general meeting, only in the event of a defective convening of the general meeting or adoption of a resolution on a matter not included in the agenda.

Any resolution of the general meeting that is in conflict with the provisions of the articles of association or good practice and detrimental to the company’s interest or aimed at harming a shareholder may be appealed against by filing a statement of claim against the company to repeal the resolution. A statement of claim against the company to declare a resolution of the general meeting invalid may be filed if the resolution was adopted in breach of the law. Both proceedings may only be commenced within statutory periods.

Proxy battles

Polish law does not set out any regulations that would prohibit shareholders from joining forces and gathering enough shareholder proxies to win a corporate vote. It is a strategy that often accompanies takeovers.

32  Article 486 Section 1 of the CCC.
Formally, the right to appoint a proxy at the general meeting and the number of proxies cannot be limited. A proxy exercises all rights of the shareholder at the general meeting unless the power of attorney provides otherwise. A proxy may grant a further power of attorney if the power of attorney so provides. A proxy may represent more than one shareholder and vote differently under the shares held by each shareholder. A shareholder holding shares registered on a collective account may appoint separate proxies to exercise the rights attached to the shares registered on this account. A shareholder holding shares registered on multiple securities accounts may appoint separate proxies to exercise the rights attached to the shares registered on each account.

The provisions on the exercise of a voting right by proxy apply to the exercise of a voting right through another representative.33

Shareholder campaigns
There are no regulations or established market practice regarding shareholder campaigns.

iv Takeover defences
Shareholder and voting rights plans, white-knight defences and other measures
The Takeover Directive34 has not been fully transposed into Polish national legislation, and therefore there are no explicit provisions governing the admissibility of reactive defensive measures that could be undertaken by the management board. It is clear that the shareholders taking over a company are guided exclusively by their own interests rather than the interests of the company, which might be better judged by its management board, representing the next shareholders’ interests, as well as the interests of other persons associated with it (i.e., company stakeholders such as banks, creditors, employees and the state).

Members of the management board generally do not support takeovers since they are likely to lose their positions in the aftermath of a takeover. Therefore, through the prism of their own interests, they opt for taking defensive measures ad hoc. Unfortunately, Polish law does not regulate (neither authorises, nor prohibits, nor requires) the admissibility of reactive defensive measures by the management without the authorisation of the general meeting. Consequently, in principle, and if they are not prohibited by law, defensive measures are allowed, and their exercise depends on the will of the management board members and the actual position of the management board in the company. From a broader perspective, however, it seems that the taking of defensive measures by the management board, and thus exerting influence on the shareholding structure, does not fall within the competence of the management board under the CCC at all.

The regulation aimed at protecting companies against takeovers stipulates an obligation to announce a takeover bid for the sale or exchange of shares. The purpose of the announcement is to allow other shareholders to exit the company or to reduce their involvement therein, and consequently to have one of the investors acquire a stake resulting in the acquisition (change) of control of the company. If the shareholder taking over the company fails to make the announcement and, at the same time, exceeds a certain threshold

33 Article 412 Section 1-7 of the CCC.
34 2004/25/EC.
of the total votes in the company, that shareholder cannot exercise the voting rights attached to the shares. Furthermore, the Financial Supervision Authority may impose a penalty of up to 10 million zlotys on the entity that failed to make the announcement.35

Staggered boards
The rules for the appointment and dismissal of members of the company’s bodies should be described in the articles of association subject to the provisions of the CCC. In the absence of any statutory provision, it would seem that the company’s articles of association may provide for staggered boards. However, according to the statutory rule, members of a company’s bodies may always be revoked by the general meeting. Therefore, staggered boards are not a sufficient solution for takeover defences under Polish law.

v Contact with shareholders
Mandatory and best practice reporting to all shareholders
The mandatory provisions applicable under Polish law focus on the shareholders’ right to information. Compared with the right to information in limited liability companies, this right is limited in joint-stock companies since, together with the right of supervision, it is vested with the supervisory board, which should be appointed within the company.

The main source of information for shareholders is reports, which the company is obliged to publish immediately, or at least no later than 24 hours after the occurrence of or upon becoming aware of a reportable event. Furthermore, pursuant to the provisions of the CCC, in the course of the general meeting, the management board is obliged to provide a shareholder, at the latter’s request, with information concerning the company, if this is justified for the purpose of evaluating an issue included in the agenda. The management board may refuse to provide information if it could inflict damage on the company, an affiliate company or a subsidiary company or cooperative, in particular through the disclosure of technical, commercial or organisational secrets of the business enterprise. A management board member may refuse to provide information if providing it could constitute grounds for criminal, civil or administrative liability of the member. A reply is deemed given if relevant information is available on the company’s website in a place designated for replies to shareholders’ questions.

For important reasons, the management board may provide information in writing outside a general meeting. The management board is obliged to provide information within no more than two weeks of a request being submitted during a general meeting. If a shareholder submits a request for information concerning the company outside a general meeting, the management board may provide the information to the shareholder in writing. In the documents submitted to the next general meeting, the management board is obliged to disclose in writing information provided to a shareholder outside a general meeting together with the date on which the information was provided and the person to whom it was provided. Information submitted to the next general meeting does not have to include information made public and provided during a general meeting.

35 Article 97 Section 1 Item (5) and (5a) of the Act on Public Offering and Conditions for Introducing Financial Instruments to Organised Trading, and Public Companies.
A shareholder refused requested information in the course of a general meeting who has requested that his or her objection be recorded in the minutes may apply to the registration court requesting that the management board be obliged to provide the information.36

According to the Best Practice Code, companies should ensure adequate communications with investors and analysts by pursuing a transparent and effective disclosure policy. To this end, they should ensure easy and non-discriminatory access to disclosed information using diverse tools of communication. The Best Practice Code specifies all the information that should be published on a company’s website.37 Furthermore, if a shareholder requests information concerning the company, the company’s management is obliged to respond to the shareholder no later than within 30 days, or notify him or her of its refusal to provide the information, if the management board made this decision on the basis of Article 428 Section 2 and Section 3 of the CCC.38 All responses should be published on the company’s website.39

Selective meetings and communications: circumstances in which meetings can take place with individual shareholders

The Best Practice Code recommends that companies should allow investors and analysts to ask questions and receive explanations – subject to prohibitions defined in the applicable legislation – on topics of their interests. This recommendation may be implemented through open meetings with investors and analysts, or in any other format allowed by a company.40

It must be underlined that the principle of equality of shareholders should be observed with respect to meetings and the provision of information to shareholders. Issuers of securities admitted to trading on the regulated market are obliged to ensure equal treatment of the holders of securities of the same type in the same circumstances. The foregoing shall not prevent the issuer from redeeming debt securities earlier, pursuant to the legislation of the country where the issuer’s registered office is established, in cases where derogation from the original conditions of issue is necessary in accordance with social priorities.41

Issue of information to shareholders in advance of shareholders’ meetings

Companies should use best efforts, including taking all steps well in advance as necessary to prepare a periodic report, to allow investors to review their financial results as soon as possible after the end of a reporting period.42

Resolutions of the general meeting should allow for a sufficient period between decisions causing specific corporate events and the date of determination of the rights of shareholders pursuant to the corresponding events.43

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36 Articles 428 and 429 of the CCC.
38 See the chapter on mandatory and best practice reporting to all shareholders.
40 Recommendation No. I.R.3.
43 Principle No. IV.Z.14.
As a rule, a periodic report should be published at least 26 days before the general meeting.\textsuperscript{44}

**VI OUTLOOK**

With the Polish national economy constantly growing, it is clear that the public market will evolve. However, because of changes in the law, and particularly the adoption of the MAR, it is quite possible that we will see more delistings than IPOs. The main barriers to the development of the Polish capital market are a limited inflow of capital, a lack of understanding of the market, risk aversion and the choosing of banks for savings. These are the reasons why stock market specialists and advisers underline how important it is to strive for the support and education of listed companies, and to tighten the requirements for small stock companies (i.e., New Connect, small companies stock; and Catalyst, bonds stock).

The corporate market and the listed companies market will also probably be influenced by a substantial change to Polish corporate law planned for a few years, i.e. the introduction of the Polish simplified joint-stock company, which is supposed to be similar to the French société par actions simplifiée or the Slovak jednoduchá spoločnosť na akcie. The respective amendments to the CCC introducing this new type of company should enter into force on 1 March 2020.\textsuperscript{45} The initiative for this regulation came from the idea of creating a new simplified and inexpensive tool for start-up investments. However, this must not be the only goal of the new company structure, which is also supposed to serve other, larger enterprises. The advantages offered by the simplified functioning of the simplified joint-stock company and its financing might attract more investors than the public stock market, where companies and their managers may be penalised with huge administrative fines, such as those provided for in the MAR.

What is more, the new simplified joint-stock company may prove attractive to investors from English-speaking areas given the fact that it enables the establishment of a single tier board of directors familiar to the corporate concepts of British and American law. The legal model of this new type of company also deviates from the traditional concept of protecting a company’s creditors based on the company’s share capital, instead introducing a new flexible model for these companies based on solvency tests preceding payments made to shareholders. It remains to be seen how the simplified joint-stock company form will be welcomed by Polish and foreign investors.

\textsuperscript{44} Section 100.3 of the Ordinance of the Minister of Finance on current and periodic information provided by issuers of securities and conditions for recognising as equivalent information required under the law of a non-Member State.

\textsuperscript{45} Introduction of the Polish simplified joint-stock company may be postponed until 1 March 2021.
I OVERVIEW OF GOVERNANCE REGIME

This chapter refers only to the regulations concerning sociedades anónimas, public companies limited by shares, one of the various forms companies can take under Portuguese law, since this is the most common one among listed companies and medium to large companies.

The Portuguese legal framework regarding corporate governance rules is generally provided for in the Companies Code (PCC) and in the Securities Code (PSC), with sector-specific legislation being also of relevance, namely for financial institutions and state-owned companies.

Soft law instruments need also to be taken into account. The most relevant ones are the recommendations issued by the Securities Commission (CMVM), which are applicable to listed companies but are also used as best practice guidance for other companies, and the recommendations issued by the Portuguese Central Bank (BdP) concerning governance of financial institutions, as well as the Corporate Governance Code (CGC) issued by the Portuguese Institute of Corporate Governance and applicable to companies under the supervision of CMVM, but still on a comply or explain basis.

Recent trends in Portugal concern equal gender representation at board level, namely for listed companies and state-owned companies, as well as the implementation of strategies to increase the quality of companies’ audit and transparency on beneficial ownership of companies.

II CORPORATE LEADERSHIP

i Board structure and practices

Shareholders may choose one of three mandatory governance models, depending on the structure adopted for its management and auditing bodies:

Classic model

The classic model (also known as the Latin model) establishes a single management body corresponding to a sole director (only admissible for companies with a share capital not exceeding €200,000) or a board of directors, with a variable number of members (a minimum of two) as freely defined by the by-laws. Therefore, this model is considered a one-tier structure.
Regarding the auditing body, the PCC foresees the existence of a simple structure or a reinforced structure, depending on the appointment of a sole auditor (which must be a chartered accountant) or of a supervisory board (with a minimum of three members, one of which needs to be a chartered accountant) for the simple structure, or of a supervisory board plus a chartered accountant for the reinforced structure.

The reinforced structure is mandatory for:

\(a\) public limited liability companies, if they exceed, for two consecutive years, two of the following thresholds:

- a total balance sheet of €20 million;
- a total net turnover of €40 million; and
- an average of 250 employees during each fiscal year (i.e., large public companies);

and

\(b\) companies that are issuers of securities admitted to trading on a regulated market.

**Anglo-Saxon model**

The Anglo-Saxon model establishes a single management body, a board of directors, which includes an audit committee. No sole director is admissible in this model.

Regarding the auditing body, the audit committee is composed of at least three directors with non-executive powers who are responsible for supervising the activities of the executive committee (i.e., the members of the audit committee perform similar functions to the ones exercised by the supervisory board under the classic model described above). In this model, the auditing body also includes an external chartered accountant.

In view of the above, the Anglo-Saxon model has the characteristics of a one-tier structure.

**German model**

Under the German model, the management of the company is entrusted to a board of directors composed of a variable number of executive directors only, in accordance with the by-laws, or to a sole director (only admissible for companies with a share capital that does not exceed €200,000). The directors may be appointed by the general and supervisory board or by the shareholders’ general meeting, if provided by the by-laws.

The general and supervisory board combines typical competences of the supervisory board and of the shareholders’ general meeting. Even though it does not have management powers, there are certain categories of management acts to be adopted by the board of directors that can be subject under the by-laws of the company to the prior consent of the general and supervisory board. Therefore, this model is a two-tier structure. The number of members of the general and supervisory board is set out in the by-laws, and shall be higher than the number of directors.

In this model, the auditing body also includes an external chartered accountant.

In the case of listed companies and large public companies, the creation by the general and supervisory board of a committee for financial affairs is mandatory.

Although the classic model is predominant in the Portuguese corporate landscape, listed companies and large public companies are adapting their corporate structures to the Anglo-Saxon model, which is perceived to better address the corporate governance guidelines issued and enforced by CMVM and by the BdP.
**Board of directors structure and practices**

The board of directors is responsible for managing the activities of the company. However, members of the audit committee in the Anglo-Saxon model are legally prevented from carrying out executive tasks.

The company’s by-laws may authorise the board of directors to delegate the day-to-day management of the company to one or more directors (executive directors) or to an executive committee (in the classic model and Anglo-Saxon model only), the latter being recommended under the CGC.

Moreover, the board of directors may also grant powers to a specific director or several directors to deal with certain aspects of the management of the company, unless the by-laws prohibit this scenario.

Also very common, namely in large stock companies and listed companies, and in accordance with the CGC, is the creation of special committees by the management body, with or without the participation of its members, and with duties to assist on specific matters.

The chair of the board of directors, to be appointed by the board of directors unless the by-laws attribute such choice to the shareholders’ general meeting, may be entitled with the casting vote whenever the board is composed of an even number of directors or if provided by the by-laws. The chair is also responsible for convening board of directors’ meetings and chairing them. Although under the PCC there is no requirement for the roles of CEO and chair to be attributed to different persons, the CGC recommends that, if the chair is an executive director, then mechanisms for the coordination of the non-executive directors are effectively put in place.

Representation of the company is also legally attributed to the board, which can, nonetheless, attribute powers to certain directors to execute specific management decisions. However, powers to bind the company are freely defined in the company’s by-laws, rendering any act that is taken by those persons entitled under the by-laws to bind the company without a prior decision of the board of directors valid and binding on the company.

**ii Directors**

**Appointment and dismissal**

In the classic and Anglo-Saxon models, directors are appointed and dismissed by the shareholders’ general meeting, with the supervisory board or the audit committee, respectively, being entitled to suspend directors that are temporarily unable to duly perform their mandate. In the German model, the general and supervisory board is responsible for the appointment, suspension and dismissal of directors, unless the by-laws entrust such powers to the shareholders’ general meeting. However, in any case, listed companies are also required to include in their by-laws a mechanism enabling at least one director to be appointed by the minority shareholders under certain conditions.

Terms of office can run for up to four years, as defined in the company’s by-laws and being freely renewed; however, directors remain in office after the lapse of such term until the date on which new directors are appointed, or until the end of the month subsequent to the month in which the director delivered his or her resignation to the company, whichever occurs first.

Directors are required to be natural persons. If a legal person is appointed as a director, it is required to appoint a natural person to act as director for its own name and account, with the legal person being jointly responsible with the natural person for the performance by the second of its director duties.
Independence requirements are only imposed by the PCC in respect of the audit committee. It is required that for listed companies and large public companies, at least one of its members has higher education adequate for the performance of its duties and is knowledgeable in auditing or accounting, and, for listed companies, that most of its members are independent directors (e.g., that they are not associated with any specific set of interests in the company, and that are not in any situation that may hinder the directors’ analysis and decision capacity). In addition, the members of the audit committee are subject to incompatibility provisions, requiring that, among others, they are not members of the management bodies of companies that are in a group relationship with the company where they serve as members of the audit committee.

Under the German model, directors are subject to specific incompatibility requirements, namely being required to not be a member of the general and supervisory board.

However, the CGC recommends that each company should include as non-executive directors an adequate number of independent directors.

In addition, Law No. 62/2017, of 1 August imposes a requirement that listed companies shall have in their management (and supervisory) bodies, as from the first elective shareholders’ general meeting after 1 January 2020, women representing at least 33.3 per cent of the total members of such bodies. This was a measure already recommended by the CGC.

**Duties**

Directors (both executive and non-executive or inside and outside directors) are required to comply with certain legal duties, including a duty of care (availability for the performance of the position, technical skills and knowledge of the company’s activity) and a duty of loyalty (performance according to the company's interest, to the shareholders’ long-term interests and to the interests of the remaining stakeholders).

Non-executive directors are also subject to a special duty of vigilance in respect of the performance of the executive directors.

As such, all directors (both executive and non-executive) are entitled to the same level of information, at the same time, and can request any information from the company as they deem necessary to the adequate performance of those duties.

Other legal duties of directors include an obligation to:

- preserve the share capital and avoid and react to thin capitalisation (loss of more than half of the company’s share capital), upon which directors are legally required to call a shareholders’ general meeting;
- not compete (the director may not pursue, by himself or herself or through entities, activities that are in competition with the activity of the company, unless so authorised by the relevant corporate body);
- prevent any conflict of interests (a director is required to avoid situations in which he or she has or could have an interest that conflicts with the company’s interests, to declare such conflict or potential conflict to the other directors, and is also prohibited from taking part in the relevant decisions that could be affected by such conflict or potential conflict of interests); and
- ensure conformity between actions and respective records and publications.

Compliance with these duties implies that the directors shall not accept a mandate in cases where there is a lack of appropriate personal and professional conditions to carry out the mandate in adequate form (e.g., lack of time or necessary knowledge and preparation to
take on a position); and that they must be duly informed when making decisions, for which directors shall request all necessary information and endeavour to obtain the same, including expert advice.

Moreover, directors must be always mindful of the confidentiality obligation that they owe to the company as directors, and also of their duty to review board documentation and to raise any points of concern, making sure that any points are duly reflected in the minutes of the meeting and ensuring that they vote against any decisions in breach of their duties.

A special assessment should be exercised in transactions entered into between the company and another director or a shareholder of the company (or persons or entities related with them), and also when the company grants any loans or guarantees to persons or entities related to a director or a shareholder.

**Remuneration**

The PCC provides that the corporate body responsible for determining the remuneration of directors varies depending on the corporate governance model of the company, as follows:

a  one-tier management structure models (classic and Anglo-Saxon models): the remuneration of directors is determined by the shareholders’ general meeting or a remuneration committee appointed by the latter; and

b  two-tier management structure model (German model): the remuneration of directors is determined by the general and supervisory board or by its remuneration committee, except if the company’s by-laws specifically attribute such competence to the shareholders’ general meeting or to a remuneration committee appointed by the latter.

In all three governance models, the remuneration of the members of the management body may comprise a fixed and a variable component, the latter including profit-sharing, being the maximum percentage of profits to be attributed to directors, which shall be specifically authorised in the by-laws. However, audit committee members are only entitled to a fixed remuneration (such rule being recommended under the CGC to apply to all non-executive directors).

Law No. 28/2009, 19 June, imposes on public interest entities (as defined in Article 3 of the Annex to Law No. 148/2015, 9 September) disclosure obligations regarding the remuneration policy of the members of the management (and supervisory) body, implementing a say on pay rule.

Under the CGC, further recommendations have been issued with a view to ensure that the remuneration scheme of the company:

a  adequately remunerates directors for the responsibilities that they undertake and the competencies they use for the company’s benefit; is aligned with the company’s long-term interests; and rewards performance;

b  is aligned with the company’s long-term interests; and

c  rewards performance.

**Liability**

Breach of their duties by directors gives cause for civil liability, which shall arise from a court’s decision, and which cannot be limited or excluded by agreement.

Liability of directors is always joint, the law establishing an assumption of fault by directors that may, nevertheless, be warded off if the directors:

a  prove their actions were fault-free;
prove that their actions were performed on an informed basis, free of any personal interest and according to a business judgement criterion;

were not part of the resolution, or voted against it, having expressly recorded in the minutes of the meeting their disagreement; or

based their actions on a shareholders’ resolution.

Directors are required to guarantee their liability by delivering a bond or taking on an insurance policy with a minimum coverage of €50,000 (or €250,000 for listed companies and large public companies); however, such guarantee is legally waived for non-executive directors that are not remunerated as such, and may be waived by the shareholders’ general meeting to other directors (excepted for listed companies and large public companies).

Directors are also subject to tax-related liability (civil or criminal liability), liability over administrative offences, criminal liability and civil liability within the context of insolvency and environmental affairs.

iii Auditing bodies

Company auditing bodies and their tasks vary from corporate model to corporate model. However, broadly speaking, auditing bodies are responsible for the ongoing supervision of a company’s activity, especially financially and accounting-wise, but this is not absolute: for instance, any agreement to be entered into between the company and its directors, if lawful, must be preceded by an opinion of the company’s auditing body.

In addition, the members of the auditing bodies are subject to the same duties of care and diligence as directors in the performance of their mandate, and can likewise be liable towards the company and its stakeholders for breach of such duties.

Considering the tasks vested on the auditing bodies, it is understandable that their members are subject to independence requirements and to incompatibilities (as previously discussed when addressing the audit committee), while the auditors must be certified chartered accountants registered with the Chartered Accountants Association. Such requirements were increased with Law No. 148/2015, of 9 September.

III DISCLOSURE

Directors are required to annually produce and disclose to the shareholders, which approve the same, the accounting documentation of the company, which includes the submission by the board of directors to the shareholders’ general meeting of the annual accounts, the attachments to the annual accounts (where the directors are required to disclose, if the company’s accounts do not follow IFRS rules, all transactions with related parties) and the annual management report (where the directors are required to disclose, among others, the authorisations granted to transactions between the company and its directors, and the financial risk coverage policy of the company).

However, directors are also required to disclose to shareholders other situations, such as if the company is under thin capitalisation (loss of more than half of the company’s share capital), upon which the directors are legally required to call an shareholders’ general meeting. This information needs to be made available to shareholders at the company’s head office and website at least 15 days (21 days for listed companies) before the date of the shareholders’
general meeting, and afterwards needs to be mailed to the shareholders representing at least 1 per cent of the share capital. During the shareholders’ general meeting, the shareholders are also entitled to request information deemed necessary to duly decide.

In addition, shareholders are generally entitled to obtain relevant information concerning the company from the directors if holding, by themselves, at least 1 per cent of the share capital or, together with other shareholders, at least 10 per cent of the share capital. This information is afterwards required to be available to the other shareholders in the company. Failure to provide the information required entitles the shareholders to judicial relief.

For listed companies, further disclosure obligations towards the market are imposed on the company and its directors, including information of an accounting nature (disclosed on a different timely basis) and also any information that may have an impact on the value of the securities being traded (immediately disclosed). There are, however, certain situations that may legitimise a delay in the disclosure of this information to the market.

Notwithstanding CMVM being responsible for organising and making available to the market the information disclosed by the listed companies, such information shall also be included on the company’s website and, preferably, also made available in English.

The PSC also requires that listed companies include in their annual management report:

a. a chapter concerning the company’s corporate governance structure and practices, detailing, among other things, the share capital structure;
b. a chapter identifying limitations on transfers and special rights attributed to shareholders;
c. a chapter outlining the voting rights limitations (even those arising from shareholders’ agreements of which the company is aware);
d. a chapter regarding any relevant agreements entered into by the company and its employees or the members of the corporate bodies; and
e. a chapter identifying the matters included in the CGC with which the company is not complying (including a justification of such non-compliance).

This comply or explain model is of relevance in the assessment of the implementation of the best practices foreseen in the CGC.

Moreover, under the CGC, companies are also urged to put in place a permanent contact with the shareholders, its investors and other market stakeholders in general, and to implement adequate systems to ensure that the relevant information is produced and disclosed in a timely manner to the relevant stakeholders.

IV CORPORATE RESPONSIBILITY

As already discussed, the directors are responsible for disclosing to the shareholders in the annual accounting documentation the financial risk coverage policy of the company, together with a detailed description in the management report of the risks and uncertainties that the company faces or may face, assessing not only financial risks but also other non-financial matters, such as of a labour or environmental nature, which can affect the company’s situation. Therefore, albeit indirectly, directors are always responsible and accountable for risk management, with the auditing bodies also being responsible for the supervision of risk.

Sector-specific legislation requires companies to create risk management mechanisms. For instance, risk management committees are mandatory for credit institutions with a significative dimension, internal organisation and nature, and with a significative scope and
complexity of their activities, which are composed of non-executive directors with specific knowledge adequate to fully understand and monitor the risk strategy of the company. For other credit institutions, the tasks of the risk management committee are carried out by their auditing bodies.

The CGC also requires that companies undertake adequate risk management and internal auditing systems suitable to the dimension and complexity of the risks associated with their activity.

Furthermore, directors are required to perform their mandate to achieve the company’s interest, which results from an assessment of not only the shareholders’ interests, but also the interests of other relevant stakeholders, such as the company’s creditors and employees.

Moreover, and especially regarding listed companies and other large public companies, there is a move towards the implementation of corporate social responsibility programmes with the aim of involving companies in the social concerns of the community.

In addition, concerns about integrity and ethical behaviour in the workplace led to the enactment of Law No. 73/2017, of 16 August, pursuant to which companies with at least seven employees are required to put in place a code of good practice to prevent and combat harassment in the workplace.

V SHAREHOLDERS

i Shareholder rights and powers

The shareholders’ general meeting is composed of all the shareholders with voting rights and to which the more structural decisions concerning the company are attributed (e.g., amendments to the by-laws of the company and distribution of profits). The shareholders’ general meeting may adopt resolutions on matters that are specially assigned to it in the law or in the by-laws and that do not fall within the scope of powers of the other corporate bodies. The shareholders’ general meeting may also deliberate on matters relating to the management of the company when requested to do so by the board of directors.

Each share carries one vote, unless the by-laws foresee either that one vote is attributed only to a certain number of shares if it encompasses all shares of the company and if at least €1,000 of capital is equivalent to one vote; or votes issued above a certain threshold are not considered when issued by a sole shareholder when acting by itself or as a representative of other shareholders. Nevertheless, in the latter case, the CGC recommends that the by-laws foresee the obligation to review such voting rights limitation at least within every consecutive five-year period.

Multiple-vote shares (i.e., shares that grant more voting rights to their shareholders than other shares that also grant voting rights) are not admissible under the law, although certain authors have recently challenged the applicability of this limitation to listed companies, namely if such limitation was eschewed for loyalty-type securities. There is, however, little market practice in the granting of special rights (including rights to privileged dividends) to long-term shareholders.

Shareholders are legally required to vote or abstain using all the shares they hold in the company, and cannot split their voting rights to issue different votes in respect of the same issue.

Dissenting shareholders have the right to exit the company against the payment of a monetary consideration in certain legally defined situations, such as:

\[a\] when the shareholder votes against the transfer of the corporate seat to another country;

or
if the shareholder voted against a merger, demerger, transformation or return to operation of a company after winding-up proceedings are initiated, and such exit right is provided for in law or in the company by-laws.

The inclusion of other exit rights in the by-laws, for which dissenting shareholders would need to rely on mechanisms agreed in a shareholders’ agreement, is not accepted by some scholars.

ii Shareholders’ duties and responsibilities
Shareholders are required to not take part in any decision when, among others, it pertains to any:

- waiver of any obligation of the shareholder, whether as a shareholder or a member of other corporate bodies;
- dispute between the company and the shareholder;
- dismissal, for just cause, of a shareholder as member of a corporate body; or
- any relationship between the company and the shareholder outside the corporate relationship.

Other than the foregoing, and without prejudice to a general duty to act in good-faith, shareholders are not subject to any specific duty of loyalty or diligence towards the company or its stakeholders. There is also no code of best practice for shareholders.

Notwithstanding, shareholders are not entitled to influence the board of directors (unless a decision by the shareholders on managerial matters is requested by the board), and any shareholders exerting such influence (i.e., shareholders that by themselves or under a shareholders’ agreement have the right to dismiss a director and have determined such person to act or not act in a certain way) will be, with the influenced director, jointly liable towards the company, its shareholders and its creditors for such influence if a decision detrimental to the company’s own interests is adopted. This also applies to the influence of the shareholders over members of the auditing bodies.

Shareholders are also subject to joint liability with the persons they appoint (when able to determine such appointment by themselves or under a shareholders’ agreement) as directors or members of the auditing bodies when the same are not fit for the performance of such mandate.

iii Shareholder activism
Among other rights, under the PCC shareholders are entitled to bring actions on behalf of the company against those members of the corporate bodies that have breached their duties if the company fails to initiate such actions.

However, possibly because of the existence of controlling shareholders in most Portuguese listed companies and the legal powers attributed to shareholders under Portuguese law (namely, having a direct or indirect say on the remuneration of the corporate bodies), shareholder activism is limited, and usually reveals itself only at the annual shareholders’ general meeting. As such, proxy battles and shareholder campaigns are not common.

Moreover, as the power to appoint (and dismiss) the directors is with the shareholders, directors are more likely to align themselves with the (controlling) shareholders, or at least to heavily consider the shareholders’ interests in the way they manage the company.
*Takeover defences*

Companies usually include defensive mechanisms in their by-laws against takeovers, such as the granting of pre-emption rights to the existing shareholders, the requirement for the company’s consent to a transfer of shares and limitations to voting rights.

For listed companies, the PSC provides for a type of board neutrality rule pursuant to which, as from the moment the board of directors is aware of a decision to launch a takeover bid over more than one-third of a specific category of the company’s share capital, and until the conclusion or prior to the ending of the takeover process, the board of directors cannot take any decisions outside the normal management of the company that may significantly impact the purposes of the bidder. This rule can, however, be bypassed by a decision of the shareholders’ general meeting expressly convened with the purpose to decide on such actions and approved by two-thirds of votes issued. More importantly, this rule is not applicable to Portuguese companies if an offer is made by a company from a foreign country where such board neutrality rule is not in force.

Breakthrough rules of sorts also exist, allowing Portuguese companies to choose to provide in their by-laws that restrictions (whether arising from the by-laws or shareholders’ agreements) applicable to the transfer of securities and to the exercise of voting rights in the company are suspended regarding a takeover bid, and that if the bidder acquires more than 75 per cent of the company’s share capital with voting rights following the takeover, any of those limitations to the transfer of securities and the exercise of voting rights cease to apply to the bidder. These limitations, if adopted, are valid for an 18-month period and need to be subsequently renewed by a decision of the shareholders’ general meeting. Failure to adopt this provision ensures that the by-laws of companies cannot require that any decision to change or eliminate restrictions to the sale of securities or the exercise of voting rights must be approved by a majority of more than 75 per cent of issued votes.

With Decree-Law No. 20/2016, of 20 April, financial institutions (other than savings banks and mutual agricultural credit banks) are required to decide on the maintenance of any voting rights limitations included in their by-laws every five years, the decision to be made by simple majority if proposed by the board of directors. Failure to take that decision until the end of each five-year period renders the limitation null and void.

In addition, the PSC also requires that any shareholder agreement in respect of listed companies that aims to ensure or prevent the success of a takeover bid is disclosed to CMVM – failure to do so renders any decision approved with the votes issued in execution of such agreements null and void.

Moreover, the PSC also requires that the board of directors issues a report (to be made available to the public) upon receiving a takeover bid stating the board of directors’ assessment (duly justified and impartial) of such offer, including information about any negative votes in said report, but does not limit the board of directors from searching for another investor (in fact, it expressly acknowledges such).

Staggered boards (i.e., boards where the directors are appointed to different terms of office) are not common, since the board of directors is generally appointed as whole and, for some scholars, directors cannot be appointed to a term exceeding the term of the board of directors, and shareholders have full control over the possibility to dismiss at all time the members of the board of directors.
v Contact with shareholders

Primary contact between the board of directors and the shareholders occurs at the annual shareholders’ general meeting, in which directors usually take part. Other formal contact opportunities may arise from the exercise, by the shareholders, of their right to information.

VI OUTLOOK

Corporate governance will continue to be a significant concern for companies and their stakeholders in the future, both for listed and non-listed companies, especially by reason of the ongoing proliferation of non-statutory rules and regulations issued under the powers of regulatory entities. The implementation in Portugal of the Long-Term Shareholder Engagement Directive (SHRD II) – currently under discussion in the National Parliament - will bring about some developments in very relevant matters, such as directors’ remuneration and third party transactions as regards companies trading in a regulated market.

In addition, and driven mainly by the current strength of the Portuguese economy, the structuring of complex investment vehicles, with specific tailored corporate and governance structures, will continue to contribute to advance innovative solutions on corporate governance.
Chapter 18

RUSSIA

Danil Guryanov, Bogdana Shtoma and Andrey Shevchuk

I OVERVIEW OF GOVERNANCE REGIME

i Legal and institutional framework

The core statute setting forth the general framework for the Russian governance regime is the Russian Civil Code (RCC).¹ The RCC outlines the basic available corporate forms, including the most commonly used forms: the limited liability company (LLC) and the joint-stock company (JSC); the structure and powers of the various corporate bodies; the rules on representation; the statutory duties and the matters of civil liability of a company’s management and controlling persons; and the procedure for bringing derivative actions.

The JSC Law³ and the LLC Law⁴ each expand upon and supplement the RCC provisions. Importantly, the JSC Law also specifies takeover procedures in respect of public JSCs.

Another statutory framework is the Securities Market Law.⁵ This lays out the operational rules for all securities market participants in relation to the offering of securities, the marketing of financial products and the disclosure of information. Regulatory and interpretative acts of Russian regulatory and enforcement agencies (such as the Standards for Issuance of Securities⁶ and the Disclosure Rules)⁷ expand upon and supplement the provisions of the Securities Market Law.

Both public and non-public corporations active in certain highly regulated sectors of the Russian economy (such as banks, insurers, non-state pension funds and professional securities market participants) are bound by industry-specific legislation. This legislation specifies management qualification and reputation requirements, liquidity and financial stability standards, risk management and compliance procedures, and, in certain cases, specific requirements in relation to the structure of the governing bodies of the regulated

¹ Danil Guryanov, Bogdana Shtoma and Andrey Shevchuk are lawyers at Herbert Smith Freehills CIS LLP.
⁶ Regulation No. 428-P On Securities Issuance Standards, the Procedure of State Registration of Issuance (Additional Issuance) of Securities, the Procedure of State Registration of Securities Issuance Reports and the Registration of Securities Prospectuses approved by the Central Bank of the Russian Federation on 11 August 2014.
companies. The Russian Central Bank (CBR) is the key regulator: it is in charge of the listed companies’ regime, and is generally responsible for the prudential regulation and supervision of Russia’s financial services industry.

Best practice provisions for listed companies are set out in the Corporate Governance Code (CGC)\(^8\) and the listing rules of licensed stock exchanges.\(^9\) Listed companies are expected to comply with the CGC or disclose and explain non-compliance in their annual reports. Companies must comply with the listing rules requirements to obtain and maintain premium or standard listings (rather than mere quotations) at the stock exchange. Best practice provisions for certain regulated companies are determined and enforced by self-regulatory organisations (SROs) in each sector.

**ii Latest developments**

Since 2010, when the government launched an initiative to transform Moscow into an international financial hub, it has taken a series of steps to achieve that ambitious goal. Among those are improvement of quality of the capital markets’ infrastructure and the financial services’ regulatory framework, implementation of measures against the abuse of inside information and market manipulation, more close regulation of the financial industry (in particular, since 2013, the CBR has been waging a large-scale campaign against financial institutions and their management involved in bad faith or suspicious transactions or practices detrimental to their clients and to the financial stability of the financial institution itself).

Corporate governance matters have also been on the radar of the Russian policymakers. A major step forward was the reform of the RCC in 2014, introducing new classification of commercial entities into public and non-public companies (with non-public companies having significantly greater flexibility in their governance arrangements).\(^10\)

The government followed up by concentrating its efforts on balancing the (often differing) interests of the various stakeholders in both public and non-public corporations. The conflicts between the interests of the majority and minority shareholders, and the shareholders in general and the management of the company were the two focal points of the government’s attention on this front.

Russian policymakers have sought to balance the interests of minority and majority shareholders, in particular, by introducing a series of previously non-existent checks and balances.

In particular, liability of the majority shareholders and ultimate controlling persons of the companies for the damage to the companies they control as a result of their bad faith or unreasonable actions, or both, was reinforced (and, in relation to the liability of the ultimate controlling persons, introduced for the first time outside the bankruptcy context). The minority shareholders have retained the right to bring derivative actions to enforce such liability and the shareholding threshold to bring such derivative actions has been retained as low as 1 per cent. The right to bring derivative actions has also been granted to supervisory board members. At the same time, certain changes to the procedure of bringing such claims were made to avoid the abuse of this instrument and turning it into a greenmail tool.

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\(^9\) Each stock exchange develops a set of rules for access to public trading in securities that in turn are based on the benchmark approved by the regulators.

\(^10\) A company is deemed to be public if it has a registered prospectus in respect of its shares or instruments convertible into shares and has entered into a listing agreement with a licensed stock exchange.
The potential for overextending the powers of the minority shareholders (who are often seen by the Russian policymakers as having a short-term speculative interest in the business) and a rise in shareholders’ activism appears to remain one of the key concerns for the government. With that in mind, certain anti-abuse protections were introduced into the statutory provisions regulating the minority shareholders’ information rights. The shareholders whose shareholding in the company is less than 25 per cent have to explain a proper business purpose for requesting access to certain documents of the company. Such access may be denied, in particular, if the requesting shareholder is evidently acting in bad faith, is a competitor of the company, affiliated with a competitor, or both.

Insofar as the accountability of the management is concerned, as part of the 2014 RCC reform the law has been amended to expressly set out an overriding duty of the members of governing bodies of companies and their controlling persons: to act in the company’s best interests reasonably and in good faith, subject to an obligation to indemnify the company for damage resulting from a breach of that duty. To improve the quality of the board oversight, the government has also expanded the powers and information rights of the supervisory board members.

The Supreme Court as recently in December 2019 reinforced the principle of the management accountability in its landmark decision stating that even if the general shareholders’ meeting or the supervisory bodies approve a transaction (or even instruct the management to go ahead with it), the management (1) shall be free to decline to proceed with it as they deem that it would be detrimental to the company and (2) may still be held accountable for any resulting losses (if they do proceed). The Supreme Court held that: (1) the management’s obligation to act in the best interests of the company honestly and in good faith is paramount; (2) the management is primarily responsible for the day-to-day operations of the company; and (3) it may not relieve itself from liability by blindly following the decisions of other corporate bodies of the company.

The management and controlling persons accountability continues to remain a priority for CBR as the primary regulator of the financial services industry, especially following a series of high-profile insolvencies and bail-outs in that sector since 2013.

II CORPORATE LEADERSHIP

i Board structure and practices

Russian law provides for a two-tier board structure in public companies, including a supervisory board (also referred to as the board of directors) and the executive bodies. The two-tier structure is also mandatory for non-public companies that have more than 50 shareholders or that are subject to a specific regulatory regime (e.g., credit institutions).

The executive bodies of a company include the CEO (or several joint CEOs) and the management board. The formation of a management board is optional, except for those companies that are subject to special regulatory regimes (such as credit institutions).

Supervisory board and management board

Functions and formation

The functions of the supervisory and management boards are to supervise and advise CEOs (or joint CEOs) and limit their discretion on matters that are crucial for the stability and sustainable development of the company. The supervisory board is responsible for determining the company’s long-term strategy and deciding on matters that affect key aspects of that
strategy. The minimum competence of the supervisory board is specified by the RCC and the JSC Law. The competence of the management board is determined wholly by the company’s charter. The management board usually includes the company’s senior management and is subordinate to the supervisory board. Its primary function is to advise the CEO on the implementation of strategy approved by the supervisory board.

**Decision-making procedures**

With few exceptions, the law does not regulate the decision-making procedures of the supervisory board or the management board, so that shareholders are free to specify the relevant procedures in the charter.

**Committees**

Until recently, the formation of supervisory board committees was generally discretionary. However, from July 2018 public corporations are required to form an audit committee in their supervisory boards and implement risk management and internal control functions in general.

Additional requirements regarding the formation of supervisory board committees are included in the stock exchange rules. Compliance with such additional requirements is often a condition for a company to be included in certain quotation lists.

**CEO (or joint CEOs)**

The CEO (or joint CEOs) (referred to in law as the sole executive body) has the duty of managing the company. The CEO is held accountable by Russian law for the company’s overall compliance with the applicable law. The CEO is vested with the power to enter binding contracts with third parties on behalf of the company. Additionally, the CEO may issue powers of attorney to other individuals or legal entities to allow them to represent the company.

Where there are joint CEOs, the scope of powers of each of them may differ depending on the provisions of a company’s charter. The functions of the CEO may alternatively be performed by a specialised management company on the basis of a management services agreement.

**ii Directors**

**Appointment and removal**

**Supervisory board**

Supervisory board members of a public JSC are elected annually by the general shareholders’ meeting. Members may be re-elected for an unlimited number of terms. The supervisory board in a public JSC is elected by cumulative voting. Each shareholder receives a number of votes equal to the product of the number of shares held by the shareholder by the number

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11 Since July 2018, the competence of the supervisory board has been broadened, empowering its members to propose candidates for the CEO (or joint CEOs), the supervisory board itself and the audit committee at their own discretion; however, the number of such candidates shall not exceed the overall number of board members.
of seats on the supervisory board, and may distribute these votes among the nominees as desired. The supervisory board is then composed of the candidates who receive the largest number of votes.

Management board and the CEO (or joint CEOs)
Statute does not prescribe the term or procedure for the appointment of members of the executive bodies. In view of this, the matter is governed by the company’s charter.

Independence, expertise and reputation
The professional suitability of supervisory board members and executive body members is becoming increasingly important in Russia. Under Russian law, no person disqualified by a court for an administrative or criminal offence (e.g., the falsification of financial and accounting reports, money laundering or insider trading) can serve as a CEO or a member of the management or supervisory boards of a public or non-public company for the term of their disqualification. There are further reputational and qualification requirements for supervisory board members and executive body members of regulated companies.

In the absence of limitations in the charter, supervisory board members are generally free to simultaneously hold managerial and supervisory positions in other companies. The approach is entirely different for executive body members, which require express authorisation from the supervisory board to be able to combine more than one office. Additionally, there are certain specific restrictions for regulated companies.

Remuneration of directors and senior management
Membership of the supervisory board does not result in employment by the company per se. In view of this, the basic position is that membership of the supervisory board is unpaid. However, the general shareholders’ meeting may decide to remunerate or compensate the supervisory board members. Executive body members are company employees and their salary is stipulated in their employment contracts. In practice, the remuneration of the senior management is usually made subject to the consent of the supervisory board. The public corporations are required to disclose their remuneration policy and the amount of remuneration of the key managers and supervisory board members in their annual reports.

Conflicts of interest
Russian law contains the principle that supervisory board members and executive body members should act in the absence of conflicts of interest. To enforce this principle, supervisory board members and executive body members are required to provide to the company the information necessary to determine whether a transaction undertaken by the company qualifies as a related-party transaction – that is, a transaction in which an executive body member or supervisory board member or a controlling person\(^\text{12}\) of the company is interested personally or through companies under their control or their respective relatives. Such transactions do not require mandatory approval, unless a supervisory board member or a more than 1 per cent shareholder (having received notice from the management of

\(^{12}\) The definition of a controlling person for the purposes of related-party transactions includes the persons holding, directly or indirectly, a controlling stake in the capital of the company, the persons vested with power to appoint its CEO or to elect more than 50 per cent of supervisory board members, or both.
its intention to proceed with the transaction) requests such approval, or the management submits the transaction for prior approval of its own accord (e.g. to enhance its legitimacy). As a general rule, the interested parties are banned from voting on the items of the agenda in which they have an interest. In 2019, draft law was put forward to extend the scope of these disenfranchisement provisions to the persons under the interested parties’ control.

A transaction made or approved in the presence of a conflict of interest or resulting in a loss to the company, (or both) may trigger an obligation for the conflicted persons to indemnify the company for the loss. There are a number of financial services sector specific provisions targeting the matter of the conflict of interest (in particular, regarding the risks assessment of the credit institutions’ dealings with its connected persons).

**Liability**

**Internal liability**

In the event that a supervisory board’s members or executive body, or a company’s controlling persons, are in breach of their duties to the company, they are obligated to indemnify the company for the damage resulting from the breach. There is a statutory restriction on the ability to limit management’s liability in relation to bad faith (all companies) and unreasonable conduct (public companies), and the liability of controlling persons.

The CEO is not exculpated from liability merely because he or she obtained all requisite corporate approvals for an action (the Supreme Court reinforced this position in its December 2019 ruling) – if the action caused damage to the company and none of the exemptions from liability apply, all persons who voted in favour of that action (or abstained from participation in the voting in bad faith) may be held jointly and severally liable.

**External liability**

The general position under Russian law is that executive body members, supervisory board members and a company’s controlling persons are not liable to parties who contract with the company for the company’s debts. However, there are several exemptions to this principle. One exception is that management and the controlling persons\(^{13}\) are liable in the event that the company is declared insolvent.

Another exception is set out in the Securities Market Law, which provides that any person who has signed or approved a prospectus is subject to secondary liability for losses caused to investors as a result of inaccurate, misleading or incomplete information being contained in the prospectus.

### III DISCLOSURE

The JSC Law and the Securities Market Law are the key statutes establishing disclosure obligations. The JSC Law requires all public companies to disclose annual reports, annual accounts, lists of affiliates and corporate documents. The Securities Market Law sets out

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\(^{13}\) The definition of a controlling person for the purposes of insolvency laws, includes the CEO (or joint CEOs), the persons holding a controlling stake in the capital of the company, the persons vested with representative authority on behalf of the company and the persons exercising de facto control over its activities. The definition and criteria of a controlling person have been summarised in Resolution of the Plenum of the Supreme Court of the Russian Federation No. 53 dated 21 December 2017.
wider disclosure obligations that are triggered by the company registering a prospectus of its securities. The disclosure obligations may apply to non-public companies that have issued securities (such as bonds)\(^ {14} \) to the public and that were required to register a prospectus. The Disclosure Rules provide further detail to supplement the Securities Market Law.

The Securities Market Law disclosure requirements can be classified as periodic and one-off disclosure obligations. The periodic disclosure obligations include the publication of quarterly reports, which primarily include quarterly financial statements. One-off disclosures relate to material facts (i.e., certain price-sensitive information concerning the reporting company).

A complex procedure applies if a reporting company wishes to terminate (or become exempt) from its disclosure obligations. This procedure involves a super-majority vote by the shareholders and a special authorisation from the CBR.

Additional disclosure obligations may apply to regulated companies, with credit institutions being subject to the highest level of transparency and most rigid reporting standards.

In light of the continuing geopolitical unrest and the ongoing ‘war of sanctions’, amendments to the JSC Law and the Securities Market Law were introduced in December 2018 to empower the government to determine instances where a company may become exempt from some of the disclosure requirements that would otherwise have been applicable to it.

### IV CORPORATE RESPONSIBILITY

#### i General

The CGC defines corporate governance as ‘a system of relationships between the executive bodies of a company, its board of directors, its shareholders and other stakeholders’. The CGC recommends that supervisory boards take into account both financial and non-financial risks affecting a company’s activities (including ethical, social, ecological and operational risks), the interests of all external stakeholders (including employees), and applicable social and ecological standards.

The obligation of the management to take into account the interests of all of the company’s stakeholders is not expressly set out in any specific piece of legislation, but is rather derived from a range of general legislative provisions.

As a matter of practice, even in the absence of a proper regulatory framework that would incentivise them to do so, many major companies tend to assume broad social responsibility undertakings in implementing their internal ethics codes and, on certain occasions, as part of their government-relations strategy.

#### ii Employees

All Russian companies are subject to social obligations, such as ensuring minimum salary levels for employees, making contributions to social and pension funds for employees, conducting assessments of workplace conditions, and introducing additional benefits and

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\(^ {14} \) Non-public companies may not issue shares and instruments convertible into shares to the public: this right belongs to public companies only.
regimes if necessary based on these assessments. Separate benefit regimes are also established for different categories of employees (such as women with family responsibilities and rotational system employees).

iii  Small and medium-sized businesses
The government is seeking to support Russian small and medium-sized businesses (SME). Given the significant effect that the government has on the Russian economy, Russian law sets mandatory provisions for state agencies and state-owned companies to purchase a specified amount of goods and services from SMEs.

iv  Anticorruption
Although Russian anticorruption legislation is mainly focused on governmental authorities and state-owned companies, there are still some broadly stated rules targeting companies with no state participation to take measures to prevent corruption. In particular, commercial bribery is a criminal offence under Russian law. Further, private companies are prompted to introduce anticorruption policies and procedures preventing conflict of interest (such policies and codes have become common in large Russian companies but remain rare for smaller privately held companies). Companies with significant foreign participation tend to follow the anticorruption standards applicable to their overseas parent undertakings (e.g., the UK Bribery Act or US Foreign Corrupt Practices Act).

v  Currency control and anti-money laundering
Russian financial institutions have a number of supervisory functions in relation to currency control and anti-money laundering (AML). Russian residents are required to collect all foreign currency export proceeds in their bank accounts in Russia. For those purposes, the overseas contracts of Russian residents are required to be registered with an authorised Russian bank, which will then handle the payments under the relevant contract. The purpose of this regulation is to prevent capital flight from Russia.

The AML laws require that companies operating with money – banks and other credit institutions, securities market participants, insurance companies, investment fund management companies, realtors, pawnshops and others – to monitor and, if necessary, report their clients' suspicious transactions the value of which exceeds the threshold set out in law.

vi  Compliance
To ensure their stability and protect their clients, credit institutions and professional participants of securities markets are required by the JSC Law to maintain an internal compliance function (including, by reference to the Basel Committee principles). As noted above, the public corporations are required to introduce risk management and internal control function (although there is no express requirement for them to maintain a compliance function). Even where there is no specific legislative requirement regarding the maintenance of a compliance function, in practice, this function is usually fulfilled by various departments within the relevant company's corporate structure.
V SHAREHOLDERS

i Shareholder rights and powers

Russian policymakers have adopted a restrictive approach towards the powers of the general shareholders’ meeting in public companies. The scope of these powers is determined by the JSC Law only and may not be extended (but, conversely, may be further limited in favour of the supervisory board) by the charter. The matters attributed to the competence of the general shareholders’ meeting by the JSC Law, are limited to those that are likely to result in a fundamental change to the nature of the business of the company or the composition of its assets, and the balance of powers between the various governing bodies set out in the charter.

By contrast, the regulation is more flexible for non-public companies. For example, the competence of the general shareholders’ meeting in a non-public company may be extended compared to the one set forth by the statute.

Equality of voting rights

Russian law establishes the principle of equality of voting rights: all ordinary shares and all preference shares of a single issue provide equal rights in proportion to their nominal value. The voting rights are usually carried by ordinary shares only. The preference shares in public JSCs become voting shares in certain exceptional circumstances only (most commonly, non-payment of dividends due on those shares).

Non-public JSCs may issue voting preference shares granting voting rights on all or some of the matters on the agenda of the general shareholders’ meeting. LLCs do not issue shares, and as a general rule provide a percentage of votes determined as the ratio between the nominal value of the participatory interests held by the shareholder and the aggregate amount of the charter capital of the LLC. Disproportionate voting arrangements may be set out in the charter of an LLC or a non-public JSC (but not a public JSC).

Rights of dissenting shareholders

The law contains specific protections for shareholders who attended a general shareholders’ meeting and voted against a resolution or did not participate in the relevant general shareholders’ meeting (dissenting shareholders). A dissenting shareholder can challenge such a resolution of the general shareholders’ meeting. Additionally, the law permits dissenting shareholders of JSCs to request that the company buys out all or a part of their shareholding, if the resolution in question concerns certain fundamental matters (such as the company’s reorganisation or the entry into of a major transaction with a value exceeding 50 per cent of the company’s assets).

ii Shareholders’ duties and responsibilities

The most important statutory obligations of shareholders are their financial obligations (in particular, payment of their share of the company’s capital) and their obligations not to hinder the activities of the company (in particular, by maintaining the confidentiality of commercially sensitive information, participating in adopting key corporate decisions and avoiding causing damage to the company).
Shareholder activism

Say on pay

The general shareholders’ meeting is the competent body to decide on the timing and amount of the distribution of dividends to shareholders. However, the supervisory board may issue a recommendation on the amount of dividends or a recommendation not to distribute the dividends at all (in which case the general shareholders’ meeting cannot decide otherwise).

Derivative actions

Shareholders can sue members of the executive bodies and the supervisory board, as well as persons exercising de facto control over the company, for damage caused to the company by those persons.

Proxy battles and proxy solicitation

Unlike in some Western jurisdictions, the issues of proxy fights and proxy solicitation are not typical in Russia. In view of this, there are no special regulations in this respect.

Shareholder campaigns

Large shareholder campaigns are not very common in Russia; although, some of the institutional minority investors (particularly portfolio companies) in Russian public corporations have been increasingly active in bringing derivative actions against controlling shareholders in the public corporations for losses caused by their actions.

Long-term shareholder value

The management of Russian companies is subject to an overarching obligation to act reasonably and in good faith to ensure that the company continues as a going concern with a view to profit. As such, the management is encouraged by the Russian legislators to try to work towards an increase of the shareholder value long-term. Recognising that in certain circumstances the management may be tempted or pressured to prioritise short-term (and sometimes speculative) goals by some of the shareholders (particularly controlling shareholders), a number of checks and balances to enable the management to follow a proper course of action have been put in place in Russian legislative acts (including the enhanced liability of the management and controlling persons of the company for the damage caused to the company). The overall principle is reinforced through securities market specific prohibition for all market participants from engineering any short-term price increases in the company’s stock (market manipulation).

Takeover defences

Takeover rules

Russian law does not generally prohibit acquisitions of significant stakes in public JSCs on the basis of private bilateral deals between the purchaser and the selling shareholder or shareholders. That said, the JSC Law contains a number of provisions addressing the procedure for acquisition of more than 30 per cent stake in public JSCs (Takeover Rules).

The Takeover Rules:
require a shareholder that consolidated a more than 30, 50 or 75 per cent of voting shares in a public JSC to submit an offer to the remaining shareholders in the target company allowing them to exit the target by putting their shareholdings to the bidder at a specified price: a mandatory tender offer (MTO);

allow a shareholder that intends to consolidate a more than 30 per cent stake voluntarily to submit an offer to all other shareholders to sell their shares to the bidder at a specified price: a voluntary tender offer (VTO); and

c where a shareholder has consolidated more than 95 per cent of voting shares in a public JSC:

- require such shareholder to notify the remaining minorities of their right to put their shares to such shareholder; and
- provided that at least 10 per cent of the shares have been purchased on the basis of an MTO or a VTO, allow such shareholder to call the shares of the remaining minorities thereby consolidating 100 per cent of voting shares in the target company.

Defence strategies

Unlike many Western jurisdictions, the Takeover Rules provide little specific regulation on defence strategies against hostile takeovers. Arguably, the main reason for this is that due to high concentration of control in Russian corporations, more often than not, the actual acquisition of control over the target happens on the basis of a bilateral deal between the previous controlling owner and the purchaser and the Takeover Rules are triggered after that deal is completed. The provisions of Takeover Rules are seen, with rare exceptions, as an unpleasant formality to comply with, rather than a meaningful set of instruments for acquisition of control over the target.

The Takeover Rules are, therefore, primarily focused on granting a certain degree of protection to the minority shareholders in Russian public targets upon the occurrence of a change of control, rather than regulating in detail the ways in which existing shareholders may defend against the prospect of such change of control.

Key decisions taken by shareholders

The underlying principle of the Takeover Rules is that a change of control over a public company is a matter for the shareholders in that company to decide, ultimately, through accepting or declining to accept a takeover bid. The CEO, the management and the supervisory boards are, therefore, limited in their ability to influence that decision (or the takeover process as a whole) other than through issuing a recommendation to the shareholders to accept or decline to accept the relevant offer. In particular, the management and the supervisory board are limited in their ability to implement a crown-jewel defence, as, after the an MTO or a VTO procedure contemplated by the Takeover Rules is triggered, the decision-making powers in the company are redistributed between the main governance bodies in favour of the general shareholders’ meeting (such that the approval of the latter is required for any transaction exceeding 10 per cent of the company’s assets or any issuance of new shares or instruments convertible in the shares).
**Staggered board**
Russian corporate governance rules contemplate that the supervisory board is re-elected by the general shareholders’ meeting annually in full. There are no instruments under Russian law to appoint a supervisory board in a public JSC, the members of which are classified into different categories (for example, each with an individual rotation cycle).

**Poison pill defences**
Poison-pill defences are usually structured through issuance of convertible instruments, voting preferred shares, emergency issuance of additional shares to all existing shareholders other than the purchaser and analogous measures.

Russian law does not expressly prohibit those kinds of arrangements (unlike some Western jurisdictions), which makes them theoretically possible. However, the regulation of the instruments customarily involved in structuring poison pill-type defences makes the implementation of any such defence in practice very challenging.

**Voting preference shares**
As a general rule, preference shares in Russian public companies are non-voting shares and only become voting shares in a limited number of cases. Where the preference shares have become voting shares prior to an MTO or a VTO procedure having been triggered pursuant to the Takeover Rules, those shares may be acquired by the purchaser on the basis of an MTO or a VTO.

Russian law contemplates the concept of voting preference shares that grant voting rights on all or some of the matters within the competence of the general shareholders’ meeting permanently or upon occurrence of certain specified circumstances. However, such instrument is available to non-public companies only, which are outside the scope of the Takeover Rules.

**Convertible instruments**
Russian law allows issuing instruments convertible into voting shares in a company (such instruments include convertible bonds, convertible preference shares and options).

It must be taken into account that after an MTO or a VTO procedure pursuant to the Takeover Rules has been triggered, the issuance of convertible securities is only possible by resolution of the general shareholders' meeting.

**White knight**
The Takeover Rules include a concept of a competitive offer (i.e., an MTO or a VTO that has been submitted by a different bidder after an MTO or a VTO from the original bidder has been received by the target); however, it is very rarely used in practice given the practical considerations outlined above.

**Contact with shareholders**

**Mandatory and best practice reporting to all shareholders**
Shareholders have a general right to access information and documents concerning the company's activities. Both the JSC Law and the LLC Law list the information that is available to all shareholders and set out the procedure for accessing this information. Access to certain documents of JSCs, such as a company's accounts and the minutes of its management board,
is open only to a shareholder or shareholders collectively holding not less than 25 per cent of voting shares. In certain cases, minority shareholders need to show proper business purpose to get access to the documents of the company. Moreover, the JSC Law and LLC Law have recently been supplemented with a new provision empowering the government to release certain companies from the statutory obligations to provide information on interested-party and major transactions to their stakeholders.

VI OUTLOOK

Since 2010, the government programme to transform Moscow into an international financial centre has been the key driving force behind corporate governance reforms in Russia. One key idea behind that initiative was to make the Russian jurisdiction more attractive to international financial investors and give a boost to domestic capital markets.

While the momentum behind this initiative has somewhat been stalled, particularly, in the recent years following the political crisis in Ukraine and Russia becoming subject to an EU and US sanctions, the government has continued its efforts in improving the corporate governance regime for Russian companies. Russian policymakers and the companies themselves have recognised the importance of proper corporate governance, irrespective of the level of interest of foreign investors in the Russian jurisdiction.

Russian policymakers continue their work on further enhancing management accountability. One of the suggested innovations (which have not yet been approved by the Parliament) relates to the treatment of quasi-treasury shares. While treasury shares owned by a company itself are non-voting and are not counted towards a quorum, there is no similar limitation for shares in the company held by its subsidiaries. Therefore, as has been the case in numerous high-profile shareholders’ conflicts surrounding prominent Russian companies, the control by management of a significant quasi-treasury stake results in an excessive entrenchment of the management. The concepts of accountability of management and controlling persons remain of even greater importance in the financial services sector, with the continuing trend for clearing the sector of corrupt and bad-faith participants.

Protection of minority shareholders in the process of takeovers of public companies is another hot topic and a leitmotif of 2019–2020. One of the key proposed changes to the takeover regime concerns the indirect change of control over public companies. The takeover rules at this stage are triggered only through the change of ownership of a significant stake in the company itself. The change of control over a significant shareholder does not trigger the takeover rules and has on numerous occasions been used to avoid the implementation of the minority protection measures contemplated by the law.

In summary, the government is continuing its work on improving the Russian governance regime with a view to reaching a balance of interests between the various interested parties, despite the unfavourable political and economic circumstances. Hopefully, those efforts will receive an additional boost if and when the international sanctions against Russia are lifted.
Chapter 19

SINGAPORE

Andrew M Lim, Richard Young and Lee Kee Yeng

I OVERVIEW OF GOVERNANCE REGIME

The Singapore corporate governance regulatory framework is contained in certain mandatory rules, comprising mainly of the Companies Act (CA), the Securities and Futures Act (SFA) and, in respect of companies listed on the Singapore Exchange (SGX), the Listing Manual, and best practice recommendations as primarily set out in the form of the Code of Corporate Governance (Code) and the accompanying Practice Guidance issued by the Monetary Authority of Singapore (MAS).

The CA is the principal piece of legislation that applies to all companies (both private and public) incorporated in Singapore and, in some limited instances, to foreign corporations with business operations in Singapore.

Entities listed on the SGX are also subject to continuing obligations in the form of listing rules in the Listing Manual. Such rules include requirements on the manner in which securities are to be offered, regulate transactions with interested persons and prescribe the disclosure obligations of listed issuers. The principal function of these rules is to provide a fair, orderly and transparent market for the trading of securities.

The SFA enforces the disclosure requirements of the Listing Manual by making it an offence for a listed company to intentionally or recklessly fail to meet its disclosure obligations under the Listing Manual. In the case of a negligent failure, a listed company may be subject to civil penalties and liabilities pursuant to the SFA.

In addition, in the case of companies listed on the SGX, the SFA empowers the SGX to apply to the courts for a court order to enforce compliance with the listing rules. The SFA also prescribes the statutory prospectus requirements and the disclosure obligations of directors, chief executive officers (CEOs) and substantial shareholders of a listed company in relation to their interests in securities.

The listings and enforcement framework for listed companies has been further enhanced since 2015 with SGX’s establishment of three independent committees (namely the Listings Advisory Committee, the Listings Disciplinary Committee and the Listings Appeals Committee), and amendments to the Listing Manual to empower the SGX to impose a greater range of sanctions. Under the enhanced enforcement framework, the SGX has the authority to impose sanctions, such as issuing fines to a listed company of an amount not exceeding S$250,000 per contravention (subject to a maximum of S$1 million per...

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1 Andrew M Lim, Richard Young and Lee Kee Yeng are partners at Allen & Gledhill.
2 Section 203 of the SFA.
3 Sections 232 and 234 of the SFA.
4 Section 25 of the SFA.
hearing for multiple charges), requiring a listed company to implement an effective education or compliance programme, requiring a listed company’s directors or executive officers to undertake a mandatory education or training programme and requiring the resignation of a director or executive officer.5

The Code provides principles and provisions designed with the aim of assisting listed companies and their boards to achieve a high standard of corporate governance. Under the Code’s comply or explain approach, listed companies are expected to comply with the provisions in the Code, and variations from the provisions are acceptable to the extent that companies explicitly state and explain how their practices are consistent with the aim and philosophy of the relevant principle underlying such provision. Under the Listing Manual, a listed company must comply with the principles of the Code. Where a listed company’s practices vary from any provisions of the Code, it must explicitly state, in its annual report, the provision from which it has varied, explain the reason for variation and explain how the practices it has adopted are consistent with the intent of the relevant principle. The MAS has also issued accompanying Practice Guidance that complements the Code by providing guidance on the application of the principles and provisions and setting out best practices for companies. Adoption of the Practice Guidance is voluntary.

This chapter explores the key features of these rules and regulations from a corporate governance perspective. Financial institutions such as banks, insurers and finance holding companies have their own sets of corporate governance guidelines issued by the MAS, which are not addressed in this chapter.

II CORPORATE LEADERSHIP

i Board structure and practices

Singapore companies have a single-tier board of directors where the role of the board is governed by the constitutional documents of the company and by statute. In particular, Section 157A of the CA provides that the business of a company shall be managed by, or be under the direction or supervision of, the directors; and that the directors may exercise all the powers of a company, except for any power that the CA or the constitution of the company requires the company to exercise at a general meeting of shareholders.

The Practice Guidance provides that the board’s role is to:

a provide entrepreneurial leadership, and set strategic objectives, which should include appropriate focus on value creation, innovation and sustainability;

b ensure that the necessary resources are in place for the company to meet its strategic objectives;

c establish and maintain a sound risk management framework to effectively monitor and manage risks, and to achieve an appropriate balance between risks and company performance;

d constructively challenge management and review its performance;

e instil an ethical corporate culture, and ensure that the company’s values, standards, policies and practices are consistent with that culture; and

f ensure transparency and accountability to key stakeholder groups.6

5 Rule 1417 of the Listing Manual.
6 Practice Guidance 1.
The Listing Manual requires a listed company’s board to have at least two non-executive directors who are independent and free of any material business and financial connection with the listed company.\(^7\) In addition, the Code provides that non-executive directors are to make up a majority of the board,\(^8\) and independent directors should make up at least one-third of the board.\(^9\) Where the chairperson is not an independent director, the independent directors are to make up the majority of the board.\(^10\) The Code defines an independent director as one who is independent in conduct, character and judgement, and has no relationship with the company, its related corporations, its substantial shareholders\(^11\) or its officers that could interfere, or be reasonably perceived to interfere, with the exercise of the director’s independent business judgement in the best interests of the company.\(^12\) The Code also provides that a director who has been a director on the Board for an aggregate period of more than nine years (whether before or after listing) and whose continued appointment as an independent director has not been sought and approved in separate resolutions by (1) all shareholders and (2) all shareholders excluding shareholders who also serve as the directors or chief executive officer (and their associates) will be regarded as non-independent.

The chairperson and the CEO are to be separate persons to ensure an appropriate balance of power, increased accountability and greater capacity of the board for independent decision-making.\(^13\) The relationship between the chairperson and the CEO of a listed company must be disclosed if they are immediate family members.\(^14\)

The Practice Guidance provides that the chairperson’s overall role is to lead and ensure the effectiveness of the board, which includes promoting a culture of openness and debate at the board; facilitating the effective contribution of all directors; and promoting high standards of corporate governance.

Externally, the chairperson is the face of the board, and should ensure effective communication with shareholders and stakeholders. Within the company, the chairperson should ensure appropriate relations within the board, and between the board and management, in particular between the board and the CEO. In the boardroom, the chairperson’s responsibilities range from setting the board agenda and conducting effective board meetings to ensuring that the culture in the boardroom promotes open interaction and contributions by all.\(^16\)

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\(^7\) Rule 210(5)(c) of the Listing Manual.  
\(^8\) Provision 2.3 of the Code.  
\(^9\) Guideline 2.1 of the 2012 Code. Rule 210(5)(c) of the Listing Manual, which requires independent directors to make up at least one-third of the board will come into effect on 1 January 2022. A longer transition period of three years was provided for changes in the SGX Listing Rules relating to board composition, to provide companies with more time to make board composition changes.  
\(^10\) Provision 2.2 of the Code.  
\(^11\) The Code defines a substantial shareholder as a shareholder who has an interest or interests in one or more voting shares (excluding treasury shares) in a company and the total votes attached to that share, or those shares, is not less than 5 per cent of the total votes attached to all voting shares (excluding treasury shares) in the company, in line with the definition set out in Section 2 of the SFA.  
\(^12\) Provision 2.1 of the Code.  
\(^13\) Provision 3.1 of the Code.  
\(^14\) Rule 1207(10A) of the Listing Manual.  
\(^15\) Practice Guidance 3 of the Code.  
\(^16\) Practice Guidance 3 of the Code.
It should be noted that the definition of a director in the CA includes ‘a person in accordance with whose directions or instructions the directors or the majority of the directors of a corporation are accustomed to act’: that is, a shadow director.

**Committees to be established by the board**

The Listing Manual requires that a listed company establish one or more committees as may be necessary to perform the functions of an audit committee, a nominating committee and a remuneration committee, with written terms of reference that clearly set out the authority and duties of the committees.17 The Code provides that:

- the duties of the audit committee include, among other things:
  - reviewing significant financial reporting issues and judgements so as to ensure the integrity of the financial statements of the company and any announcements relating to the company’s financial performance;
  - reviewing at least annually the adequacy and effectiveness of the company’s internal controls and risk management systems;
  - reviewing the assurance from the CEO and the chief financial officer on the financial records and financial statements;
  - making recommendations to the board on proposals to the shareholders on the appointment and removal of the external auditors, and the remuneration and terms of engagement of the external auditors; and
  - reviewing the adequacy, effectiveness, independence, scope and results of the external audit and the company’s internal audit function.18

The importance of the audit committee is emphasised by the inclusion of provisions not just in the Code, but also in the CA and the Listing Manual. For example, Section 201B of the CA stipulates the composition and functions of the audit committee. Rule 704(8) of the Listing Manual provides that in the event of any retirement or resignation that renders the audit committee unable to meet the minimum number (not less than three), the listed company should endeavour to fill the vacancy within two months, but in any case not later than three months. Rule 1207(10C) of the Listing Manual requires the audit committee to comment on whether the listed company’s internal audit function is independent, effective and adequately resourced;

- the role of the nominating committee is to, among other things:
  - make recommendations on the reappointment of each director;19
  - determine annually if a director is independent;20 and
  - recommend for the board’s approval the objective performance criteria and process for the evaluation of the effectiveness of the board as a whole, and of each board committee separately, as well as the contribution by the chairperson and each individual director to the board.21

18 Provision 10.1 of the Code.
19 Provision 4.1 of the Code.
20 Provision 4.4 of the Code.
21 Provision 5.1 of the Code.
The Practice Guidance also provides that the nominating committee should take into account the number of directorships and principal commitments of each director in assessing whether he or she is able to or has been adequately carried out his or her duties; and the role of the remuneration committee is to review and make recommendations to the board on a framework of remuneration for the board and key management personnel, and the specific remuneration packages for each director, the CEO and other key management personnel.

Remuneration

The Code provides that the level and structure of remuneration of the board and key management personnel are to be appropriate and proportionate to the sustained performance and value creation of the company, taking into account the strategic objectives of the company. A significant and appropriate proportion of executive directors’ and key management personnel’s remuneration is to be structured so as to link rewards to corporate and individual performance. Performance-related remuneration is to be aligned with the interests of shareholders and promote the long-term success of the company. Remuneration is to be appropriate to attract, retain and motivate directors to provide good stewardship of the company and key management personnel to successfully manage the company for the long term.

In addition, every company is to be transparent on its remuneration policies, level and mix of remuneration, the procedure for setting remuneration, and the relationships between remuneration, performance and value creation.

For Singapore-incorporated companies, Section 169 of the CA provides that emoluments for a director in respect of his or her office must be approved by a resolution that is not related to other matters.

ii Directors

Singaporean law does not impose an all-embracing code of conduct on directors. In practice, a company’s constitution prescribes the ambit of the directors’ powers. The duties and responsibilities of directors of Singapore-incorporated companies arise under common law and the CA, and for directors of listed companies, the SFA, the Listing Manual and the Code.

There are two broad categories of directors’ duties under common law and statute. They are the duty of good faith (which encompasses specific obligations arising out of the fiduciary obligations of directors) and the duties of care and skill. These duties are owed to the company alone, and not to individual shareholders or groups of shareholders or other members of the company’s group.

In relation to the duty of good faith, Section 157(1) of the CA provides, among other things, that a director shall at all times act honestly in the discharge of the duties of his or her office. Section 157(2) of the CA prohibits, among other things, a director from making improper use of his or her position as an officer or agent of the company or any information

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22 Practice Guidance 4.
24 Principle 7 of the Code.
26 Provision 7.3 of the Code.
27 Principle 8 of the Code.
acquired by virtue of his or her position as an officer or agent of the company to gain, directly or indirectly, an advantage for him or herself or for any other person, or to cause detriment to the company. Section 158 of the CA, however, allows nominee directors to disclose information to their nominating shareholders if authorised by the board of directors by general or specific mandate, provided that such disclosure is not likely to prejudice the company.

In relation to the duties of care and skill, Section 157(1) of the CA also provides that a director must use reasonable diligence in the discharge of the duties of his or her office. Directors have a continuing duty to acquire and maintain a sufficient understanding of the company’s business to enable the proper discharge of their duties. However, Section 157C of the CA allows directors to rely on information and advice prepared or supplied by employees, professionals and experts with respect to matters within their respective areas of competence. This statutory protection only applies if the director acts in good faith, makes proper inquiry where the need for inquiry is indicated by the circumstances and if the director has no knowledge that such reliance is unwarranted.

A director’s breach of duties may result in the following consequences:

a statutory liabilities: Section 157(3) of the CA provides that a director who breaches his or her statutory duties to act honestly and use reasonable diligence in the discharge of his or her duties, or makes improper use of his or her position as an officer or agent of the company or any information acquired by virtue of his or her position, will attract both civil and criminal liabilities. A director who is in breach of any of these statutory duties shall be liable to the company for any profit made by him or her or for any damage suffered by the company as a result of the breach. If he or she is guilty of an offence under the Companies Act (for example, by making a solvency statement without reasonable grounds or by authorising the making of payments to acquire the company’s shares when the company is not solven), he or she is also liable on conviction to a fine and/or imprisonment. Further, Section 331 of the SFA provides that where an offence under the SFA is committed by a listed company with the consent or connivance of, or is attributable to any neglect on the part of, a director, the director as well as the listed company will be guilty of the offence and liable to be proceeded against;

b liabilities under common law: breaches of common law duties also enable the company to take action against a director and sue for its loss;

c disqualification and debarment: in certain circumstances, a director may also be disqualified either automatically, or by a disqualification order made by the court against him or her, or be the subject of a debarment order. Such a director will be prohibited from taking part in the management of companies, whether directly or indirectly, during the period of the disqualification or disqualification order; and

d sanctions under the Listing Manual: under the Listing Manual, a director is required to immediately resign from the board of directors of a listed company if he or she is disqualified from acting as a director in any jurisdiction for reasons other than on technical grounds. Further, where the SGX-ST is of the opinion that a director or executive officer of a listed company has wilfully contravened any relevant laws, rules and regulations, or refused to extend cooperation to the SGX-ST or other regulatory agencies on regulatory matters, the SGX-ST may take action, including objecting to his or her appointment as an individual director or executive officer in any issuer for a period not exceeding three years. The SGX-ST may refer any contravention of the listing rules to the Disciplinary Committee and also refer possible breaches of directors’ duties to other relevant authorities.
A listed company's shareholders need to be satisfied regarding the independence and integrity of its directors. The CA and the SFA lay down the statutory framework governing directors' dealings with the company and securities of the company and its related corporations, and require that certain personal interests be disclosed and approved.

Under the SFA, the interests and any changes in interests of a director or any of his or her family members in securities of a listed company or any of its related corporations must be promptly disclosed to the listed company within two business days.\(^{28}\)

As fiduciaries, directors must not allow themselves to get into a position where there is a conflict between what they ought to do for the company and what they might do for themselves. An area in which conflicts of interest often arise is the entering into of transactions between the company and a director. Under the CA, a director who is in any way, whether directly or indirectly, interested in a transaction or proposed transaction with the company must, as soon as he or she is aware of the relevant facts, either declare the nature of his or her interest at a board of directors’ meeting, or send a written notice to the company containing details on the nature, character and extent of his or her interest in the transaction or proposed transaction with the company. However, this disclosure requirement is not applicable if the interest of the director consists only of being a member or creditor of a company that is interested in a transaction or proposed transaction with the first-mentioned company, if the interest of the director may properly be regarded as not being a material interest.\(^{29}\)

In addition to the above, subject to limited exemptions, the Listing Manual considers transactions between a listed company and any of its directors (and their respective associates) to be interested person transactions and, therefore, subject to the enhanced disclosure and approval requirements for such transactions.

### III Disclosure

The Listing Manual imposes a continuing obligation on a listed company to announce material information and make periodic reports. In particular, a listed company must announce any information known to it concerning it or any of its subsidiaries or associated companies that is necessary to avoid the establishment of a false market in the company's securities or would be likely to materially affect the price or value of its securities.\(^{30}\) The requirement does not apply to information that is confidential as a matter of law or where such particular information meets all of the following criteria:

- a reasonable person would not expect the information to be disclosed;
- the information is confidential; and
- the information:
  - concerns an incomplete proposal or negotiation;
  - comprises matters of supposition or is insufficiently definite to warrant disclosure;
  - is generated for the internal management purposes of the entity; or
  - is a trade secret.

A listed company must also observe the corporate disclosure policy set out in Appendix 7.1 of the Listing Manual, which prohibits a listed company from selective disclosure of

\(^{28}\) Section 133 of the SFA.

\(^{29}\) Section 156 of the CA.

\(^{30}\) See Practice Note 7.1 of the Listing Manual for further guidance on what constitutes such information.
information to certain parties without a legitimate corporate objective and also provides, among other things, illustrations of events that are likely to require immediate disclosure, stipulations on the clarification or confirmation of rumours or reports, and the content and preparation of public announcements.

Material information must be disclosed when it arises, even if during trading hours. The SGX will expect the issuer to request a trading halt to facilitate the dissemination of the material information during trading hours. As a guide, a trading halt requested for dissemination of material information will last at least half an hour after the release of the material information, or such other period as the exchange considers appropriate.

From 7 February 2020, listed companies may announce their financial statements either on a semi-annually or quarterly basis. Companies whose auditors have expressed an adverse or qualified opinion or have otherwise indicated concern over the ability to remain as a going concern must disclose their financial statements on a quarterly basis. In the case of interim financial statements (quarterly or half yearly, as the case may be, but excluding full year financial statements), a listed company’s directors must provide a confirmation that, to the best of their knowledge, nothing has come to the attention of the board of directors that may render the interim financial statements false or misleading in any material aspect. Apart from the general obligation on material information and the periodic reporting requirements above, the Listing Manual also imposes a higher threshold of disclosure for transactions between the listed company and its interested persons, and material transactions exceeding a specified threshold.

An interested person, in relation to a listed company, means a director, CEO or controlling shareholder, or an associate of any such director, CEO or controlling shareholder. An immediate announcement is required for any interested person transaction (IPT) of a value equal to or more than 3 per cent of the listed company’s latest audited consolidated net tangible assets (NTAs). If the aggregate value of all transactions (excluding transactions below S$100,000) entered into with the same interested person during the same financial year amounts to 3 per cent or more of the listed company’s latest audited consolidated NTAs, the listed company must make an immediate announcement of the latest transaction and all future transactions entered into with that same interested person during that financial year. Shareholders’ approval is required for any IPT of a value equal to or more than 5 per cent of the group’s latest audited consolidated NTAs, or 5 per cent of its latest audited consolidated NTAs, when aggregated with other transactions entered into with the same interested person during the same financial year (excluding transactions below S$100,000). Chapter 10 of the Listing Manual regulates acquisitions, realisations and, from 7 February 2020, the provision of financial assistance, by a listed company or its subsidiary (which is not listed on the SGX-ST or an approved exchange). Transactions that fall within the purview of Chapter 10 include an option to acquire or dispose of assets, but exclude an acquisition or disposal that is in the ordinary course of its business or of a revenue nature. Transactions are categorised as non-disclosable transactions, disclosable transactions, major transactions, and very substantial acquisitions or reverse takeovers, depending on the relative figures as computed on the bases set out in Rule 1006 (which formulates bases to assess the
size of the transaction based on factors such as the net asset value, net profits and consideration
for the transaction). The announcement and shareholder approval requirements depend on
the relative size of the transaction as regards the listed issuer. Disclosable transactions have to
be immediately announced, and the announcement must contain the specific information
prescribed under Chapter 10. Major transactions and very substantial acquisitions or reverse
takeovers must, in addition to an immediate announcement, be made subject to shareholder
approval.

IV CORPORATE RESPONSIBILITY

i Whistle-blowing

The Code provides that the audit committee is to review the policy and arrangements for
concerns about possible improprieties in financial reporting or other matters to be safely
raised, independently investigated and appropriately followed up on. Companies are to
publicly disclose, and clearly communicate to employees, the existence of a whistle-blowing
policy and procedures for raising such concerns.35

ii Sustainability reporting

The Listing Manual also requires listed companies to produce annual sustainability reports
on a comply or explain basis.

Issuers have to publish a sustainability report at least once a year, and the sustainability
report should describe the sustainability practices with reference to five primary components:
material environmental, social and governance factors; policies, practices and performance;
targets; sustainability reporting framework; and the board statement. Where the issuer cannot
report on any primary component, it must state so, and explain what it does instead and the
reasons for doing so.

Under the practice note issued by the SGX, the SGX does not advocate a particular
sustainability reporting framework, but issuers are advised to carefully select an appropriate
framework for their business model and industry. External assurance by independent
professional bodies is not mandatory; however, issuers that have been reporting for several
years may find it useful to undertake external assurance, which may increase stakeholder
confidence in the accuracy and completeness of the sustainability information disclosed.

V SHAREHOLDERS

i Shareholder rights and powers

As mentioned earlier, Section 157A of the CA provides that the business of a company shall
be managed by or under the direction of the directors. Nonetheless, there are certain matters
that require shareholder approval. Under the CA, these include:

a an alteration of or addition to the constitution of a company, subject to any entrenching
   provision in the constitution;

b the disposal of the whole or substantially the whole of a company's undertaking or
   property;

c the issue of shares by directors;

35 Provision 10.1 of the Code.
The following matters as prescribed under the Listing Manual also require shareholder approval:

- the issue of securities to transfer a controlling interest;
- share buy-backs;
- interested person transactions exceeding a certain threshold;
- major transactions, very substantial acquisitions and reverse takeovers; and
- voluntary delisting.

In relation to voluntary delistings of listed entities on the SGX, changes were implemented in July 2019, with enhanced protection for minority shareholders following SGX’s consultation in 2018. A voluntary delisting must be accompanied by an exit offer to allow shareholders a way to cash out before the delisting – from 11 July 2019, the SGX now requires the terms of such exit offer to be both fair and reasonable (and not just reasonable). In addition, the approval threshold for a listed entity to approve a voluntary delisting has been amended to 75 per cent of shareholders present and voting, with the offeror and its concert parties being required to abstain from voting. This is a significant change from the previous regime where all shareholders (regardless of their role in the exit offer) would be allowed to vote on the voluntary delisting resolution.

ii  Takeover defences

Transactions involving potential takeovers would also be governed by the principles under the Singapore Code on Take-overs and Mergers (Takeover Code), which is issued by the MAS and administered and enforced by the Securities Industry Council. Its primary objective is fair and equal treatment of all shareholders in a takeover or merger situation. When a target company’s board has been notified of a bona fide offer, or after the target’s board has reason to believe that a bona fide offer is imminent, the board cannot, without shareholders’ approval, take any steps that could effectively result in either the offer being frustrated, or denial of the target shareholders’ opportunity to decide on the merits of the offer.\(^{36}\) The target company’s board of directors must also obtain competent independent advice when it receives an offer or is approached with a view to an offer being made, and must subsequently inform the shareholders of the substance of this advice.\(^{37}\)

iii  Contact with shareholders

The Code provides that companies are to have in place an investor relations policy that allows for an ongoing exchange of views so as to actively engage and promote regular, effective and fair communication with shareholders. The company’s investor relations policy is to set out the mechanism through which shareholders may contact the company with questions and through which the company may respond to such questions. The Code provides that companies are to treat all shareholders fairly and equitably in order to enable them to exercise shareholders’ rights and have the opportunity to communicate their views on matters

\(^{36}\) Rule 5 of the Takeover Code.
\(^{37}\) Rule 7.1 of the Takeover Code.
affecting the company. Companies are to give shareholders a balanced and understandable assessment of the company’s performance, position and prospects. Companies are to provide shareholders with the opportunity to participate effectively in and vote at general meetings of shareholders and inform them of the rules governing general meetings of shareholders. The Code also provides that companies are to communicate regularly with shareholders and facilitate the participation of shareholders during general meetings and other dialogues to allow shareholders to communicate their views on various matters affecting the company. All directors are to attend general meetings of shareholders. Under the CA, shareholders have a right to inspect certain company documents. For instance, shareholders have a right to inspect or obtain from the Registrar of Companies copies of the registers of directors, CEOs, secretaries and auditors. Shareholders also have a right to be furnished with minutes of all proceedings of general meetings, and copies of financial statements. In cases where a shareholder has appointed a nominee to the board, the nominee director may also disclose company information to the shareholder provided that the disclosure is not likely to prejudice the company and is made with the authorisation of the board.

iv Shareholder activism

There are statutory remedies that allow minority shareholders seeking redress for a wrong committed against a company to commence action or arbitration in the name of the company pursuant to a derivative action, or for remedies on the grounds of minority oppression. Members are also given the right to requisition or call for a general meeting, subject to minimum shareholding requirements. In addition, members representing not less than 5 per cent of the total voting rights may make a requisition for a resolution to be proposed at an AGM.

VI OUTLOOK

Proposed amendments to strengthen oversight of audits of listed entities

In a consultation paper released on 16 January 2020, the SGX has sought feedback on the proposed amendments including a proposal that all issuers (including foreign incorporated issuers) must appoint an auditing firm and partner registered with ACRA and the qualifications of valuers engaged by listed entities on the SGX. These proposals are intended to enhance regulation of the audit process for SGX listed entities and the manner in which valuations are undertaken.

38 Principle 11 of the Code.
40 Principle 12 of the Code.
41 Provision 11.3 of the Code.
42 Section 12 of the CA.
43 Sections 189 and 203 of the CA.
44 Section 158 of the CA.
45 Sections 176 and 177 of the CA.
46 Section 183 of the CA.
I OVERVIEW OF GOVERNANCE REGIME

Listed companies in South Africa operate within a robust and flexible governance framework comprising statutes, regulations, common law, and both international and South African codes of best practice. The Companies Act 71 of 2008 is the primary source of company law in South Africa. Each public company is constituted in accordance with the Companies Act and its constitutional document, the memorandum of incorporation (MOI), which establishes the company's capacity, legal powers and governance.

Public companies whose securities are listed on the Johannesburg Stock Exchange (JSE), South Africa's main securities exchange, must adhere to various requirements imposed on them by the Listings Requirements of the JSE (Listings Requirements). Given the high levels of public interest in such companies, the Companies Act and the Listings Requirements together impose a demanding accountability and transparency regime.

Insofar as ‘good practice’ standards are concerned, the King IV Code on Corporate Governance (King Code), which is recognised as one of the world’s leading corporate governance codes, sets out principles and recommended practices that an organisation should apply in order to substantiate a claim that it is practising good governance, reflected in four outcomes: ethical culture, good performance, effective control and legitimacy. Certain

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1 Ezra Davids is a partner, Ryan Kitcat is a senior associate, and Lauren Midgley is an associate at Bowmans.
2 The Companies Act recognises two types of company: a profit company and a non-profit company. A profit company may be a private company (whose securities may not be offered to the public), state-owned company, personal liability company, or public company. This chapter focuses on public companies whose securities are listed on the Johannesburg Stock Exchange.
3 An object of the Companies Act is to create a facilitative and enabling corporate law regime. As such, companies are subject to certain ‘unalterable’ provisions of the Companies Act that prescribe core company law rules applicable to a company, with the remaining provisions being ‘alterable’ default provisions that apply to a company only to the extent that the MOI does not vary them. There is, therefore, a lot of flexibility in incorporating a company in South Africa.
4 The JSE is operated by JSE Limited.
6 The King IV Code on Corporate Governance forms part of the King IV Report on Corporate Governance™ for South Africa, 2016, issued by the Institute of Directors in Southern Africa NPC (IoDSA).
recommended practices in the King Code are incorporated into the Listings Requirements, making it mandatory for JSE-listed companies to comply with them, with the balance of the King Code’s recommendations to be implemented on an ‘apply and explain’ basis.

The philosophies underpinning the principles and recommendations in the King Code reflect and recognise three paradigm shifts that appear to be taking place globally: (1) from financial capitalism towards more inclusive capitalism, which takes account of all sources of capital – financial, manufactured, intellectual, human, social, relationship and natural – involved in the value-creation process; (2) from short-term capital markets towards long-term, sustainable, capital markets; and (3) from silo reporting towards integrated reporting, based on integrated thinking, which takes into account the connectivity and interdependencies between a range of exogenous factors (e.g., the economy, society and environment) and endogenous factors that affect a company’s ability to create value over time.

II CORPORATE LEADERSHIP

1. Board structure and practices

The business and affairs of a company must be managed by or under the direction of the board, which has the authority to exercise all of the powers and perform all of the functions of the company, except to the extent that the Companies Act or the company’s MOI provides otherwise. While shareholders still retain ultimate authority in respect of specific reserved matters (including the right to reconstitute the board), the Companies Act vests the board with original statutory authority – without any delegation from shareholders – regarding the conduct of the company’s business and affairs. Such power may only be exercised collectively by way of majority vote; in the absence of a specific delegation from the board, individual directors do not have the power to bind the company.

The traditional structure of a South African board is unitary, with no separation between executives and non-executives. The King Code contains various recommendations on board composition, including that the board comprise a majority of non-executives, most of whom should be independent. The Listings Requirements require that independence be determined holistically on a ‘substance over form’ basis, which takes into consideration various interests, positions and relationships listed in the Companies Act and the King Code that might reasonably call the integrity or objectivity of the director into question.

Typically, the board delegates the responsibilities of day-to-day operational management to an executive team, whose members are subject to board oversight and are appointed and dismissed at the behest of the board. The board may appoint any number of committees and may delegate to such committees any of its authority; however, the directors retain ultimate responsibility for the committees’ decisions and actions.

Available at: www.iodsa.co.za/page/KingIVReport. The IoDSA owns all copyright and titles in the ‘King IV Report on Corporate Governance for South Africa, 2016’. King IV™, King IV Report™ and King IV Code™ are trademarks of the IoDSA.

7 The King Code recognises that companies (and other organisations) are an integral part of society: they both contribute to and are dependent on society, and are affected by and have an effect (both positive and negative) on the societies in which they operate.

8 The King IV Report at 4-5 (‘Foreword’).

9 Section 66 of the Companies Act.

10 See Section V.i.
The Companies Act requires public companies to constitute an audit committee.\textsuperscript{11} Public, state-owned and certain significant private companies (i.e., those that have attained a certain ‘public interest score’ derived from factors such as annual turnover, workforce size, and nature and extent of activities) are required to appoint a social and ethics (S&E) committee.\textsuperscript{12} Under the Listings Requirements, ‘King compliant’ audit, remuneration and S&E committees are mandatory. Risk and nomination committees are only encouraged, although JSE-listed companies constitute such committees in practice.

JSE-listed companies must appoint a chairperson (or a lead independent director, in the event that the chair is not an independent non-executive) to lead the board, as well as a CEO to lead management. As independence is considered essential to the proper fulfilment of the chair’s role, the Listings Requirements insist that these positions be held by separate individuals. However, in certain limited instances, a dispensation may be granted by the JSE allowing an executive chair to be appointed on a temporary basis.

Non-executive directors have no automatic right to remuneration. Rather, the Companies Act provides that the company may pay its directors for their service in such capacity only in accordance with a special resolution approved by the shareholders within the previous two years. As such, the Companies Act places the decision of whether to remunerate individual directors squarely in shareholders’ hands, with a view to curtail excessive compensation and encourage good corporate governance.

\textbf{ii} Directors

\textbf{Appointment, nomination, removal and term of office}

In the case of a profit company other than a state-owned company, at least 50 per cent of the directors (and alternate directors) must be elected by shareholders. For the remainder, the MOI may include a right in favour of a person named in, or determined in terms of, the MOI to appoint a director; certain persons who hold office are also recognised as \textit{ex officio} directors.

Under the Companies Act, directors are appointed for an indefinite term, unless the MOI provides to the contrary. However, owing to the growing awareness surrounding the link between director tenure and independence, the King Code recommends that arrangements for periodic, staggered rotation be put in place. These arrangements should strike a balance between retention of valuable knowledge and experience on the one hand, with the need to infuse fresh ideas and perspectives into board decision-making on the other. As such, companies often provide in their MOIs for staggered retirement by rotation, whereby certain classes of directors (usually non-executives) retire at each annual general meeting (AGM), and then stand for re-election by shareholders. To prevent this process from becoming a mere formality, some companies have adopted policies limiting the duration for which non-executives may hold office. For JSE-listed companies, the annual retirement of at least one-third of non-executive directors is mandatory.\textsuperscript{13} The board will recommend whether each of such directors is eligible to stand for re-election, taking into account past performance and contributions made.

\begin{itemize}
  \item \textsuperscript{11} See Section III.
  \item \textsuperscript{12} See Section IV.
  \item \textsuperscript{13} In a new company, all directors must retire at the first AGM.
\end{itemize}
Shareholders have the right to remove a director for any reason by way of an ordinary resolution (which requires a simple majority threshold) adopted at a shareholders’ meeting by those entitled to exercise voting rights in such director’s election. To mitigate against the risk of director entrenchment, the Companies Act states that this shareholder right prevails despite anything to the contrary contained in a company’s MOI or rules, or in any other agreement.14

The board is also empowered to remove a director by way of resolution, but only on prescribed grounds pertaining to such director’s fitness to hold office, namely where the director has: (1) become ineligible or disqualified in terms of the Companies Act (e.g., where the director is labouring under a legal disability, or has been convicted of a dishonesty-related offence); (2) become meaningfully incapacitated; or (3) been neglectful or derelict in the performance of his or her functions as a director.15

Directors’ duties

The fiduciary duties of directors, as well as the duty of care and skill, have been partially codified in the Companies Act. However, the common law principles are preserved, informing the interpretation of, and filling gaps in, the statutory provisions.

All directors, be they executive or non-executive, owe the same fiduciary duties individually and directly to the company. A ‘director’ (which encompasses alternate directors, prescribed officers and members of board committees) must exercise his or her powers and functions in good faith and for a proper purpose, and in the best interests of the company.16

At common law, the duty to act in good faith and in the best interests of the company is the paramount and overarching fiduciary duty from which all others flow. These duties are to: (1) act within designated powers; (2) maintain and exercise unfettered discretion and independent judgement; and (3) avoid conflicts of interest.

The Companies Act has incorporated, and in some ways expanded upon, this latter integral common-law fiduciary duty. It prescribes that directors must: (1) not use their company position, or any information obtained while acting in such capacity, to gain a personal advantage or knowingly cause harm to the company or a subsidiary thereof;17 and (2) fully disclose any material personal financial interest that they may have in respect of any matter to be considered at a board meeting, and if present at the meeting, recuse themselves so as not to take part in the deliberation of the matter.18

While our courts draw no distinction between executive and non-executive directors when applying fiduciary duties, the duty of care and skill provides a court with scope to weigh the director’s specific role and function within the company. Section 76 of the Companies Act.

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14 Moreover, while the MOI may ordinarily set a higher percentage of voting rights to approve a resolution, the simple majority threshold cannot be varied in the case of a resolution effecting the removal of a director.

15 Regardless of circumstances, before any vote is cast on his or her removal, a director is afforded certain procedural rights under the Companies Act (and in accordance with common law rules of natural justice). These include the right to receive reasonable notice of the resolution, and a reasonable opportunity to make representations in his or her defence at the meeting.

16 Section 76 of the Companies Act.

17 Section 76 of the Companies Act.

18 Section 75 of the Companies Act.
Act requires that a director should at all times act with the degree of care, skill and diligence that may reasonably be expected of a person: (1) carrying out the same functions; and (2) with the general knowledge, skill and experience of that director.

In order to promote innovation and encourage calculated risk-taking by entrepreneurs, the Companies Act has adopted a US-style ‘business judgment rule’, which guards against court interference in directors’ honest errors of judgment. In essence, the rule provides that a director is deemed to have satisfied his or her duties if such director made an informed, unconflicted decision that he or she genuinely and rationally believed was in the best interests of the company.

**Liability**

Directors, prescribed officers and board committee members may be held jointly and severally liable for any loss, damages or costs sustained by the company as a consequence of having breached any of their duties, or for having breached the Companies Act or the company’s MOI.

Section 77 lists specific instances where a director may incur liability, including where a director knowingly: (1) acted without authority on behalf of the company; (2) acquiesced in the reckless trading of the company’s business; (3) conducted an act calculated to defraud stakeholders; or (4) was party to false or misleading communications to the market.

In limited instances, directors may also be subject to criminal penalties, particularly in instances involving fraud or dishonesty.

**Requirements and diversity**

Directors are not legally required to possess any special qualifications, skills, business acumen or experience in the company’s business to hold office. That said, the duty of care and skill is such that directors cannot avoid liability by remaining culpably ignorant of company affairs or blindly deferring to other board members or experts.

The King Code recommends that the board should comprise the appropriate balance of knowledge, skill, experience, diversity and independence for it to discharge its governance role and responsibilities objectively and effectively. In light of these recommendations, as informed by global trends, board diversity is becoming an ever-greater priority for South African companies; particularly in light of our unique history and the prevalent role that Broad-Based Black Economic Empowerment (B-BBEE) plays in our corporate environment.¹⁹

The traditional understanding of ‘diversity’ is also evolving in South Africa: the Listings Requirements have long required the adoption of policies that promote racial and gender diversity at board level, but a recent amendment²⁰ expands upon these diversity attributes to include culture, age, experience and skillset, in line with the King Code.

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¹⁹ See Section IV.
²⁰ Effective from December 2019.
III DISCLOSURE

The purposes of the Companies Act include encouraging transparency and high standards of corporate governance as appropriate, given the significant role of enterprises within the social and economic life of the nation.21 Under the Companies Act, all companies must report to shareholders annually on the state of the company. Public companies are required to hold an AGM at which certain minimum business must be conducted, including director elections and appointing an auditor. Public companies must also have their annual financial statements (AFS) audited.

The AFS, presented at the first shareholders’ meeting after being approved by the board, must contain certain prescribed information. In addition to an auditor’s report (if relevant), a detailed directors’ report on the business and financial condition of the company is required, such that shareholders are able to appreciate the state of the company affairs. Further, audited AFS must include a host of particulars regarding the emoluments received by directors and prescribed officers – on an individual basis, and not as an aggregate amount – including all fees, bonuses, options, pension contributions and any non-financial benefits.

Director remuneration has become a contentious issue in recent years. Responding to growing calls for transparency on this subject, the King Code includes a recommendation (which has been incorporated into the Listings Requirements) that companies should produce and disclose, in respect of a reporting period, a remuneration policy and a report on the implementation of that policy.22 This report must be tabled annually for a separate non-binding advisory vote by shareholders at the AGM. If 25 per cent or more of voting rights are exercised against any part of this remuneration policy, the board must engage with shareholders in good faith to understand shareholder dissatisfaction and the reasons for dissenting votes. The board is required to appropriately address reasonable and legitimate concerns raised in the evaluation of performance. Although the advisory vote given to shareholders is non-binding, this vote coupled with increased disclosure encourages the board to engage with shareholders, promotes transparency and provides shareholders with a platform to express their dissatisfaction.

The audit committee plays a vital role in ensuring that adequate accounting records are maintained and that company reporting is comprehensive and reliable. As such, the Companies Act mandates that all public companies must elect an audit committee at the AGM. In contrast to regular board committees, which are appointed by and derive their authority directly from the board, audit committees hold a special status as a statutory committee, appointed by (and by inference, accountable to) shareholders. These committees must comply with the composition requirements (e.g., at least three independent, financially literate members), and must carry out prescribed duties (e.g., nominating and confirming the independence of the company auditor), contained in the Companies Act.

21 Section 7 of the Companies Act.
22 The King Code recommends further detailed disclosures regarding: (1) each board committee; (2) the CEO; (3) risk management and governance; (4) stakeholder arrangements; and (5) inspections by environmental regulators, and any related findings of non-compliance or criminal sanctions.
The Listings Requirements contain various continuing disclosure obligations and General Principles regarding disclosure by listed entities to their securities holders and the general public, including to ensure that: (1) full, equal and timeous public disclosure is made regarding activities that are price sensitive; (2) full information is given regarding substantial changes in business operations and matters affecting the MOI; (3) the highest standards of care are adhered to when disseminating information into the market; and (4) the Listings Requirements promote investor confidence in disclosure standards and corporate governance. Accordingly, JSE-listed entities are subject to stringent financial reporting and disclosure requirements in key areas, including: (1) year-end and interim financial results and trading statements; (2) price sensitive information; (3) profit forecasts; (4) directors’ dealings; and (5) significant corporate actions.

Insofar as the application of the King Code is concerned, good corporate governance outcomes may be achieved through the King Code’s ‘apply and explain’ application and disclosure regime. That is, a company should: (1) mindfully consider and apply the recommended practices that underpin the King Code principles proportionally in line with the company’s size, resources, and the extent and complexity of its activities; and (2) provide a narrative account of that application, with reference to the recommended practices. This ‘apply and explain’ approach is intended to generate an account that allows stakeholders, including shareholders, to evaluate and independently assess the extent to which the company and its group is applying the principles and recommendations in the King Code. This account should be contained in an integrated report prepared by the company, which the King Code defines as a ‘concise communication about how an organisation’s strategy, governance, performance and prospects, in the context of its external environment, lead to the creation of value in the short, medium and long term’.

The King Code describes ‘materiality’ in relation to the inclusion of information (financial or other) in an integrated report as referring to matters that ‘could substantively affect the organisation’s ability to create value over the short, medium and long term’.

## IV CORPORATE RESPONSIBILITY

### Corporate citizenship

The purposes of the Companies Act include encouraging the efficient and responsible management of companies. Directors are obliged when making decisions to act in the best interests of the company. Reflecting the growing awareness of the integral societal role...
companies occupy, the Companies Act essentially promotes the ‘enlightened shareholder value’ approach: boards are permitted to take broader stakeholder interests into account, while remaining cognisant of their principal duty of maximising shareholder value.

The King Code adopts an approach to corporate citizenship based on the view that an organisation has rights, obligations and responsibilities in the society in which it operates. That is, a company is ‘licensed to operate by its internal and external stakeholders, and by society in the broad sense’.29 In recognition of the interdependent relationship between a company, its stakeholders and the company’s ability to create value, the King Code recommends a stakeholder-inclusive approach ‘in which the [board] takes into account the legitimate and reasonable needs, interests and expectations of all material stakeholders in the execution of its duties in the best interests of the [company] over time’.30 Consequently, directors must grapple with finding the right balance between these approaches when making decisions in the best interests of the company.31

S&E committee
The Companies Act requires public companies to appoint an S&E committee, which is meant to guide the organisation in fulfilling its role as responsible corporate citizen. The S&E committee’s functions include:

a monitoring the company’s activities, having regard to any relevant legislation, other legal requirements or prevailing codes of best practice, including the King Code, with regard to matters relating to:
• social and economic development;
• good corporate citizenship, including issues of discrimination, corruption, and development of local communities;
• the environment, health and public safety, including the impact of the company’s activities and of its products or services;
• consumer and employee relationships;

b reporting on matters within its mandate to the board as occasion requires; and
c reporting to shareholders on matters within its mandate at the company’s AGM.32

Risk management
The board is ultimately responsible for the company’s overall approach to risk, as expressed in a board-approved risk policy. The King Code embraces the modern approach to risk governance, which requires boards to appreciate not only the downside of risk, but also the upside, as materialised in potential opportunities and rewards. In this regard, the board should approve both the company’s risk appetite, and the limit of the potential loss the company can tolerate. The board must ensure that systematic, formal risk assessments are performed annually to identify, quantify, evaluate and prioritise risk. The annual report should incorporate a risk management statement that includes details of key risks relevant

29 King IV Report at 25 (‘Corporate citizenship’).
30 King IV Report at 17 (‘Glossary of Terms’).
31 Our courts have been known to take corporate governance practices recommended by the King Code into account when rendering judgment against errant directors: see, for example, South African Broadcasting Corporation Ltd and Another v Mpofu [2009] 4 All SA 169 (GSJ) and Minister of Water Affairs and Forestry v Stilfontein Gold Mining Co Ltd 2006 (5) SA 333 (W).
32 Regulation 43 of the Companies Regulations, 2011.
to the company and the steps taken to mitigate these risks. The board should allocate the oversight of risk governance to a dedicated committee, which should comprise executive and non-executive directors (with the latter forming the majority).

**Broad-Based Black Economic Empowerment**

As a measure to redress the legacy of apartheid, the legislature adopted the Broad-Based Black Economic Empowerment Act 53 of 2003 (B-BBEE Act) to increase levels of economic participation by previously disadvantaged race groups. Other than in certain state licensing, permitting and authorisation processes, there is no ‘hard law’ requiring any private entity to meet specific B-BBEE targets. However, various Codes of Good Practice under the B-BBEE Act must be taken into account by government entities when dealing with the private sector (e.g., selling state-owned assets and entering into public-private partnerships). As such, a low B-BBEE rating may constrain an entity’s ability to compete for business from the government, organs of state and even private sector customers (who, in turn, may be required to adhere to certain B-BBEE requirements – for instance, by ensuring that their own procurement is sourced from suitably empowered suppliers).

**Whistle-blowing**

Under the Protected Disclosures Act 26 of 2000 (PDA), employees who make certain disclosures of unlawful or irregular conduct by employers or fellow employees are protected against victimisation or any ‘occupational detriment’ (such as dismissal, demotion or harassment). Section 159 of the Companies Act, which is intended to complement the PDA, provides safeguards to company stakeholders, including shareholders, directors and employees, who make good faith disclosures of specific wrongful or unlawful acts of a company, director or prescribed officers. Such whistle-blowers are immune from civil, criminal or administrative liability and have qualified privilege in relation to the disclosure.

V SHAREHOLDERS

i Shareholder rights and powers

Shareholders are entitled to attend, speak and vote at a meeting, either themselves or via proxy. This allows shareholders to ask difficult questions of directors, express their views or lobby support from other shareholders for a particular agenda (e.g., a ‘vote no’ campaign).

Shareholders have the ability to requisition a shareholders’ meeting by delivering signed demands to the company, specifying the purpose for which the meeting is proposed. If the company receives, in aggregate, demands from holders of at least 10 per cent of the voting rights entitled to be exercised in relation to the matter proposed, it must call a meeting unless the company or another shareholder successfully applies to court to set aside the demand on the grounds that it seeks only to reconsider a matter that has already been decided by shareholders, or is frivolous or vexatious.

Any two shareholders of a company may propose that a resolution concerning any matter in respect of which they are each entitled to exercise voting rights (e.g., the removal of a director) be submitted to shareholders for consideration at the next shareholders’ meeting, at a meeting demanded by shareholders or by written vote.
Although the board is imbued with wide-ranging statutory powers to manage company affairs,\(^{33}\) the board must defer to shareholders on certain prescribed matters requiring their approval, either by way of an ordinary resolution or special resolution (requiring a 75 per cent approval threshold). Key examples of matters requiring ordinary resolutions are the appointment and removal of directors under the Companies Act, and the entering into of a Category 1 transaction (being principally substantial acquisitions and disposals) under the Listings Requirements. Special resolutions are required for matters concerning fundamental company affairs, such as amending the MOI or entering into a fundamental transaction (e.g., statutory mergers, schemes of arrangement, and disposals of all or a greater part of a company’s assets or undertaking).\(^{34}\) The Listings Requirements provide an overlay of special resolution matters (e.g., the carrying out of a general repurchase of securities).

The Companies Act contains a range of remedies and protective mechanisms for shareholders. The statutory derivative action contained in Section 165 enables a shareholder (among other stakeholders) to demand that the company bring or continue proceedings, or take related steps, to protect the legal interests of the company.\(^{35}\) A company may apply to court to set aside the demand only on the grounds that it is frivolous, vexatious or without merit.

In extreme cases, a shareholder may apply to court for an order necessary to protect any right of the shareholder, or rectify any harm done to the shareholder by: (1) the company due to an act or omission that contravened the Companies Act, the MOI or the shareholder’s rights; or (2) any director of the company, to the extent that he or she is or may be liable for a breach of fiduciary duties. Similarly, a shareholder may apply to court for appropriate relief if: (1) any act or omission of the company has had a result; (2) the business of the company is being carried on in a manner; or (3) the powers of a director, prescribed officer or related person are being exercised in a manner that is oppressive or unfairly prejudicial, or unfairly disregards the interests of that shareholder. Having considered the application, the court may make any interim or final order it considers fit, including an order restraining the conduct complained of, ordering a compensation payment, or varying or setting aside an agreement or transaction.

Shareholders also have the right to bring a claim for damages against any other person who intentionally, fraudulently or due to gross negligence causes the company to do anything inconsistent with the Companies Act.

Dissenting minority shareholders may, in certain prescribed circumstances (e.g., fundamental transactions), force the company to purchase its shares in cash at a price reflecting fair value.\(^{36}\) This is a ‘no fault’ appraisal right that enables a shareholder to sell all of its shares and exit the company. It applies if the shareholder notified the company of its

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33 See Section II.i.

34 In certain instances, the Companies Act and the Listings Requirements impose more stringent requirements for the passing of a special resolution. For instance, resolutions proposing fundamental transactions require shareholder approval be obtained at a quorate meeting of 75 per cent of disinterested shareholders present and voting (i.e., excluding voting rights of the acquirer and related or concert parties). Similarly, in respect of JSE-listed companies undertaking related party transactions, the votes of related parties and their associates will not be taken into account in the approval of any resolution in connection with the related party transaction.

35 A trade union or employee representative may also bring a statutory derivative action to protect the company’s legal interests.

36 Section 164 of the Companies Act provides for appraisal rights.
objection to the resolution to approve the action or transaction, and the shareholder voted against the resolution (which was nonetheless approved) and complied with various exacting procedural requirements.

If 15 per cent or more of shareholders vote against a resolution proposed for implementing a fundamental transaction, any dissenting shareholder may require the company, at its expense, to obtain court approval before implementing the resolution. A single dissenting shareholder may also apply to court, at its expense, to have a resolution set aside. A court may only set aside the resolution if it is satisfied that there is manifest unfairness to shareholders or a material procedural irregularity.

Where an offer for a target company has been accepted by at least 90 per cent of the target company's disinterested shareholders, the Companies Act allows a buyer to initiate a minority ‘squeeze out’, by compulsorily purchasing the remaining shares held by non-accepting shareholders. However, Section 124 provides a measure of protection to minority shareholders in such instances, by not only empowering them to compel the buyer to take up their shares, but also allowing them to apply to court for an order prohibiting the ‘squeeze-out’ or imposing conditions thereon (usually on the basis that the offer is unfair).

**Shareholders’ duties and responsibilities**

Shareholders, be they controlling or otherwise, owe no fiduciary or statutory duties to the company or other shareholders. Based on the principle of separate legal personality, shareholders are not liable for the company’s acts or omissions. Only under exceptional circumstances may a court attribute personal liability to a shareholder who has abused the principle of corporate personality under the common law, or rely on the statutory mechanism in the Companies Act to ‘pierce the corporate veil’ where an ‘unconscionable abuse’ of a company’s separate juristic personality has transpired.

The Companies Act contains disclosure obligations impacting on-market or off-market stake-building by shareholders. Persons who acquire or dispose of a beneficial interest in securities, such that they hold or no longer hold 5 per cent or any further multiple of 5 per cent of the voting rights attaching to a particular class of securities, must notify the issuer within three business days thereof. This applies irrespective of whether the acquisition or disposal was made directly, indirectly, individually or in concert with any other person, and options and other interests in securities must be taken into account.

Institutional investors, such as pension funds, mutual funds, and insurers, may be required to engage in stewardship activities by virtue of obligations to responsibly manage their investments in JSE-listed companies – particularly insofar as sustainability and environmental, social and governance (ESG) factors are concerned. For example, pension funds in South Africa are obliged, before making an investment in and while invested in an asset, to consider any factor that may materially affect the sustainable long-term performance of the asset, including those of an ESG character. A recent guidance note issued on such requirement by the Financial Sector Conduct Authority (FSCA) – the body responsible for enforcing the market conduct rules of financial institutions under the Financial Markets Act 19 of 2012 (FMA) – contemplates ‘active ownership’ by pension funds, being the prudent fulfilment of responsibilities relating to the ownership of, or an interest in, an asset. These

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37 Section 115 of the Companies Act.
38 The issuer then has 48 hours to disclose the acquisition/disposal to the market and shareholders.
39 Regulation 28 of the Pension Funds Act 24 of 1956.
responsibilities include guidelines to be applied for the identification of sustainability concerns in that asset, and mechanisms of intervention and engagement with the responsible persons in respect of the asset when concerns have been identified.  

iii  Shareholder activism

Shareholder activism has gradually been on the rise in South Africa. This trend can be attributed to numerous factors, including South Africa’s regulatory and corporate governance framework, which creates an enabling environment for shareholder activism or activist-like interventions. In addition to the array of shareholder rights and protections under the Companies Act, each iteration of the King Report has included ever-increasing recommendations regarding greater shareholder participation, thereby entrenching the position that shareholders have an active role to play in policing good governance.

Historically, most shareholder campaigns in South Africa have focused on executive compensation and board composition. On remuneration, following the introduction of ‘say-on-pay’ rules, certain JSE-listed companies have had to reconsider their remuneration policies following significant shareholder opposition to such policies or implementation reports. On board composition, campaigns have forced companies to take steps to change the make-up of their boards or pushed for the resignation of the CEO. The most notable example of this was in 2014, involving PPC, a cement manufacturer, where activists sought to remove the entire board. In the M&A context, the influence of shareholder activism is also gradually increasing. Shareholders have intervened to block or force certain M&A activity. Recent examples of the former include shareholder opposition to a proposed takeover of PPC, and Prudential’s opposition to an attempted takeover of poultry producer Sovereign Foods by Country Bird Holdings. An example of the latter is Grand Parade Investment’s disposal of its interests in certain franchises.

JSE-listed companies that are involved in or fund carbon-intensive industries are experiencing increased shareholder activism in respect of sustainability and ESG issues, from both institutional investors and NGOs (such as Just Share, the Raith Foundation and the

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40 FSCA Guidance Notice 1 of 2019 (June 2019): Sustainability of investments and assets in the context of a retirement fund’s investment policy statement.

41 Other factors include: (1) the influence of shareholder activism in other jurisdictions, mainly the US and Europe; (2) a widely held market with an internationalised shareholder base; and (3) a greater tendency towards active engagement by institutional and other investors, as facilitated by more efficient media platforms and other technological advancements that aid communication.

42 See Section V.i.

43 During 2014, a group of shareholders requisitioned a special shareholders’ meeting to consider the removal of the entire board of PPC and to replace it with the nominees of the requisitioning shareholders. These measures successfully forced the board to engage with the requisitioning shareholders’ concerns.

44 In 2018, PPC was the subject of a merger attempt by a consortium comprising its smaller rival AfriSam and a Canadian investment house, Fairfax Financial Holdings. This failed as a result of shareholder resistance to a perceived undervaluation of PPC. Following failure of the proposed transaction, activist shareholders pressed for the removal of the chairperson and reconstitution of the PPC board.


46 In February 2019, Grand Parade Investments (GPI) announced that it was exiting its interests in the Dunkin’ Donuts and Baskin-Robbins franchises. A consortium of disgruntled minority shareholders had long pushed for GPI to exit these chains, given their track record of underperformance.
Centre for Environmental Rights). Recent instances of this activism have sought to compel companies to: (1) report on and disclose information on their assessment of greenhouse gas emissions attributable to their activities or portfolio; (2) develop policies on the funding of carbon-emitting operations; and (3) develop and disclose plans to protect shareholder value in the face of climate-related ‘transition risks’.

With regard to short-selling, while the regulatory framework recognises the important role that short-sellers can play in holding management accountable and ensuring that markets operate efficiently, it does not permit market abuse, which is prohibited under the FMA. In November 2018, following campaigns conducted by short-sellers that had a disruptive effect on the markets, the FSCA published a ‘Discussion Paper on the Implementation of a Short Sale Reporting and Disclosure Framework’. Discussions on the proposed framework are ongoing.

Insofar as debates around ‘short-termism’ versus the creation of long-term shareholder value are concerned, the King Code encourages boards to avoid prioritising narrow, short-term objectives at the expense of the company’s prospects for growth and profitability over the long term.

**Takeover defences**

Takeovers and ‘affected transactions’ (e.g., statutory mergers, schemes of arrangement and disposals of all or a greater part of a company’s assets or undertaking) are regulated under Chapter V of the Companies Act and the Takeover Regulations promulgated under that Act. In the context of such transactions, the Takeover Regulation Panel (TRP) is mandated to ensure the integrity of the marketplace and fairness to securities holders, and to prevent actions by offeree companies designed to impede, frustrate or defeat an offer or the making of fair and informed decisions by securities holders.

The Companies Act contains a ‘catch-all’ rule that restricts ‘frustrating action’ in the context of an offer. If the board of a regulated company has received a bona fide offer (or believes one may be imminent), it may not, without the approval of each of the TRP and the holders of the relevant securities, take any action in relation to the affairs of the company that could effectively result in: (1) a bona fide offer being frustrated; or (2) the relevant securities holders being denied an opportunity to decide on the merits. Examples of ‘frustrating action’

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47 Under the FMA, market abuse offences include: (1) prohibited trading practices (e.g., knowingly engaging in practices which create an artificial price or false appearance of demand for a security); and (2) false, misleading or deceptive statements (e.g., publishing any statement, promise or forecast in respect of a listed company which the person knows is materially false, misleading or deceptive).


51 The TRP has the power to initiate or receive complaints, conduct investigations and issue compliance notices.

52 Section 126 of the Companies Act.

53 Unless such action was taken in terms of a pre-existing obligation/agreement.
under the Companies Act include: (1) issuing or granting options in respect of unissued securities; (2) disposing or acquiring a material asset; (3) making an abnormal distribution; and (4) entering into contracts outside the ordinary course of business.

The rule against ‘frustrating action’ therefore makes it difficult for a board to ward off a hostile bidder by adopting takeover defences common in the US, such as a shareholder rights plan (poison pill). However, there are various steps that the board could legitimately take, which would have the effect of creating hurdles in the implementation of the hostile bid, without necessarily constituting ‘frustrating action’ – for instance, mobilising opposition by key stakeholders with respect to the takeover.

Contact with shareholders

Contact with shareholders is an important feature of corporate governance in South Africa. Shareholders regularly pursue one-on-one or collaborative engagement with listed companies on a range of issues. Good practice codes such as the United Nations-supported Principles for Responsible Investment (UN-PRI) and Code for Responsible Investment in South Africa promote ‘active ownership’, responsible stewardship, and collaborative engagement by institutional investors, particularly in respect of ESG issues.

The FMA includes rules prohibiting insider trading and market abuse. Shareholders must adhere to these provisions when engaging with management or pursuing stewardship activities, whether engaging with management one-on-one or collaboratively with other shareholders. A shareholder may become an ‘insider’ by becoming privy to ‘inside information’ for the purposes of the FMA, at which point insider trading rules would apply to it.

Collaborating shareholders should take into account ‘acting in concert’ rules under the Companies Act and Takeover Regulations. As a general principle, provided the collaboration is not for the purpose of proposing or entering into an ‘affected transaction’ or offer, the collaboration would not amount to acting in concert. As such, there is considerable scope for shareholders to come up with collaborative engagement plans to conduct stewardship and other activities. We expect a significant amount of contact with shareholders in relation to ESG and sustainability issues going forward.

The King Code promotes proactive shareholder engagement through a number of its recommendations. Among other things, the King Code recommends that the board

54 The FMA defines ‘inside information’ as ‘specific or precise information, which has not been made public and which – (1) is obtained or learned as an insider; and (2) if it were made public, would be likely to have a material effect on the price or value of any security listed on a regulated market’.

55 There are three broad categories of insider trading offences under the FMA: (1) dealing offences (e.g., when an insider, who knows he or she has inside information relating to listed securities, deals in those securities to benefit him- or herself or another person); (2) disclosure offences (e.g., when an insider knowingly discloses inside information); and (3) influencing offences (e.g., when an insider knowingly encourages another person to deal in listed securities likely to be affected by inside information).

56 The Companies Act regards concert party conduct as any action pursuant to an agreement between or among two or more persons, in terms of which any of them cooperate for the purpose of entering into or proposing an affected transaction or offer.

57 In 2010, UN-PRI published guidance on this particular issue, following engagements between the PRI South Africa Network Engagement Working Group and the TRP. Available at: https://cdn.ymaws.com/www.iodsa.co.za/resource/collection/58CA7BC8-8C67-4CF7-A644-0EDB06165C8B/2013.05.14_PRI_Collaborative_Engagement_Guidance.pdf.
encourage shareholders to attend the AGM, at which all directors should be available to respond to shareholders’ queries. In line with the ‘stakeholder inclusive’ approach, the King Code recommends the adoption of comprehensive policies on stakeholder relationship management, and that engagement take place through media platforms designed to facilitate access by a broad range of stakeholders, such as websites, advertising and press releases.

VI OUTLOOK

The proliferation of high-profile corporate governance failures in South Africa – notably the 2017 saga involving alleged accounting irregularities at Steinhoff – has intensified public interest in, and regulatory scrutiny of, corporate governance. Listed companies that simply pay lip-service to corporate governance, viewing compliance as a ‘tick box’ approach unconnected to the long-term viability of their businesses, will undoubtedly experience increased levels of activism and calls from shareholders for ever-greater levels of accountability and transparency from the companies in which they are invested.

We expect sustainability and ESG issues to feature high on the corporate governance agenda in the coming years, for boards and shareholders (particularly institutional investors) alike.58

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Chapter 21

SOUTH KOREA

Hyeon Deog Cho, Min Yung Hong, Yeong-Ik Jeon and Jung-Chull Lee

I OVERVIEW OF GOVERNANCE REGIME

i Sources of law and enforcement

The Korean Commercial Code (KCC) is the basic law on corporate governance in South Korea. Additional matters regarding the governance of listed companies are stipulated in the Listing Rules on the Securities Market, the Listing Rules on the KOSDAQ Market and other rules set forth by the Korea Exchange (KRX), which have been established by the Financial Investment Services and Capital Markets Act (FSCMA) and the special rules for listed companies set forth in the KCC.

The Act on Corporate Governance of Financial Companies (Corporate Governance Act) shall apply in preference to the KCC with respect to the corporate governance of financial companies.

Although they are not related to corporate governance, the FSCMA sets forth separate rules for matters related to finance such as the issuing of new shares of a listed company or restructuring (including mergers and spin-offs), as well as various disclosures, such as the registration statement.

The Ministry of Justice (MOJ) is responsible for the issuance of ex ante rulings under the KCC, and for the ex post facto imposition of fines or other sanctions for any breach of the KCC.

The Financial Services Commission (FSC), and the Financial Supervisory Service (FSS), which has been delegated with certain authorities of the FSC, are responsible for the issuance of rulings under the Corporate Governance Act and the enforcement thereof (including sanctions).

The KRX also manages and regulates listed companies through the examination and management of listings.

ii Nature and recent development of the corporate governance regime

In terms of corporate governance, under the KCC joint-stock companies and limited companies, which are the most common corporate entity forms in Korea, have four corporate governance bodies:

a the general shareholders’ meeting;

b a board of directors composed of registered directors of the company;

c a representative director or directors appointed among the directors; and

d a statutory auditor or auditors, or an audit committee.

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1 Hyeon Deog Cho and Min Yung Hong are senior attorneys, Yeong-Ik Jeon is an attorney, and Jung-Chull Lee is a foreign attorney at Kim & Chang.
Among these bodies, the general shareholders’ meeting is the supreme decision-making body, and it determines fundamental matters pursuant to the KCC and the articles of incorporation of the company. The board of directors makes decisions on important operational matters that are not specially reserved for the resolution of the general shareholders’ meeting by the KCC and the articles of incorporation. Boards of directors consist of executive directors, outside directors, and non-executive, non-outside directors. Given that executive directors generally become members of the management, the management and the board of directors are not always clearly distinguished. The representative director has the authority to perform matters resolved by the board of directors, and to decide and perform ordinary management activities. The statutory auditor or the audit committee supervises the management of the company’s business and audits the company’s financials and accounts.

Amendments to the KCC in 2012 introduced the executive officers governance structure, consisting of officers who are not registered directors but who are responsible for carrying out the company’s daily operations and implementing decisions of the board of directors, and decisions of the general shareholders’ meeting under the supervision of the board of directors.\(^2\) If a company decides to have executive officers under its articles of incorporation, there will be no representative director. Accordingly, the company will be able to clearly distinguish the management and the board of directors by separating the executive functions from the board of directors; however, there have not been many cases where such structure has been actually used in Korea.\(^3\)

Following the recent introduction of a stewardship code, which is accepted by the National Pension Service and other institutional investors, and the increased role of proxy advisory organisations, demands for the improvement of the governance regime, including management transparency, board diversity and the expertise of outside directors, has been growing. Accordingly, there has been an increase in the number of women, foreigners and professional managers being appointed as outside directors, and increased emphasis has been placed on the qualification of the independence of outside directors and audit committee members.

In particular, seeking board-focused management, the Corporate Governance Act stipulates that the chief operating officer, who is in charge of strategic planning, financial management, risk management and other major issues, shall be appointed or dismissed by a resolution of the board of directors.

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2. Articles 408-2 to 408-9.

3. In Korea, discussions continue regarding using governance restructuring to reinforce the independence of boards of directors and statutory auditors (and audit committees) from controlling shareholders. Related to this issue, the MOJ has taken the following actions: (1) in March 2018, it submitted an opinion on 13 pending bills related to improving corporate governance with the National Assembly’s Legislation and Judiciary Committee; and (2) in March 2019, it announced that it will push for the proposed amendments to the KCC, which includes the introduction of multi-step derivative actions, mandatory electronic and cumulative voting system for large public companies, and separate election of audit committee members.
II CORPORATE LEADERSHIP

i Board structure and practices

Under Korean law, boards of directors shall have a single-tier structure. Except with regard to small companies, a board of directors may not be replaced, as it is an essential body that is required under the KCC.

However, the KCC adopts a committee within the board of directors system, whereby a committee established within the board of directors may be delegated with certain authorities of the board of directors and resolve on relevant matters. Under the KCC, the board of directors may decide whether to establish any committee at its own discretion pursuant to the company’s articles of incorporation.

A listed company with total assets equal to or greater than 2 trillion won as of the end of the latest fiscal year (thus being a large listed company) must establish an audit committee and a committee to recommend outside director candidates.

Financial companies are obliged to establish:

a a committee in charge of recommending candidates for outside directors, representative directors and audit committee members;

b an audit committee;

c a remuneration committee; and

d a risk management committee.

The independence of the audit committee has been strengthened: at least two-thirds of the audit committee of a financial company or a large listed company is required to be composed of outside directors.

In addition to these legally required committees, listed companies are increasingly requiring the professional examination of a separate committee: for example, an internal transaction committee that examines the fairness of transactions between affiliates and specially related parties, or a remuneration committee that examines the remuneration system for directors and officers.

Composition of the board

The board of directors shall be composed of at least three directors, and there is no limit on the maximum number of board members. However, a company whose paid-in capital is less than 1 billion won may elect not to establish a board of directors.

Specifically, at least one-quarter of the total number of directors appointed in listed companies shall be outside directors, and large listed companies (i.e., those with assets of 2 trillion won or more) shall have at least three outside directors who will constitute a majority of the total number of directors. Furthermore, a recent amendment to the FSCMA prohibits a large listed company’s board from comprising members from a single gender.

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4 Article 393-2 of the KCC.
5 Articles 542-8 and 542-11 of the KCC.
6 Article 16 of the Corporate Governance Act.
7 Article 383 of the KCC.
8 Article 542-8 of the KCC.
9 The National Assembly passed this amendment to the FSCMA on 9 January 2020. It has been announced that the amendment will become effective on 5 August 2020, subject to a two-year grace period from the effective date of the amendment for this obligation.
Company representatives

In principle, the representative director represents the company externally, and has the authority to undertake matters resolved by the board of directors, and to decide on and perform ordinary management activities internally. The board of directors has the authority to make material decisions regarding the company (e.g., the disposal or transfer of its material assets and the borrowing of large-scale property).\(^{10}\)

In addition, Korean courts consider that a resolution of the board of directors shall be required for important matters that have not been generally and specifically delegated to the representative director by the board of directors and that do not fall under ordinary day-to-day operations.\(^{11}\)

Directors participate in the decision-making processes of the board of directors, and exercise a supervisory role over the operations of the representative director or representative executive officer. However, in principle, a director may not represent a company without a delegation of the board of directors, the representative director, or both.

Legal responsibilities of the board

Directors shall be jointly and severally liable for damage suffered by the company if they have violated any law or the articles of incorporation due to their wilful misconduct or negligence, or if they have neglected their duties. If the foregoing acts have been conducted in accordance with a resolution of the board of directors, the directors who have consented to such resolution shall assume the same liability against the company.\(^{12}\)

Directors may be exempt from the foregoing liabilities pursuant to unanimous shareholders’ consent (this is highly unlikely for listed companies). The 2012 amendments to the KCC also provide that a director’s liability that exceeds six times his or her annual salary (or three times, in the case of outside directors) may be exempt if the company has set forth relevant matters regarding this in the articles of incorporation in advance.\(^{13}\) However, such limits on liability shall not apply in certain cases, such as damage caused by a director’s wilful misconduct or gross negligence, or by his or her violation of certain regulations regarding self-dealing provided under the KCC.

Directors may be liable under the Criminal Act for breach of fiduciary duty if they have breached their duty of care as bona fide managers or their fiduciary obligation to the company, and if the company has suffered damage due to such breach and such director or third party profited therefrom.\(^{14}\)

\(^{10}\) Article 393 of the KCC.
\(^{11}\) The courts view that, if a representative director acts for and on behalf of a company at his or her own discretion without obtaining a resolution of the board of directors, even when such an act requires the resolution of the board of directors, the relevant transactional activity shall be effective unless the counterparty knew or was able to know that the resolution of the board of directors had not been obtained. In such case, the company asserting that the counterparty knew or was able to know that the resolution of the board of directors had not been obtained shall assume the responsibility to verify such fact.
\(^{12}\) Article 399 of the KCC.
\(^{13}\) Article 400 of the KCC.
\(^{14}\) Article 355, Paragraph (2) of the Criminal Act.
Control of the board

In principle, meetings of the board of directors may be convened by any director. However, the articles of incorporation typically provide that the representative director is authorised to convene meetings of the board of directors. Any director may convene meetings of the board of directors if he or she is authorised to convene such meetings by a resolution of the board of directors.15

Usually, the representative director concurrently holds the position as chair of the board of directors, and has the authority to convene board meetings. Accordingly, in most cases the representative director, who doubles as chief executive officer and chair of the board, also leads the board of directors and management.

In principle, a financial company shall appoint an outside director as the chair of the board of directors. If a financial company appoints a person who is not an outside director as chair, a representative of the outside directors shall be appointed separately.16

Generally, although they are not legally obliged to do so, listed companies are increasingly appointing an outside director as the chair of the board of directors to ensure the objectiveness and independence of the board’s examination procedures.

Delegation of board responsibilities

As the representative director represents the company, the general practice is to affix the seal of the company and attach the certificate of the corporate seal impression issued by the court on him or her so that he or she can carry out the company’s external activities (including the execution of agreements).

In principle, the board of directors has the authority to make material company decisions, and to delegate certain authorities to committees within the board of directors.17

The board of directors may also delegate certain duties (except for matters requiring a resolution of the board of directors or any committee) to the representative director. Generally, a company’s internal regulations stipulated by a resolution of the board of directors determine the matters on which the representative director is authorised to make decision at his or her own discretion without obtaining a resolution of the board of directors.

Separation of the roles of CEO and chair

There is no express provision on the authority or responsibility of the chair of a board of directors under the KCC. However, it is usually provided in the articles of incorporation that the representative director shall concurrently hold the position of chair of the board of directors. The chair shall assume the same responsibilities as other directors.

The representative director has the authority to perform business on behalf of the company, and the chair has the authority to convene and proceed with meetings of the board of directors.

Direct communication with shareholders

There is no law or regulation restricting the representative director or the chair from directly communicating with shareholders.

15 Article 390 of the KCC.
16 Article 13 of the Corporate Governance Act.
17 Article 393-2 of the KCC.
However, as the regulations on fair public disclosure apply to listed companies, and the FSCMA sets forth regulations on insider trading, a listed company’s communications with its shareholders are subject to the limits set forth therein.

**Remuneration of directors and senior management**

The general practice is to have a cap on remuneration for all directors resolved at the general shareholders’ meeting, and the amount of remuneration for respective directors resolved by a resolution of the board of directors.\(^{18}\)

For financial companies, matters regarding the methods for the determination and payment of the remuneration of officers (excluding outside directors, non-standing directors, audit committee members, compliance officers and risk management officers) need to be resolved by the remuneration committee, which is a committee established within the board of directors.\(^{19}\)

There is no special provision on the amount of remuneration of non-registered officers (senior management). The general practice is to determine such amount at the representative director’s own discretion or under regulations on officer remuneration resolved by the board of directors.

**Committees**

The board of directors may establish internal committees under the board, such as an audit committee.\(^ {20}\)

Large listed companies must establish an audit committee and a committee to recommend outside director candidates.\(^ {21}\) Financial companies are also required to establish an officer candidate recommendation committee, audit committee, remuneration committee and risk management committee.\(^ {22}\)

Matters resolved by the committees (excluding the audit committee) may be resolved again by the board of directors.\(^ {23}\)

**Board and company practice in takeovers**

In the case of a hostile takeover, it may be possible for a board of directors to use defence tactics such as the acquisition of treasury shares or the issuance of new shares to friendly third parties, including specific shareholders. To issue new shares to friendly third parties, however, express grounds should be given in the articles of incorporation, and other regulatory issues exist (e.g., the issuance price will be restricted under the FSCMA). Furthermore, in a dispute over management control, the issuance of new shares to friendly shareholders for the purpose of defending against such dispute is likely to be invalidated by court.

A listed company may acquire treasury shares by a resolution of the board of directors in an amount up to its distributable profits, and may use methods such as tender offers or purchases on exchange.\(^ {24}\)

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18 Article 388 of the KCC.
19 Article 22 of the Corporate Governance Act.
20 Article 393-2 of the KCC.
21 Articles 542-8 and 542-11 of the KCC.
22 Article 16 of the Corporate Governance Act.
23 Article 393-2 of the KCC.
24 Article 165-3 of the FSCMA.
To defend against a hostile takeover, the articles of incorporation can stipulate the supermajority voting system for certain agendas of the general shareholders’ meeting, including the dismissal of directors, or the golden parachute system, which requires the payment of a substantial amount of severance pay upon the dismissal of directors; however, it remains controversial whether these systems are permitted under the KCC.

**ii Directors**

Under Korean law, there is no difference between outside directors and executive directors in terms of their authority, obligations and responsibilities.  

Due to their independent status, there has been a lot of criticism about outside directors, with the contention being that they merely act as a rubber stamp without assuming actual roles in supervising the management of companies. However, outside directors have recently been expanding the scope of their actual participation in board of director decision-making processes by raising their opposition to specific agenda items or requesting additional examination.

In principle, notice shall be given to directors and statutory auditors no later than one week prior to a meeting of the board of directors in order to convene the meeting of the board of directors. This period may be shortened by the articles of incorporation, and the meeting may be held without convocation upon unanimous consent of all the directors and statutory auditors.

There is no express statutory provision on whether outside directors are allowed or obligated to directly visit a subsidiary of the relevant company or engage in direct communication with lower management or employees. However, it would be difficult for outside directors to force such visits or communication without the permission of the management of a subsidiary, since the independence of an entity cannot be denied even for subsidiaries.

**Legal duties and best practice**

In terms of legal duties, there is no distinction between executive (inside) directors and outside directors. Both are obliged to perform their duties for the company in good faith in accordance with their duty of care as bona fide managers, and in accordance with the law and the articles of incorporation.

**Liability of directors**

A director shall be liable for damage suffered by the company if he or she has violated any law or the articles of incorporation due to his or her wilful misconduct or negligence, or has neglected his or her duties. If the foregoing acts were performed in accordance with a resolution of the board of directors, the directors who have consented to such resolution shall assume joint and several liability against the company.

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25 There can be an actual difference, however, in the accessibility to a company’s information between executive directors who are engaged in the ordinary business affairs of the company and who are members of the company’s management; and outside directors who have limited involvement in the management of the company.

26 Article 390 of the KCC.

27 Article 382, Paragraph (2) and Article 382-3 of the KCC, and Article 681 of the Civil Code.

28 Article 399 of the KCC.
Directors may be exempted from the foregoing liabilities pursuant to unanimous shareholders’ consent (which is highly unlikely for listed companies). As previously mentioned, if a director’s liability exceeds six times his or her annual salary (three times, in the case of an outside director), it may be exempted if the company has set forth relevant matters in this regard in the articles of incorporation in advance.29,30

If a company fails to do so, shareholders may file a lawsuit against the directors on behalf of the company based on the directors’ breach of their duties.31 Recently, there have been discussions about expanding the scope of derivative actions and introducing a multi-step derivative action system: that is, a system whereby the shareholders of a parent company may institute a derivative action against the directors of a subsidiary if those directors have caused damage to the subsidiary due to their negligence in the performing of their duties.

Directors may be liable under the Criminal Act for breach of fiduciary duty if they have breached their duty of care as a bona fide manager or a fiduciary obligation to the company, and the company has suffered damage due to such breach and such director or third party profited therefrom.32

Directors are appointed by a resolution of the general shareholders’ meeting. When appointing two or more directors, use of a cumulative voting system may be requested, although most companies restrict such system through their articles of incorporation.33,34

If a listed company convokes a general shareholders’ meeting to appoint directors, it shall provide certain information about the candidates to the shareholders. Directors may be appointed only from the candidates notified as above.35

Large listed companies shall appoint outside directors from those candidates recommended by the committee formed to recommend outside director candidates.36

For financial companies, candidates for outside directors, representative directors and audit committee members are recommended by the committee to recommend officer director candidates.37

The term of office of directors shall not exceed three years; however, such period may be extended by the articles of incorporation until the adjournment of an annual general shareholders’ meeting convened with respect to the last fiscal year during a term of office.38

Although there is no special qualification requirement for executive directors, outside directors should satisfy certain qualification requirements that are mainly related to their independence.39

29 Article 400 of the KCC.
30 However, such limit on liability shall not apply in certain cases, for example, damages caused by a director’s wilful misconduct, or gross negligence or violation of certain regulations, such as self-dealing, provided under the KCC.
31 Article 403 of the KCC.
32 Article 355, Paragraph (2) of the Criminal Act.
33 Articles 382 and 382-2 of the KCC.
34 Recently there have been discussions about amending the KCC to make the cumulative voting system mandatory for listed companies of a certain minimum size.
35 Articles 542-4 and 542-5 of the KCC.
36 Article 542-8 of the KCC.
37 Article 17 of the Corporate Governance Act.
38 Article 383 of the KCC.
39 Article 382, Paragraph (3) and Article 542-8 of the KCC. Note that the amendment to the Enforcement Decree of the KCC that has been in force since 29 January 2020 sought to strengthen the independence of outside
For large listed companies, at least one member of the audit committee should be an expert in accounting or finance.\(^{40}\) As for financial companies, certain qualification requirements are specified for the executive and outside directors.\(^{41}\)

**Conflicts of interest**

To prevent a conflict of interest between a company and a director, when a director, or any of his or her relatives and entities he or she controls, intends to engage in a transaction with the company (self-dealing), the relevant party shall disclose the material facts regarding such self-dealing to the board of directors in advance, and obtain approval therefor by an affirmative vote of at least two-thirds of the total number of the directors. Any self-dealing shall be fair in terms of its conditions and procedures.\(^{42}\)

According to the 2012 amendment to the KCC, a director shall also obtain the approval of the board of directors by an affirmative vote of at least two-thirds of the total directors to exploit business opportunities that are likely to present current or future profits to the company for his or her own benefit or that of a third party.\(^{43}\)

Since outside directors cannot engage in the regular business of a company,\(^{44}\) they are not able to directly engage in the performance of a company’s business. However, they shall monitor the management as members of the board of directors by, inter alia, reviewing and examining matters reserved to the board of directors, participating in the board of directors, engaging in discussions or exercising voting rights.

### III  Disclosure

Companies of a certain minimum size (including listed companies) are subject to an external auditor’s audit. Under the Act on External Audit of Stock Companies, which has lately been restated:

\(a\) the independence of external auditors has been strengthened by requiring the FSS to designate an external auditor for a period of three years after a listed company’s appointment of an external auditor for six years at its own discretion; and

\(b\) the external audit system has been reinforced by stipulating the obligation to submit internal accounting management systems to an external audit.\(^ {45}\)

All external audit reports shall be publicly disclosed under the applicable laws.

Listed companies and some other companies are required to publicly disclose certain matters, including audit reports, on a quarterly basis, and are also required to publicly disclose directors by expanding the grounds for disqualifying outside director candidates. Such Enforcement Decree stipulates that the following persons cannot serve as outside directors of a listed company: (1) anyone who worked as an outside director of such company for more than six years; (2) anyone who worked as an outside director of the company or any of its affiliates for more than nine years in total.

\(^{40}\) Article 542-11.

\(^{41}\) Articles 5 and 6 of the Corporate Governance Act.

\(^{42}\) Article 398 of the KCC.

\(^{43}\) Article 397-2 of the KCC.

\(^{44}\) Article 382, Paragraph (3) of the KCC.

\(^{45}\) Articles 11 and 8 of the Act on External Audit of Stock Companies.
them in accordance with the FSCMA. The public disclosure regulations of the KRX are applicable to listed companies, including certain disclosure requirements in the event of any major decision such as the issuance of new shares, the acquisition of treasury shares, a merger or spin-off, and the transfer of a material business or asset. In addition, listed companies are obliged to make public disclosures in a fair manner so as to prevent any information gap due to the selective provision of important information to certain persons.

Most public disclosures are mandatory, and the comply or explain model has been introduced for certain financial companies. Starting from 2019, under the recently amended KRX regulations, large listed companies are required to publicly disclose their corporate governance reports setting forth, inter alia, the current status of the protection of shareholders’ rights, the independence of boards of directors, fairness in the course of the appointment of the directors, and the expertise of a company’s internal and external audit organisations.

Communication between management and shareholders usually takes place through investor relations activities, and shareholders are increasingly requesting meetings with management, including directors.

IV CORPORATE RESPONSIBILITY

Financial companies are required to organise a risk management committee and appoint a compliance officer and a risk management officer.

A listed company with total assets equal to or greater than 500 billion won should establish compliance guidelines, and appoint a compliance officer who is responsible for ensuring officers and employees comply with the compliance guidelines.

Recently, the MOJ has been making efforts to facilitate the internal control processes by announcing the Standard Compliance Guidelines for Listed Companies to enhance the effectiveness of the compliance system. The Guidelines provide that:

- an internal reporting system for whistle-blowing may be established;
- personal information about whistle-blowers and details of related internal reports shall be kept confidential;
- extenuating circumstances shall be taken into consideration in cases where a whistle-blower reports a tort or illegal act in which he or she has been involved; and
- no whistle-blowers shall be subject to any disadvantages due to their whistle-blowing.

In addition, as corporate social responsibility has emerged as an important issue, there is growing interest in the ethical management of companies, and companies are increasingly disclosing their internal policies related to such issues.

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46 Note that the amendment to the Enforcement Decree of the KCC that was announced on 29 January 2020 sought to obligate public companies to provide their business plans and audit reports in conjunction with any notice or public announcement of convocation of shareholders' meetings, and such provision will take effect on 1 January 2021.
47 Articles 159 and 161 of the FSCMA, and Article 7 of the Regulations on Public Disclosure on the Securities Market.
49 Articles 16, 21, 25 and 28 of the Corporate Governance Act.
50 Article 542-13 of the KCC.
With an increased emphasis on the importance of the ethics of owners or officers of large enterprises, their abuse of authority against employees often becomes a social issue. There are cases where officers have not only resigned but have also been held criminally responsible for committing abusive acts.

V SHAREHOLDERS

i Shareholder rights and powers

Every shareholder shall have one vote for each share held,51 and no extra vote or dividend shall be acknowledged for the reason that the shareholder has been holding shares for a long period of time. However, a company may issue shares without voting rights in accordance with the articles of incorporation. Because the appointment or dismissal of directors is a matter reserved to the general shareholders’ meeting, shareholders have an indirect influence on the board of directors.52 Among other things, the following matters require a resolution of the board of directors as well as a special resolution of the general shareholders’ meeting:53

a amendments to the articles of incorporation;
b reductions in paid-in capital;
c mergers or spin-offs of the company;
d the transfer of all or material parts of the business; and
e comprehensive share transfers and share exchanges.

However, not all matters reserved to the board of directors need to be approved by the shareholders.54 Minority shareholders holding a certain equity interest have certain rights depending on their shareholding, including:

a shareholder proposal rights;
b the right to call a general shareholders’ meeting;
c the right to request a cumulative vote with regard to the appointment of directors;
d the right to request an injunction (suspension) for a violation by the directors; and
e the right to institute a derivative action and the right to inspect accounting books.55,56

ii Shareholders’ duties and responsibilities

A shareholder of a listed company is required to publicly disclose his or her equity interest with regard to certain matters if the equity interest constitutes at least 5 or 10 per cent,57 but shall not assume any other special legal obligations or responsibilities.

51 Article 369 of the KCC.
52 Articles 382 and 385 of the KCC.
53 Articles 374, 434, 438, 522 and 530-3 of the KCC.
54 The appraisal rights of dissenting shareholders are acknowledged for some matters requiring the approval of the general shareholders’ meeting as described above (e.g., merger and comprehensive share transfer).
55 Articles 363-2, 366, 382-2, 402, 403, 466 and 542-6.
56 Requirements for the exercise of minority shareholders’ rights shall be relaxed for listed companies with certain restrictions on holding periods (Articles 363-2, 366, 382-2, 402, 403, 466 and 542-6).
57 Articles 147 and 173 of the FSCMA.
However, any person who instructs a director to perform business by using his or her influence over the company shall assume the same responsibility as that director with regard to such instructed or performed business.\(^{58}\) It is possible that the foregoing responsibilities would be recognised for the controlling shareholder.

In cases of self-dealing, the relevant party shall disclose the material facts regarding the self-dealing to the board of directors in advance, and obtain the approval of the board by an affirmative vote of at least two-thirds of the total number of the directors to prevent a conflict of interest between the company and the major shareholder. Any self-dealing shall be fair in terms of its conditions and procedures.\(^ {59}\) In addition, no listed company shall grant certain credit or provide debt guarantees to major shareholders and their specially related parties.\(^ {60}\)

Although there have been theoretical discussions on the responsibilities assumed by a controlling party against minority shareholders, there is currently no legislation in this regard.

**Institutional investors’ duties and best practice**

Although no special statutory provision of any special legal obligations or responsibilities is available with regard to the exercise of shareholders’ voting rights, institutional investors have recently been introducing a stewardship code; accordingly, the role of proxy advisory organisations, which provide advice on the details of exercising voting rights based on their analysis of the agenda of the general shareholders’ meeting, has been reinforced.

To secure trust in the expertise of proxy advisory organisations, an amendment to the FSCMA has been proposed, and the introduction of a declaration system for proxy advisory organisations has been discussed, granting rights to request the submission of information to the FSC and to prohibit unsound business activities of proxy advisory organisations.

**iii Shareholder activism**

Shareholder activism is increasing in Korea, and proxy battles frequently take place. One activist recently carried out a campaign to publicly oppose the agenda for the restructuring of a large listed company, and the relevant agenda was not adopted.

There seem to be conflicting views about shareholder activism: on the one hand, such activity is not optimal for long-term corporate value, as it merely seeks short-term profits; however, on the other hand, shareholder activism should be understood as a reasonable aim to protect minority shareholders and improve corporate governance.

Any person intending to solicit another person to exercise his or her voting rights by proxy for listed companies should public disclose this in advance and deliver the power of attorney or reference documents.\(^ {61}\)

**iv Takeover defences**

Given that every shareholder has one vote per share,\(^ {62}\) dual class share systems are not an appropriate defence in Korea against a hostile takeover.

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58 Article 401-2 of the KCC.
59 Article 398 of the KCC.
60 Article 542-9 of the KCC.
61 Article 152 of the FSCMA.
62 Article 369 of the KCC.
In the case of a hostile takeover, it may be possible for the board of directors to use defence tactics such as the acquisition of treasury shares or the issuance of new shares to friendly third parties, including specific shareholders. As previously mentioned, express grounds must be included in the articles of incorporation to issue new shares to friendly third parties, and other regulatory issues exist. Furthermore, in a dispute over management control, the issuance of new shares to friendly shareholders to defend against a takeover is likely to be invalidated at court. Listed companies may acquire treasury shares by a resolution of the board of directors in an amount up to their distributable profits, and may use methods such as tender offers or purchases on exchange.

Another possible measure is selling treasury shares to friendly third parties, given that the disposal of treasury shares is also a matter reserved to the board of directors and is not subject to regulations on the issuance of new shares. Such practice, however, is generally perceived in a negative light.

The staggered board system is not prohibited under the applicable laws and regulations, and some listed companies operate this system.

As previously mentioned, in defending against a hostile takeover, the articles of incorporation can stipulate a supermajority voting system for certain general shareholders’ meeting agendas, including the dismissal of directors or the golden parachute system; however, whether these systems are permitted under the KCC remains controversial.

Contact with shareholders usually takes place through investor relations activities, and shareholders are increasingly keen to meet with management, including directors. In some cases, management will hold individual meetings with major shareholders. Although holding individual meetings with a shareholder or certain shareholders is not prohibited, the selective provision of internal information only to some shareholders is not permitted. In such case, a company has an obligation to make fair public disclosures; provided, however, that selective provision of information would be exceptionally permitted if the receiving party signs an agreement that it will keep such information confidential and not engage in share transactions by using the relevant information.

Notice on the convocation of a general shareholders’ meeting shall be given to shareholders at least two weeks prior to the date set for such meeting, provided that if a company has made a public disclosure of the convocation of the general shareholders’ meeting, it may elect not to give notice thereon to shareholders with an equity interest representing no more than 1 per cent.

For listed companies, the system of soliciting a person to exercise a shareholder’s voting rights by proxy is generally used. To this end, the person intending to do so should make public disclosure of this in advance, and deliver a power of attorney or reference document regarding this.

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63 Article 165-3 of the FSCMA.
64 Article 363 of the KCC.
65 Article 542-4 of the KCC.
66 Article 152 of the FSCMA.
Usually, shareholders do not expressly state whether they agree or disagree with the agenda submitted to the general shareholders’ meeting. However, the National Pension Service has recently begun announcing how it would vote on certain agendas to the extent specific conditions are met.

VI OUTLOOK

In 2018, the state-run National Pension Service (NPS), which is the world’s third-largest pension fund, adopted a stewardship code, and due to certain highly publicised cases of misbehaviour by owners recently, there is growing public opinion in Korea that shareholders should actively exercise their shareholder rights. In connection with the foregoing, the NPS enacted its internal shareholder activism guideline, which became effective on 27 December 2019 and establishes detailed standards and processes for shareholder activism based on the stewardship code. With such guideline in effect, the NPS is expected to take a more active stance as a shareholder, and for certain portfolio companies selected by its fund management committee, exercise its shareholder rights to the fullest extent permitted under applicable laws and regulations.

Furthermore, shareholder activism has been on the rise in Korea, with an increasing number of domestic and overseas activist investors seeking to influence the management of large Korean conglomerates. We anticipate that the growth of activism will lead to increased attention being paid to corporate governance, especially regarding issues such as the re-election of owners as executive directors, concurrent directorships, and the independence and diversity of outside directors.

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67 On 6 September 2019, the FSC announced that it would propose an amendment to the Enforcement Decree of the FSCMA to relax the 5 per cent reporting obligation, whereby the legislative intent therefor is to enhance and support institutional investors’ shareholder activism. It was recently announced that such amendment would become effective as of 1 February 2020.
Chapter 22

SWEDEN

Christoffer Saidac, Mattias Friberg and Khaled Talayhan¹

I OVERVIEW OF GOVERNANCE REGIME

Corporate governance in Swedish companies whose shares are admitted to trading on a regulated market (listed companies) is regulated by a combination of statutory laws and regulations and self-regulation-based generally accepted practices. The framework includes the Swedish Companies Act and the Swedish Annual Accounts Act, supported by the Swedish Corporate Governance Code (Code) and the rules of the regulated markets on which shares are admitted to trading, as well as recommendations and statements from the Swedish Financial Reporting Board, statements by the Swedish Securities Council on what constitutes good practice in the Swedish securities market, and the Council for Swedish Financial Reporting Supervision's review of financial reports of Swedish listed companies.

Enforcement of regulations applicable to listed companies – the Swedish Stock Exchange's Issuer Rules, the Code (under the comply or explain regime), and statements from the Swedish Financial Reporting Board, the Council for Swedish Financial Reporting Supervision and the Swedish Securities Council – may be carried out by the Stock Exchange through disciplinary procedures. In addition, the law may be enforced through actions by the Swedish Financial Supervisory Authority and in local courts.

Ownership structure on the Swedish stock market differs from the structure in countries such as the United Kingdom and the United States. While the majority of listed companies in those countries have a very diverse ownership structure, ownership in Sweden is often concentrated to a single or small numbers of major shareholders, as is the case in many other continental European countries. In around one-third of the listed companies, these shareholders strengthen their positions further through holdings of shares with greater voting rights. They often play an active ownership role and take particular responsibility for the company, for example by sitting on the board of directors. A particular characteristic of Swedish corporate governance is the engagement of shareholders in the nomination process for boards of directors and auditors, which they exercise through their participation in companies’ nomination committees. Nomination committees are not regulated by the Companies Act, but by the Code. A Swedish nomination committee is not a sub-committee of the board, but a body of the general meeting of shareholders typically made up of members who are appointed by the company’s larger shareholders.

Swedish society takes a positive view of major shareholders taking particular responsibility for companies by using seats on boards of directors to actively influence

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governance. At the same time, major holdings in companies must not be misused to the
detriment of the company or the other shareholders. The Companies Act therefore contains
a number of provisions that offer protection to minority shareholders, such as requiring
qualified majorities for a range of decisions at general meetings of shareholders.

International institutional investors have requested individual voting on boards of
directors, even though such a procedure is normally superfluous and time-consuming in a
Swedish setting with the Swedish nomination committee system.

II CORPORATE LEADERSHIP

i Board structure and practices

Structure
A Swedish limited liability company is organised as a unitary structure in line with the
Anglo-Saxon one-tier model. The general meeting of shareholders, acting as the company’s
supreme decision-making body, elects a board that appoints a managing director. The
general meeting, the board and the managing director together with the auditors comprise
the four corporate bodies recognised by the Companies Act and the first three
are, in descending order, subordinated in relation to each other. The auditors, whose main
responsibility is to keep the accounts in order, are, however, independent in relation to the
others. Thus, under the Swedish corporate governance structure, there is no two-tier model
with a supervisory board overseeing the administration of the company as traditionally can
be found in continental Europe.

Composition of the board
In general, the board in Swedish listed companies includes five to 10 members and primarily
consists of non-executive directors. According to the Code, a majority of the directors of
the board elected by the general meeting must be independent from the company and its
executive management. A minimum of two of these directors must also be independent from
the company’s major shareholders. In addition to this, the Code stipulates that no more than
one board member elected by the general meeting may be part of the executive management
of the company or of a subsidiary to the company. Thus, boards of listed companies normally
consist of non-executive directors only. The managing director of the company may not be
the chair of the board, but may however be a board member.

Recurrently, the low percentage of female board members has come under review, and
within the public debate there are those who argue that legislation is required to balance the
gender ratio between female and male board directors. Under the Code, the board shall have
a composition appropriate to the company’s operations, its phase of development and other
relevant circumstances. The board members elected by the general meeting shall collectively
exhibit diversity and breadth of qualifications, experience and background. Moreover, the
company must also strive for gender balance on the board.

In 2006, the Ministry of Justice introduced a proposal for a provision, under which at
least 40 per cent of boards of listed companies would be required to comprise female directors,
and in 2015, the Minister stated that the parliament may be required to amend the law to
reach the goal of more gender-balanced boards. It was further stated by the Ministry secretary
that a bill would be presented to the parliament within a year in the event that companies
did not have female representation of at least 40 per cent before that point in time, and in
2016, the government presented a legislative proposal to this effect. However, the proposal
did not have sufficient support in parliament, and no new proposal has been put forward since. Thus, at this time, there is no legal requirement as regards female representation on boards of directors.

**Representation**

In general, under the Companies Act, the right to represent and sign on behalf of the company in all matters is vested in the board as a whole. If a managing director has been appointed, he or she has the right to sign on behalf of the company as regards the day-to-day operations. In addition to this, the board may authorise a board member, the managing director or any other person to represent the company by way of special company signature, and typically such representation rights are granted to at least two such persons jointly.

**Legal responsibilities of the board and the chair of the board**

According to the Companies Act, the principal duties of the board comprise the responsibility for the organisation of the company and the management of the company’s affairs. Furthermore, the board is also to ensure that the company’s organisation is structured in such a manner that accounting, management of funds and the company’s finances in general are monitored in a satisfactory manner. In addition to this, board members as well as the managing director have an overall duty in all matters to act in accordance with the interests of the company. The chair of the board has no specific duties or powers other than a responsibility for convening the board and leading the work of the board.

Another key task of the board is to appoint and dismiss the managing director. Whereas the board is responsible for the overall management of the company’s affairs, the managing director shall attend to the management of the day-to-day operations pursuant to guidelines and instructions issued by the board.

Thus, boards in Swedish companies have an extensive decision-making authority, but also their limitations, primarily by way of the legal provisions giving the general meeting exclusive powers as regards specific matters (e.g., share issues, amendments to the articles of association, and the election of board members and auditors).

**Remuneration of directors and compensation from shareholders**

The board remuneration is resolved upon by the annual general meeting, and the board decides the remuneration for the executive management. All share and share price-related incentive schemes for the executive management shall, however, be resolved upon by the general meeting. Pursuant to the Companies Act, listed Swedish companies are required to have guidelines for executive remuneration adopted by the general meeting. According to the Code, the remuneration and other terms of employment are to be designed with the aim of ensuring that the company has access to the competencies required at a cost appropriate to the company, and that they have the intended effects for the company’s operation.

The basic rule is that directors receive their remuneration from the company concerned. There are, however, no rules directly prohibiting a director from also accepting compensation from a shareholder who has nominated him or her. In practice, the director may, for example, be employed by the nominating shareholder. In some cases, a director being employed by the

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2 However, pursuant to the Companies Act, listed Swedish companies must at all times have a managing director appointed.
nominating shareholder waives his or her remuneration from the company. Such arrangements should be factored in when determining whether the rules regarding disqualification of a director to decide on specific matters involving such a nominating shareholder are applicable. If a board member receives compensation from a shareholder, he or she is not deemed independent from that shareholder.

ii Directors

Legal duties

Board members have a fiduciary duty to act in good faith and in the best interests of the company, which entails a duty to act in the interest of all shareholders. For that reason, the board may, for instance, not consider an activist proposal under any different standard of care compared to other board decisions, and individual shareholders may not be given an unfair advantage compared to the other shareholders in the company. However, the board may cooperate with an activist as long as the board does not breach the duty of equal treatment of all shareholders.

Provided that it is not in conflict with the Companies Act or the applicable articles of association, the board is also obliged to follow any specific instruction decided upon by the general meeting.

Liability of directors

According to the Companies Act, a board member as well as a managing director may be liable for damages to the company, the shareholders or third parties (e.g., creditors). If, in the performance of his or her duties, he or she intentionally or negligently causes damage to the company, he or she shall compensate the damage. Liability towards a shareholder or a third party may, however, only arise when damage is caused as a consequence of a violation of the Companies Act, the applicable annual reports legislation and/or the articles of association. The board may delegate specific tasks to individual members or other employees, but is not able to avoid liability for the company’s organisation or the duty to ensure satisfactory control of the finances of the company.

Further, members of the board and the managing director may also be held liable under general principles on tort and, if applicable, the Swedish Tort Liability Act. As for the board, there is no collective liability per se, and an in casu judgement must be made as regards each claim and each director. Moreover, a Swedish company is not itself capable of committing a crime, hence it is the natural person who commits the crime who ultimately will be held responsible.

Appointment, nomination and term of office

Under the Companies Act, the board is elected by the general meeting. In listed companies, director nomination is done by the nomination committee, which in Sweden is not a board committee, but rather a committee set up by the general meeting that includes representatives of the largest shareholders. The Code stipulates that a company shall have a nomination committee that, inter alia, shall nominate candidates to the board and that the general meeting shall adopt written instructions to the nomination committee. The general meeting elects the members of the nomination committee, and thus large shareholders generally have
great influence over the composition of the committee. However, at least one of the members shall be independent in relation to either the company’s largest shareholder or group of shareholders that cooperate regarding the management of the company.

Any shareholder may, however, nominate directors for election to the board and have the nomination included in the notice to attend the general meeting, as long as the proposal is presented to the board within the time frame stipulated in the Companies Act and otherwise complies with the applicable provisions in the Companies Act. Furthermore, if the matter of election of members of the board is already on the agenda of the general meeting, a shareholder has the right to propose a candidate as late as during the meeting itself.

The nomination committee shall safeguard the interest of all shareholders in its nomination of candidates. The nomination committee’s proposal is presented in the notice to attend the general meeting. The board is elected by a majority vote, unless the articles of association stipulates otherwise. Market practice in Sweden has been to elect the members of the board by a single vote. However, this is not required by law, and some international investors in Sweden have shown tendencies to start raising demands on listed companies to switch to separate voting for each member of the board. Large international institutional investors have been campaigning for individual board election and transparency of voting at general meetings.

Staggered boards are non-existent (each board member is elected annually, and there is no way of preventing a new majority shareholder from replacing the board immediately).

III DISCLOSURE

The primary rules relating to communications made by listed companies concern disclosure duties and equal treatment of shareholders. Transparency and disclosure are key aspects of Swedish corporate governance in listed companies. The EU Market Abuse Regulation (MAR), the Swedish Securities Markets Act and the Stock Exchange’s Rule Book for Issuers (Rule Book) set forth the basis for listed companies’ disclosure obligations. Under MAR, listed companies are obliged to, as soon as possible, publish all information of a precise nature that has not been made public, relating, directly or indirectly, to the issuer’s financial instruments and that, if it were made public, would be likely to have a significant effect on those financial instruments or on the price of related derivative financial instruments (i.e., inside information). Additionally and in accordance with the Securities Markets Act and the Rule Book, listed companies are obliged to disclose information related to financial reports, issues of securities, changes in the board, management and auditors, share-based incentive programmes, material closely related party transactions, and material business acquisitions and divestitures, irrespective of whether the information constitutes inside information. The purpose of the disclosure obligations is to provide sufficiently comprehensive, relevant, clear and non-misleading information to the market. To promote proper disclosures, listed companies are recommended to prepare a written disclosure policy in which the guidelines and procedures applied in the company’s communications with the capital markets and investors are specified.

As a general rule, inside information shall be disclosed as soon as possible although companies, provided that certain conditions are fulfilled, may delay the disclosure. To be allowed to delay the disclosure of inside information to the public, the following conditions must be met according to MAR: immediate disclosure is likely to prejudice the legitimate interests of the company, the delay of disclosure is not likely to mislead the public and the
company is able to ensure the confidentiality of that information. When this information is subsequently publicly disclosed, the company must notify the Swedish Financial Supervisory Authority (SFSA) that the disclosed information was delayed and, upon request by the SFSA, explain how the aforementioned conditions were met.

Generally, selective disclosure of inside information constitutes a violation of MAR, which may result in sanctions for the company. Such disclosure may also constitute a criminal offence for the person making the disclosure. However, in certain special situations – for example, ahead of a rights issue where a company wants to secure commitments from its largest shareholders – selective disclosure may be permitted if disclosure is made in the normal exercise of an employment, a profession or duties and, in case of contemplated securities offerings, pursuant to the special market-sounding rules of MAR. When delaying disclosure of inside information, listed companies are under the obligation to maintain insider lists of directors, employees and other persons with access to inside information and who work or perform tasks for the company.

MAR contains a requirement that all disclosed inside information is made public on the company’s website and stored there for at least five years. The same applies, according to the Rule Book, to all information communicated by the company to the market. There are no other rules governing the media platform to be used as distribution channels; however, social media platforms are rarely used for shareholder activity-related matters. In addition, since the purpose of the disclosure duties is to make sure that the information is disclosed to the market simultaneously on a non-discriminatory basis, in practice, companies must use an information distributor for this purpose.

In accordance with the Annual Accounts Act and the Code, listed companies shall disclose a yearly corporate governance report in which the company shall present information on its corporate governance functions and state its compliance with the Code. If the company chooses to deviate from a certain provision of the Code, it must state its reasons for doing so (the comply or explain principle). Moreover, a corporate governance report shall include a description on internal controls and risk management regarding the financial reporting, and how the yearly evaluation of the board has been conducted and reported.

Further, all Swedish companies, associations and other legal entities are obliged to register their ultimate beneficial owner or owners with the Swedish Companies Registration Office. There are a few exceptions to this obligation, including governmental bodies and listed companies. The ultimate beneficial owner is the natural person or persons who ultimately own or control a legal entity. A natural person is presumed to exercise such control if he or she, directly or indirectly, holds or controls more than 25 per cent of the votes, or holds or controls the right to appoint or remove a majority of the board of directors. Moreover, a legal entity may not have any beneficial owner or may, under certain conditions, be relieved from the obligation to report its beneficial owner due to complex ownership structures as investigation obligations are limited.

**Financial reporting and accountability**

Listed companies shall prepare annual financial statements and, as a general rule, interim financial reports for the first three, six and nine months of the financial year. The consolidated financial statements shall be prepared in compliance with IFRS and the interim financial reports for the six months of the financial year and the year-end report shall be prepared in accordance with IAS 34. Companies are entitled to disclose a lighter-form interim management statement instead of an interim financial report for the first three and nine
months of the financial year. According to the amended Transparency Directive, listed companies are no longer obliged to publish quarterly financial information. However, member states may require greater disclosure on certain conditions, and in Sweden the obligation to publish quarterly financial information remains. The Stock Exchange has set out guidance for preparing interim management statements. A company may, however, deviate from the guidance completely or on certain points if it discloses the reporting or statement format that it has chosen instead, and its reasons for doing so, on its website.

Annual financial statements shall be published within four months of the end of the financial year and three weeks before the annual general meeting. Quarterly financial reports or interim management statements shall be published within two months of the end of the reporting period.

According to the Securities Markets Act and the Rule Book, the SFSA may impose independently of the Stock Exchange a penalty payment for any failure to comply with the ongoing disclosure obligation, the obligation to disclose periodic information, and the obligation to publish and store regulated information. All financial reports shall be made available on the company’s website for a minimum of 10 years.

**Auditors**

Listed companies must appoint at least one authorised auditor or audit firm. Listed companies may not appoint the same main responsible auditor for more than seven consecutive years or the same audit firm for more than 10 consecutive years. Provided that a renewal process in accordance with the EU Audit Regulation takes place, listed non-financial companies may, however, appoint the same audit firm for another 10-year period (i.e., for a total of 20 years). The company’s statutory auditor is appointed by the general meeting to examine the company’s annual accounts and accounting practices, and to review the board’s and the managing director’s management of the company. Auditors of Swedish companies are therefore given their assignment by, and are obliged to report to, the owners, and they must not allow their work to be governed or influenced by the board or the executive management. Auditors present their reports to the owners at the annual general meeting in the annual audit report.

Furthermore, the Companies Act sets out that companies, as a rule, shall establish an audit committee. The audit committee shall, without affecting the responsibilities of the board:

- monitor the financial reporting of the company;
- monitor the efficiency of the company’s internal controls, internal auditing and risk management;
- keep abreast of the audit of the annual accounts and consolidated accounts;
- review and monitor the impartiality and independence of the auditor; and
- pay close attention if the auditor provides the company with services besides audit services, and assist in the preparation of proposals for the decision of the general meeting on the election of auditors.

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IV CORPORATE RESPONSIBILITY

Under the Code, which outlines the main responsibilities of the board in relation to internal control and risk management, one of the principal tasks of the board is to ensure that there is an appropriate system for follow-up and control of the company's operation and the risks to the company that are associated with its operations. The Code further stipulates that the board is also to ensure that there is a satisfactory process for monitoring the company's compliance with laws and other regulations relevant to the company's operations, as well as the application of internal guidelines.

Following numerous corporate scandals in Sweden and abroad in recent years, the media, as well as the public and authorities are, to an increasing extent, scrutinising corporations, their management and directors. In particular, different incentive programmes for senior executives, bonuses, other benefits and so forth, but also questionable risk management, have been subject to increased focus, which has led to public debate. In recent years, there have been a few high-profile criminal proceedings against company officials. Most of them have been brought against the executive management, but there are a few example of cases where members of a board of directors also have been charged.

In December 2016, amendments were made to the Annual Accounts Act, as a result of the implementation in Sweden of the EU Directive on non-financial reporting. The amendments entail that certain larger companies, companies that are of public interest and parent companies of large groups draw up a sustainability report that includes the information necessary to understand the company's development, performance and position and the consequences of its business, including information related to the environment, social matters, staff, respect for human rights and work counteracting corruption. These companies must also report on the diversity policy that applies to the composition of the board of directors.

V SHAREHOLDERS

i Shareholder rights and powers

Shareholders exercise their rights and powers by participating in general meetings. Shareholders’ most significant rights include voting rights in general meetings, the right to have a matter dealt with by a general meeting and the right to ask questions at a general meeting.

The annual general meeting convenes once a year, within six months of the end of the financial year. In between the annual general meetings, extraordinary general meetings may be convened either by the board, if deemed necessary, or by shareholders holding at least 10 per cent of the outstanding shares in the company. Under Swedish law, there are no special facilities for long-term shareholders.

Matters to be brought by the general meeting

Any shareholder who wishes to have a matter addressed at a general meeting may submit a written request thereof to the board. The matter must be addressed at the general meeting if the request from the shareholder is received by the board no later than seven weeks prior to the general meeting, or at a later date if the request is submitted in due time for the matter to be included in the notice to attend the general meeting. The proposed matter must concern an issue relevant to the company, which falls within the competence of the general meeting.
There are certain matters that fall under the exclusive competence of the general meeting. The Companies Act and companies’ articles of association regulate this. Matters falling within the competence of the board or the managing director of a company may be decided upon by the general meeting if the shareholders unanimously support the matter and the Companies Act does not prescribe otherwise.

Matters that fall under the exclusive competence of the general meeting include the election of board members and determining their remuneration, the election of the auditor of the company and any amendments to the company’s articles of association, as well as decisions relating to the shares or share capital of the company and certain corporate restructuring matters, such as mergers and demergers. Share repurchases or share issues shall be brought about by the general meeting; however, the general meeting may authorise the board to decide on a repurchase of the company’s own shares or share issue. The authorisation regarding share repurchases must specify the price range for a repurchase and, with regard to a share issue, the maximum number of shares to be issued. Decisions regarding dividend distributions are also reserved for shareholders; however, the dividend distribution may not exceed the proposal made by the board, except where such an obligation exists in accordance with the articles of association or where the distribution was resolved upon at the request of a minority holding at least 10 per cent of the shares in a company. Shareholders holding at least 10 per cent of the shares in a company are always entitled to request the payment of a dividend corresponding to half of the profits of the financial year, although not more than five per cent of the equity of the company.

Decision-making at the general meeting

Each shareholder has the right to participate in a general meeting. The articles of association may prescribe that, to participate at a general meeting, a shareholder must notify the company thereof not later than the date specified in the notice to attend the general meeting. The main rule is that all shares carry equal rights; however, the articles of association may prescribe otherwise.

Resolutions at a general meeting usually require a simple majority to be passed. There are, however, certain matters that require a qualified majority of both the votes cast and represented at the general meeting. A majority is purported as qualified if it is supported by at least two-thirds of the votes cast and shares represented at the meeting.

Below is an enumeration of certain matters that require a qualified majority vote:

- amendment of the articles of association;
- directed share issue;
- directed issue of warrants or convertibles;
- acquisition and redemption of own shares;
- directed acquisitions or sales of own shares; and
- mergers and demergers.

There is a possibility for listed Swedish companies to apply postal voting, however this option is rarely used. Instead, voting is done at the general meeting either by the shareholder in person or by anyone with a written power of attorney.
Objection to a decision by the general meeting

In the event that a resolution of a general meeting has not been adopted in due order or otherwise contravenes the Companies Act, the applicable annual reports legislation or the articles of association, a shareholder, the board, a member of the board or the managing director may bring proceedings against a company before a court of general jurisdiction to set aside or amend the resolution. Such proceedings may also be brought by a person whom the board has unduly refused to enter as a shareholder in the share register.

An action to have a general meeting’s resolution declared void must be commenced within three months of the date of the resolution. Where proceedings are not commenced within that period, the right to commence proceedings shall be forfeited. Proceedings may commence at a later time provided that the resolution is such that it cannot be adopted without the unanimous consent of all shareholders, consent to the resolution is required of all or certain shareholders and no such consent has been granted, or notice to attend the general meeting has not been given or significant parts of the provisions governing notice to attend the general meeting have not been complied with.

ii Shareholders’ duties and responsibilities

Protection of minority rights

An important protection mechanism for the minority shareholders of a company is the principle of equal treatment. The principle is established in the Companies Act, and is thus applicable to both listed and unlisted companies. The principle entails that shares of the same class have the same rights, unless otherwise specified in the articles of association. A dividend that results in a difference in the payout per share is, therefore, in conflict with the principle of equal treatment. The same would apply to any other asset transfers that differentiate between shareholders of the same class of shares. In cases where a minority shareholder is unfairly treated in relation to a majority shareholder (e.g., if the company enters into an unfavourable agreement with a majority shareholder), the minority shareholder will not be able to rely on the principle of equal treatment to invalidate the transaction, because in that situation all shareholders are affected equally. However, in such cases minority shareholders are protected by other provisions of the Companies Act. For example, the Companies Act states that the general meeting may not adopt any resolution that is likely to provide an undue advantage to a shareholder or another person to the disadvantage of the company or another shareholder. The board, or any other representative of the company, is also prohibited from performing any legal acts or other measures that are likely to provide an undue advantage to a shareholder or another person to the disadvantage of the company or any other shareholder.

If a minority shareholder manages to show that it has been unfairly treated, the transaction may be invalidated and the minority shareholder may receive damages. The transaction will typically not be regarded as unfair should the majority shareholder be able to show that the transaction was entered into in the normal course of business.

Some important minority shareholders’ rights include the possibility for shareholders holding not less than 10 per cent of all shares in the company (owned by one shareholder alone or by a number of shareholders in conjunction) to demand in writing that the company’s board convenes an extraordinary general meeting to address a specified matter. If the request is correctly made, the board is obliged to convene the meeting and must issue a notice to attend the meeting within two weeks of receipt of the request. A specified matter is an issue relevant to the company that can be decided upon at the extraordinary general meeting. For that reason, it is not possible for minority shareholders to demand that an extraordinary
general meeting is convened just for the opportunity to ask questions of the members of the board or the management. However, a minority that needs to ask questions of the board could initiate its right to appoint an extra auditor or a special examiner and demand that an extraordinary general meeting is held to decide on such matter. During the general meeting, the right to ask questions can be utilised as a first step to meet the information requests of the minority. If the board satisfies the minority's needs in this regard, the need to appoint an extra auditor or special examiner may no longer be necessary.

A minority shareholder may propose that an extra auditor appointed by the Swedish Companies Registration Office shall participate in the audit of the company together with the company's ordinary auditors. The proposal shall be submitted to a general meeting at which the election of auditors is to take place or at which a proposal set forth in the notice to attend the general meeting is to be addressed. If the proposal is supported by owners of at least 10 per cent of all shares in the company or at least one-third of the shares represented at the meeting, and a shareholder then submits a request to the Companies Registration Office, the Companies Registration Office shall appoint an extra auditor. As a general rule, it is the person whom the minority has proposed as an extra auditor who shall be appointed.

The extra auditor has the same privileges and obligations as the company's ordinary auditor and shall participate in the auditing of the company together with the ordinary auditor. Thus, the extra auditor shall examine the company's annual report and the company's bookkeeping, as well as the board’s and the managing director's management of the company. Both the ordinary auditor and the extra auditor shall perform their function independent of the company and its management.

It should be noted that the ordinary auditor, as well as the extra auditor, have a duty of confidentiality and may not, without due authorisation, disclose to an individual shareholder or any third party any information concerning the company's affairs learned by the auditor in the performance of his or her duties, if the disclosure could damage the company. It is therefore mainly through the disclosure of the auditor's report and other accounting documents in close proximity to the annual general meeting that the minority shareholders of the company receive information concerning the company's financial situation. The auditor's report shall be presented to the company's board no later than three weeks prior to the annual general meeting. In listed companies, accounting documents and the auditor's report shall then be made available for the shareholders during a period of not less than three weeks immediately prior to the annual general meeting.

Further, a minority shareholder may submit a proposal for an examination through a special examiner. A special examiner’s assignment is to review the company’s management and accounts during a specific period in the past or certain measures or circumstances within the company. A proposal for an examination through a special examiner shall be submitted at an ordinary general meeting or at the general meeting at which the matter is to be addressed. Where the proposal is supported by shareholders holding at least 10 per cent of all shares in the company or at least one-third of the shares represented at the general meeting, the Companies Registration Office shall, upon request by a shareholder, appoint one or more special examiners. The special examiner shall submit a report regarding his or her examination. The report shall be made available and sent to the shareholders.
Controlling shareholders and institutional investors

In many Swedish listed companies, there is a controlling shareholder (or shareholders) who has often retained control through shares with greater voting power, such as certain family or privately controlled investment companies. Together, Swedish institutional shareholders have large stakes in many Swedish listed companies. In specific cases, they try to team up and then exert great influence.

There are no particular duties for controlling shareholders or institutional investors in Swedish legislation and self-regulation, except for the general obligation to launch a takeover bid when a shareholder’s ownership exceeds a certain level (30 per cent of the voting rights in the company) and the right and obligation to redeem the remaining outstanding shares when the shareholding exceeds 90 per cent of all the shares in the company.

A shareholder does not owe the same fiduciary duties towards the company as the board and is not required to act positively in the interest of the company. However, a shareholder should compensate for damage that he or she causes to the company, a shareholder or another person as a consequence of participating intentionally or though gross negligence, in any violation of the Companies Act, the applicable annual reports legislation or the company’s articles of association.

Shareholder activism

Shareholder activism has been fairly moderate in Sweden. However, in the past couple of years shareholder activism has increased in companies that are subject to a takeover offer, wherein the activist is calling for a higher price to be paid by the bidder after an offer is completed. This is done by the bidder taking a stake in the target during the offer period and thereafter taking advantage of the strong minority protection contained in the Companies Act. There is also a growing tendency, especially among institutional investors, to take a more active role. Swedish institutional shareholders play an important role in Swedish listed companies. Together, they have large stakes in many Swedish listed companies. In specific cases, they try to team up and then exert influence. In their daily activism, they try to exert influence through direct dialogue with the board and by taking part in nomination committees, but also indirectly by making statements in industry news media.

Activist shareholders normally gain a position through the acquisition of a corner in a company, in some cases together with Swedish or non-Swedish institutional investors.

Say on pay

The Code stipulates that a company shall have a nomination committee that, inter alia, shall nominate candidates to the board and propose the remuneration payable to the board and committee work. The proposal shall be put forth at the annual general meeting. In addition, the Companies Act requires the annual general meeting to resolve on principles for remuneration to management, to which the board must adhere when setting the remuneration for the CEO and other management staff.

Derivative action

Derivative actions on behalf of the company may be brought where a minority of owners of not less than 10 per cent of all shares in the company have, at a general meeting, supported a resolution to bring such a claim or, with respect to a member of the board or the managing director, have voted against a resolution regarding discharge from liability. If shareholders
holding at least 10 per cent of the shares in the company vote against a resolution regarding discharge of liability, a claim of damages may be brought against the board and the managing director despite the fact that the rest of the shareholders have voted for discharge.

Where the general meeting has adopted a resolution to grant discharge from liability or not to commence an action for damages (without 10 per cent of the shareholders having voted against the resolution), or the period for the commencement of an action has expired, an action may nevertheless be brought where, in the annual report or the auditor's report or otherwise, from a material aspect correct and complete information was not provided to the general meeting regarding the resolution or the measure on which the proceedings were based.

iv  Takeover defences
The Swedish corporate governance framework is significantly guided by the principle of equal treatment and a strong requirement on the board to always act in the best interest of the company and its shareholders. The board may not promote shareholders’ initiatives that conflict with these rules and principles. For that reason, unless the general meeting of shareholders has resolved upon it, target boards are prevented from taking defensive measures, and, thus, the Swedish takeover rules are rather takeover-friendly in that sense. The board may, however, at all times seek alternative bids (i.e., white knights).

Staggered boards do not exist (each board member is elected annually, and there is no way of preventing a new owner from making an immediate board replacement). Poison pills and stitching, etcetera, are not allowed under Swedish law.

v  Contact with shareholders
As set out in Section III, Swedish listed companies have a duty to disclose all inside information as soon as possible. Shareholders also receive information on all matters proposed to be decided upon by the general meeting. The notice to a general meeting shall be published and made available to the shareholders no later than three or four weeks (depending on the type of general meeting) prior to the general meeting and shall include information on the decisions proposed to be taken. Shareholders also have the right to ask questions at the general meeting, and in practice often do so in connection with the managing director's presentation of the financial statements of the company.

The company may generally contact individual shareholders as long as the contact is in the interests of the company and in accordance with the principle of the equal treatment of all shareholders (i.e., the contact may not be aimed at giving one shareholder undue benefit at the expense of other shareholders or the company). However, if inside information should be disclosed, MAR requires that the disclosure is made in the normal exercise of an employment, a profession or duties. Certain situations where the company engages in discussions with a major shareholder typically meet such criteria; these may include, for example, planned share issues or other corporate restructurings. In case of contemplated securities offerings, the rules regarding market soundings in the MAR may be applicable, and the company would have to comply with certain additional requirements in the MAR.

Large shareholders acting together will have to observe the rules relating to acting in concert, which may trigger an obligation to launch a mandatory takeover bid if the joint holding of shareholders acting in concert were to exceed 30 per cent of the votes in the company.
VI OUTLOOK

The updated EU Shareholders Rights Directive⁵ has necessitated changes to legislation and the Code, but these changes have not had any major impact on the Swedish corporate governance system as a whole. Among other things, the implementation of the Directive has restricted listed companies’ flexibility in relation to remuneration to the executive management and entails stricter transparency requirements in this regard, as listed Swedish companies, as from 2021, are required to draw up a remuneration report for each financial year and submit the report to the general meeting.

I OVERVIEW OF GOVERNANCE REGIME

The statutory corporate law set out in the Swiss Code of Obligations (CO) is the main source of Swiss corporate governance regulation. The CO applies to private and public companies. As regards corporate governance, the provisions of the CO focus on transparency, shareholder rights and the principle of parity between the company’s corporate bodies. The current governance rules of the CO are rather liberal and provide companies with considerable flexibility as regards the setup of their governance structure. A revision of the CO pending will increase governance regulation, mainly by increasing shareholder rights. In this context, the Swiss Ordinance against Excessive Compensation in Listed Companies (OaEC), which came into force in 2014, will be incorporated into the CO. The OaEC introduced restrictions on several remuneration practices and gives shareholders a binding say on pay as well as the right to elect the chair of the board of directors, the members of the compensation committee and the independent proxy. The stock market law incorporated in the Swiss Federal Act on Financial Market Infrastructures and Market Conduct in Securities and Derivatives Trading (FMIA) and its accompanying ordinances also contain governance rules, in particular the shareholders’ duty to disclose significant participations as well as general rules on public takeovers.

The SIX Swiss Exchange (SIX) issued the Listing Rules (SIX-LR) and various implementing directives and circulars. These regulations set the ground for good governance with binding rules on periodic financial reporting and, in particular, ad hoc disclosure rules applicable to all SIX-listed companies. The SIX-LR are complemented by the Directive on Information in relation to Corporate Governance (SIX-DCG) and the Directive on the Disclosure of Management Transactions (SIX-DMT). The SIX-DCG requires listed companies to include a chapter on corporate governance in their annual report. The SIX Exchange Regulation, the independent regulatory body within the SIX organisation, issues focus review letters indicating the topics on which SIX’s assessment will focus in the relevant

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1 Hans-Jakob Diem and Tino Gaberthüel are partners at Lenz & Staehelin in Zurich, Switzerland. The authors would like to thank Rebecca Schmid for her contribution to this chapter.
2 See Section VI.
3 SIX Swiss Exchange is the main stock exchange in Switzerland.
reporting period. The SIX-DMT requires companies to disclose transactions in its shares and related instruments by members of the board of directors or the management board. SIX is empowered to enforce its regulation through the SIX Exchange Regulation and the Sanctions Commission, which investigate violations and may impose sanctions. Their decisions and sanctions can be appealed to the independent Appeals Panel and, ultimately, to the SIX Arbitration Court.

Further, economiesuisse issued the Swiss Code of Best Practice for Corporate Governance (Code) primarily for public corporations. The Code contains non-binding recommendations and guidelines with a special focus on the rights and duties of shareholders and the board of directors. The core objectives are ensuring transparency as well as checks and balances between management and control by the means of comply or explain.

Independent proxy advisers (such as Ethos and zRating) regularly issue voting guidelines and corporate governance principles on which they base their proxy voting services and recommendations. Corporate governance is a key focus area of those regulations. Despite such regulations being non-binding, they have a significant influence on shareholders’ voting and public perception.

Besides the regulation applicable to listed companies in general, there are specific rules on corporate governance applicable to banks, investment companies and insurance companies. The circulars on corporate governance, risk management and internal controls at banks and insurance companies, respectively, and the circular on remuneration schemes of financial institutions issued by the Swiss Financial Market Supervisory Authority, are most relevant in this context.

II CORPORATE LEADERSHIP

i Board structure and practices

Swiss companies limited by shares are governed by the general meeting of shareholders and the board of directors. The board of directors and the shareholders’ meeting each have their respective duties and competences. This reflects the principle of parity. On a day-to-day basis, the board of directors represents the company in relation to third parties and conducts the business within the limits of the corporate purpose. The board of directors is thus the company’s responsible executive body that may represent the company and manage any matter not reserved to the shareholders’ meeting by law or the articles of incorporation. However, Swiss company law allows flexible, individual governance structures. In reality, the management of the day-to-day business (except for the non-transferable and inalienable duties of the board) is regularly delegated. In listed companies, the management is usually delegated to the chief executive officer (CEO) or an executive board, resulting in a two-tier structure. Such two-tier structure is mandatory for banks and security dealers.

Any matters that have not been allocated to the shareholders’ meeting by law or the articles of incorporation are the responsibility of the board of directors. Except for

8 economiesuisse is the largest umbrella organisation representing the Swiss economy.
the non-transferable duties, the board of directors may delegate its responsibilities to individual members of the board of directors or to third parties (the executive board). The non-transferable responsibilities of the board are:

a. the overall management of the company and the issuing of all necessary directives;
b. the determination of the company’s organisation;
c. the organisation of the accounting, financial control and financial planning systems as required for the management of the company;
d. the appointment and dismissal of persons entrusted with managing and representing the company;
e. the overall supervision of the persons entrusted with managing the company, in particular with regard to compliance with the law, articles of association, operational regulations and directives;
f. compilation of the annual report, preparation for the general meetings and the implementation of its resolutions;
g. the notification of the court in the event that the company is over-indebted; and
h. for listed companies, the preparation of the compensation report as requested by the OaEC.

The board of directors may establish special committees. The Code recommends the establishment of an audit committee and a compensation and nomination committee. The audit committee’s members should have specific expertise in the area of finance and audit. Moreover, the OaEC requires listed companies to establish a compensation committee whose members must also be members of the board of directors and who are elected by the general meeting of shareholders.\textsuperscript{10} The articles of incorporation must set out the basic rules of the activities of the compensation committee. Further, the audit as well as the nomination and compensation committee should mainly be composed of independent, non-executive members. While the board of directors is ultimately responsible for the succession of the CEO as well as its members, the nomination committee establishes principles for and prepares the succession process.

The main rules regarding the remuneration of the board of directors and the management board of listed companies are set out in the OaEC (and will be transferred into the CO once the pending revision will have been completed and approved by the legislator. For more information on the status of this revision, see Section VI). The shareholders’ meeting has a binding vote on the remuneration of the board of directors and the executive board. The basis for this is the compensation report, which must be prepared by the board of directors and which is subject to a consultative vote by the general meeting of shareholders. Moreover, pursuant to the OaEC, certain forms of remuneration are prohibited, such as severance and similar payments (golden parachutes), advance compensation payments, and payments linked to the purchase or sale of companies.

\textbf{ii} Directors

The board of directors may consist of one or several members. If a company has issued different share classes, each share class may elect at least one representative to the board of directors. In practice, the board of directors consists of several members. The Code recommends that

\textsuperscript{10} Article 733 Draft CO.
the composition of the board be diverse as regards expertise and gender. The revised draft CO provides for a gender quota for listed companies exceeding certain thresholds.\textsuperscript{11} In contrast to other jurisdictions, the Swiss approach is rather soft. It is envisaged that each gender shall make up at least 30 per cent in the board of directors and at least 20 per cent in the executive board.\textsuperscript{12} If the quotas are not met, the report on compensation must specify the reasons for missing the quotas as well as the planned measures to reach the quotas in the future. It is contemplated that companies will have five years to establish the quota in the board of directors and 10 years to do so in the executive board.\textsuperscript{13}

Further, the Code stresses the importance of having a majority of independent, non-executive members in the board of directors. All board members have the same rights and duties. To ensure efficiency, the Code recommends that the board of directors shall not be too big. Pursuant to the revised draft CO, the appointment of a secretary by the board of directors will no longer be required.\textsuperscript{14} Pursuant to the CO, the term of office is generally three years unless the articles of incorporation state differently. However, for listed companies, the OaEC limits the term to one year. Re-election is possible. The members of the board of directors are elected by the shareholders’ meeting. In listed companies, the chair must also be elected by the shareholders’ meeting. In addition, the OaEC requires that the company’s articles of incorporation limit the maximum number of activities that a member of the board of directors, the executive board or an advisory board may carry out in other legal entities or other organisations registered in the Commercial Register (or a similar register abroad).

Any member of the board of directors may request information on all matters relating to the company. Any member of the board of directors and the executive board is required to provide information during a board meeting. Outside of board meetings, members of the board of directors may ask members of the executive board about the general business performance and, upon special request, about individual transactions. Inspection of files and records is only possible as far as it is necessary for a member of the board of directors to fulfil his or her duties.

Under the CO, unless the articles of incorporation state otherwise, each member of the board of directors can represent the corporation towards third parties. In practice, signing authority is regularly limited to joint signing authority. Moreover, at least one representative with individual signing power or two representatives with joint signing power must reside in Switzerland.

In the case of a two-tier structure, the relationship between the board of directors and the management board must be governed in the organisational regulations. The Code recommends having a two-tier structure with a majority of non-executive board members, and a separation of the functions of chair and CEO. If the company decides that the same

\textsuperscript{11} Article 734f Draft CO; the vote on the introduction of a gender quota was won with 95 to 94 votes in the 2018 summer session of the National Council.

\textsuperscript{12} A minority of the National Council was in favour of a higher quota (i.e., a representation of each gender of at least 40 per cent in the board of directors and at least 30 per cent in the executive board).

\textsuperscript{13} The commission of the National Council deviated from the draft bill of the Federal Council and intended to abolish Article 734f 10 years after the entering in force of the new legislation. The National Council, however, rejected such proposal with 97 to 94 votes.

\textsuperscript{14} This is, in essence, because the function of the secretary was rarely used in practice and could, therefore, be disposed of in the view of the Federal Council (Dispatch of the Federal Council on the partial revision of the CO, BBl 2017 399, 567). The National Council did not deviate from this proposed amendment.
person shall act as chair and CEO, the board of directors should establish certain control mechanisms to ensure appropriate checks and balances. For instance, an independent lead director who can independently convene and lead a board meeting should be appointed.

The board of directors must act in the best interest of the company as mandated by the duty of care and loyalty. Shareholders must be treated equally in like circumstances. According to the general view, the company’s interest encompasses the interests of the shareholders as well as the other stakeholders, with the sustainable growth of the company being the underlying principle and goal. There are no (strict) rules as to how the board should weigh the interests of the different stakeholders against each other: ultimately, this weighing and other business decisions are a matter for the board’s own diligent judgement. In various decisions of the Federal Supreme Court, the applicability of the business judgement rule has been confirmed. The prerequisites for the applicability of the business judgement rule are a diligent review or assessment process that is based on adequate information and documents and that is free of conflicts of interest. If these prerequisites are met, the Court will only assess whether the board’s decision was justifiable. If any of the prerequisites are not met, the Court will conduct a full assessment. However, a board decision based on a conflict of interest is not per se a violation of the board’s duty of care.

Under Swiss corporate law, a conflict of interest is deemed to exist if a board member has individual interests that are opposed to the interests of the company or, more frequently, if he or she has a duty (based on law, contract or otherwise) to pursue third-party interests that are opposed to the company’s interests. If a board member suffers from a potential conflict, he or she has an obligation to disclose such information to the chair or the entire board. It is then up to the board, without the potentially conflicted member, to assess the situation and resolve upon and implement appropriate measures as required to ensure that the conflict does not negatively affect the company. Such measures include an abstention of the conflicted member from the decision and, depending on the circumstances, also from the deliberations, or the establishment of an independent committee consisting of the disinterested board members. If required to address a more serious and detrimental conflict, the board may also decide to shield the conflicted member from any critical information. The draft CO set forth a specific provision dealing with conflicts of interest of board members. However, the commission of the National Council found the provision to be too broad with regard to the fact that conflicts of interest can have a wide range of nuances. The National Council followed this reasoning and voted against the introduction of the new provision with 143 to 53 votes.

III DISCLOSURE

SIX requires listed companies to publish audited annual financial statements and non-audited half-year accounts in accordance with common reporting standards, such as the IFRS or US GAAP. Listed companies must include a corporate governance report in their annual reports. The information to be published in the corporate governance report is set out in the SIX-DCG and includes, among other things, information on the group and capital structure, shareholders, change of control provisions and defence measures as well as information on the members of the board of directors and executive board, basic rules of compensation and share and option plans. Pursuant to the OaEC, the board of directors is required to prepare a compensation report. The remuneration paid directly or indirectly to current or former

15 Article 717a Draft CO.
members of the board of directors or the executive board must be listed in the compensation report. For the board of directors, the compensation of each individual must be disclosed, while for the executive board, only the aggregate amount and the highest salary paid have to be disclosed. Other than in the European Union, non-listed companies in Switzerland are not required to publish their annual reports.

The external auditors must audit the annual financial statements as well as the compensation report. Auditors must comply with strict independence requirements. They must be independent of the board of directors, the executive board and major shareholders. Auditors may not conduct business for or engage in other ways with the company outside the audit work if such activities were to endanger their independence. Auditors cannot audit their own work or the work of persons close to them. Moreover, auditors are not allowed to audit companies in which they hold a direct or significant indirect participation or against which they have a substantial claim or debt. The lead auditor of an audit mandate must be changed every seven years. In addition, auditors must meet the qualification requirements of the Federal Act on the Admission and Supervision of Auditors. The qualification requirements concern professional education and the auditor’s good standing.

Listed companies have to publish price-sensitive information occurring in the sphere of the company (under ad hoc publicity rules) as well as management transactions. The Code recommends publishing the articles of incorporation on the company’s website and making the organisational regulations available to shareholders. 16

Shareholders have disclosure duties, too. If a person (acting alone or in concert with others) directly or indirectly acquires or disposes of shares of a listed company, and reaches or crosses any of the thresholds of 3, 5, 10, 15, 20, 25, 33.33, 50 or 66.66 per cent of the voting rights of the company, such person is obliged to make a disclosure to the company and SIX. Separate disclosure duties exist for long positions (shares, long call, short put, etc.) and short positions (short call, long put, etc.). Netting of long and short positions is not permitted. Such disclosures are published on the website of SIX.

As regards non-listed companies, an acquirer of bearer shares must report his or her name, date of birth, nationality and address to the company. 17 In addition, an acquirer or a group of acquirers of registered or bearer shares representing 25 per cent or more of the share capital or voting rights must report the name and address of its ultimate beneficial owner to the company. 18 Any change to the notified information must be reported within three months. Note that this notification duty does not apply to listed companies. Further, if a company is controlled by a listed company, then the shareholder only has to notify its name and seat and the fact that it is a listed company or controlled by a listed company. The company is required to keep a register of the holders of bearer shares and the ultimate beneficial owners of shareholders holding 25 per cent or more of the share capital or voting rights. The notifications must be stored for 10 years. The register is not open to the public. Further, pursuant to a change of the Co that entered into force on 1 November 2019, as of 30 April 2021, Swiss companies are no longer allowed to issue bearer shares (except for listed companies and companies that have issued bearer shares in the form of certificated securities (Bucheffekten). Any existing bearer shares will have to be converted into registered shares.

16 Also see Section V.i for more details on the shareholders’ right of inspection.
17 This notification duty does not apply if the bearer shares are issued in the form of certificated securities (Bucheffekten).
18 This notification duty does not apply if the bearer shares are issued in the form of certificated securities.

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IV CORPORATE RESPONSIBILITY

The board of directors is responsible for the executive management of the company and must act in the company’s best interests. Establishing adequate risk and compliance management is considered to be inherent to this duty and part of good corporate governance. A requirement of the board to establish a risk committee is, however, only mandatory for certain financial institutions. Most Swiss companies allocate the responsibility at board level to the audit committee or determine risk-owners for different risk categories. The CO and the Code oblige the board of directors to establish an internal control system. To complement the Code, economiesuisse issued the Principles on Effective Compliance Management (Compliance Principles). The core of these principles is that the board of directors and the executive board must set the tone from the top to implement effective compliance structures.

The Swiss perspective on whistle-blowing is rather cautious. The Compliance Principles state that a whistle-blowing system forms part of effective compliance management. While the European Union has now voted for a specific directive on whistle-blowing, Swiss company law does not yet address whistle-blowing explicitly. However, the board of directors has an inalienable duty to ensure effective supervision over the company, wherein whistle-blowing structures should be included. In addition, Swiss employment law implicitly protects whistle-blowers from being dismissed or otherwise discriminated against as long as the act of blowing the whistle was proportionate. Along with the pending revision of the CO, these implicit protective measures shall be implemented in Swiss employment law by explicitly determining when and how a whistle-blower can report a misconduct under any laws or regulations in a legally protected and authorised way.

The board of directors’ duty of care also covers aspects of corporate social responsibility (CSR), as acts against societal values may harm the company and may pose financial, operational and reputational risks. The Code specifically states that the board of directors must avoid such risks. Swiss company law allows the board of directors and the executive board to take into account interests of stakeholders other than the shareholders. Employment law, the Gender Equality Act and any legislation regarding environmental protection cover certain CSR aspects must be observed by companies in general.

Under the SIX-DCG, companies may opt in on the duty to publish a sustainability report. If a company chooses to do so, SIX will publish the opting in on its website. In the case of opting in, companies are required to prepare a sustainability report in accordance with internationally recognised standards selected by SIX.

In 2016, a popular initiative of the Swiss Coalition for Corporate Justice (SCCJ) aimed at increasing corporations’ human rights and environmental protection efforts was submitted,
and it will be put to a Swiss people’s vote some time in the future. The initiative proposes that companies should be required to conduct due diligence on human rights and environmental sustainability for their businesses in Switzerland and abroad. Otherwise, they should become liable for violations of national and international human rights and environmental standards taking place in their business activities in Switzerland and abroad. The Federal Council, as well as several political parties, have rejected the initiative. The Federal Council responded with a counter-proposal that would require companies to report on respect for human rights and the environment, but does not provide for direct liability of companies in the event of violations. These various proposals are currently under debate in the Swiss Parliament.

V SHAREHOLDERS

i Shareholder rights and powers

Shareholders of Swiss companies have financial as well as non-financial rights. Financial rights entail the right to receive dividends that have been resolved by the shareholders’ meeting. Dividends can only be distributed from free reserves. Free reserves include disposable balance sheet profits and specifically dedicated reserves. In the event of the liquidation of a company, shareholders have a right to receive liquidation proceeds.

Non-financial rights include protection and participation rights. The main aspect of shareholders’ protection rights is the relative requirement of the equal treatment of shareholders. In principle, one share means one vote, and every shareholder has at least one vote. Swiss law does not grant any special rights (super-voting or special dividend rights) to long-term shareholders. A company may issue different share classes and allocate different voting power to such shares. This special voting power does not apply to a number of resolutions, such as the election of the auditors or a special audit. Certain resolutions of the shareholders’ meeting require a higher quorum than the regular majority vote (e.g., change of corporate purpose, limitation or exclusion of subscription rights, limitation of transferability of shares). Another protective right is the subscription right of existing shareholders in the event of a capital increase. The subscription right may be limited or excluded for important reasons by a qualified shareholders’ resolution. The action for liability, and the right to challenge shareholder resolutions that violate the law or the articles of incorporation or to claim their annulment, are further mechanisms to protect shareholders’ rights.

Participation rights entail certain information and supervision rights. Shareholders must be provided with the annual financial statements and, if applicable, the auditor’s report. In addition, shareholders may demand further information regarding the business of the company and the audit process. Shareholders may also request to inspect the company’s books and correspondence as far as such inspection does not harm business secrets or other shareholders’ interests. Shareholders may demand the performance of a special audit.

Shareholders who, alone or as a group, hold 10 per cent or more of the share capital or a participation of at least 1 million Swiss francs have the right to request the convening of a shareholders’ meeting. In addition, shareholders holding, alone or as a group, 10 per cent or more of the share capital or a participation of at least 1 million Swiss francs can request that additional items are put on the agenda of a shareholders’ meeting. Any shareholder, regardless of the size of his or her shareholding, can bring a proposal to any agenda item of

a shareholders’ meeting. The pending revision of the CO envisages lowering the mentioned thresholds to facilitate the performance of these rights. Under the revised draft CO, it is currently contemplated that, for listed companies, shareholders holding at least 5 per cent of the share capital shall be permitted to request the convening of a shareholders’ meeting and shareholders holding at least 0.5 per cent of the share capital shall be permitted to request that an item be put on the agenda of a shareholders’ meeting.\textsuperscript{25} The convocation to a general meeting of shareholders (including agenda items and proposals of the board of directors) must be made public at least 20 calendar days prior to the shareholders’ meeting. At the shareholders’ meeting, any shareholder has the right to express his or her view on any agenda item.

\hspace{1cm} \textbf{ii Shareholders’ duties and responsibilities}

Under Swiss corporate law, shareholders of a company traditionally only have the duty to pay the issue price of the subscribed shares. It is the general prevailing view that shareholders of a company do not have a duty of loyalty in relation to the company, and that they are not liable for the company’s obligations. In listed companies, shareholders must disclose their participation when crossing the thresholds of 3, 5, 10, 15, 20, 25, 33.33, 50 or 66.66 per cent of the voting rights (see Section III).

There is no general code of best practice or guideline for shareholders in Switzerland. However, economiesuisse issued the ‘guidelines for institutional investors governing the exercise of participation rights in public limited companies’ (Investors’ Code) in 2013.\textsuperscript{26} The Investors’ Code sets out five principles governing how institutional investors should exercise their participation rights in public companies. The main goal is that institutional investors take seriously their responsibility towards clients with regard to ensuring long-term, effective corporate governance of the companies in which they are invested. According to the Investors’ Code, institutional investors should systematically exercise their participation rights, and do so in the best interest of their clients. Furthermore, institutional investors shall communicate how they exercise their participation rights, including the underlying reasoning. Following the comply or explain approach, all investors who have agreed to implement the Investors’ Code have to publish a statement of accountability wherein they explain any deviation from the Investors’ Code.

The binding OaEC requires pension funds to exercise their voting rights in the election of the board members, the chair, the members of the compensation committee and the independent proxy, as well as regarding further items such as compensation. Pension funds must additionally disclose to their clients on an annual basis how they have exercised their voting rights.

\hspace{1cm} \textbf{iii Shareholder activism}

Shareholder activism and proxy fights in Switzerland have increased considerably over the past few years. Most recent activist campaigns include Cevian Capital’s campaign against Panalpina’s chair, who as a result had to resign from office. Cevian Capital further played an important role in the sale of a majority stake of ABB’s power grids division to Hitachi,

\textsuperscript{25} The National Council voted for an increase of the threshold to put items on the agenda from 0.5 to 3 per cent.

\textsuperscript{26} Available at www.economiesuisse.ch/en/publications/swiss-investors-code-downloads.
which was the largest Swiss M&A transaction in 2018. A further recurring name on the list of activist shareholders is Daniel Loeb, who, through his investment company Third Point, repeatedly raised demands to Nestlé, including the desire to sell Nestlé's stake in L'Oréal. In another campaign, Swiss activist funds Veraison proposed, among others, the election of outside chairman to the board of directors of SIX-listed Comet. After a public battle, Comet's candidate was elected as chairman by the shareholders with a mere 18,000 more votes than the board's candidate. In two other attempts, Sentis Capital and Veraison, respectively, requested an extraordinary shareholders' meeting at SAIX-listed Meyer Burger and Implenia, respectively, and the removal and election of board members. Neither campaign was successful.

In Switzerland, the demands of most activists target the composition of the board of directors (including the chairman) and executive board (in particular, the CEO) as well as their compensation, a review of and change in strategy, or corporate restructurings. Proxy advisers such as ISS, Glass Lewis and Ethos are also active in the Swiss market.

Swiss law does not provide for special provisions applicable to shareholder activists. In particular, shareholders are not allowed to inspect the share register. Moreover, the board of directors is not required to distribute to the company's shareholders any statements made by activist shareholders. As a consequence, the board of directors entertains private conversations and settlement discussions with the activist and, if such discussions are not successful, a public proxy fight between the board and the activist is started. In proxy fights it is not uncommon for the company (as well as the activist shareholder) to engage a proxy solicitor to identify shareholders, to explain the board's (or shareholder's) position and arguments, and to convince shareholders to exercise their voting rights at the shareholders' meeting. Activist shareholders may challenge shareholder resolutions. Moreover, as an interim measure, activists may request the blocking of the commercial register to prevent or at least delay the registration of a merger or capital increase.

iv Takeover defences

The Swiss takeover rules prevent the board of directors and management of the target company from taking frustrating actions without shareholders' approval after a tender offer has been formally announced. Frustrating actions are defined as those that significantly alter the assets or liabilities of the target company (e.g., the sale or acquisition of any target company's assets at a value or price representing more than 10 per cent of the total consolidated balance sheet or contributing more than 10 per cent to the profitability of the target company; the conclusion of contracts with members of the board of directors or senior management providing for unusually high severance payments). The target board is also prohibited from acquiring or disposing of treasury shares or respective derivatives, and from issuing any conversion or option rights, unless such transactions are made in the context of pre-existing employee share programmes or obligations under pre-existing instruments (such as pre-existing convertible bonds). In addition, the Swiss Takeover Board has the authority to object to defensive measures that manifestly violate company law.

However, the board may still take other steps to counter an unsolicited informal approach or formal offer, including seeking a white knight, running a PR campaign or

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27 In the context of the pending revision of the CO, it was discussed whether shareholders should be granted a right to inspect the share register. In the end, such right has not been incorporated in the revised draft CO.
bringing legal action against the bidder, especially on the basis that the bidder has not complied with its disclosure obligations, or if the terms of its offer are not in line with the takeover rules. The board could also call an extraordinary shareholders’ meeting and propose more effective defence measures, such as the sale of a material part of the business or the issuance of new shares. Apart from specific defence measures in response to a specific bid, the articles of a number of listed Swiss companies contain preventive clauses, particularly transfer and voting rights restrictions, which an offeror will normally seek to have removed from the articles as a condition to closing. Under such circumstances, the board is generally perceived to have more leverage in discussions with a bidder, especially in relation to the financial terms of a proposed offer. Since the OaEC came into effect, listed companies are no longer permitted to have staggered boards, as board members may only be elected for one year.

v Contact with shareholders

The main means of contact between a company and its shareholders is the annual general meeting of shareholders. In addition, shareholders may request special information from the company. Listed companies are required to make ad hoc notifications of price-sensitive facts arising within the sphere of the company.

It is quite common for listed companies to entertain regular contact with its major shareholders and proxy advisers to explain the company’s long-term strategy and to better understand shareholder concerns. However, the principle of equal treatment of shareholders, ad hoc publicity and insider regulations in principle require the board to not disclose non-public price-sensitive information to selected shareholders. Any such contacts must be in the interest of the company. These contacts are often entertained by the chair, the lead director and investor relations.

The pending revision of the CO also intends to improve communication with shareholders by facilitating the use of technology. For instance, listed companies shall be required to offer shareholders the possibility to request registration in the share register by electronic means (e.g., email). In addition, it is contemplated that shareholders shall have the possibility of electronic remote voting. Under the OaEC, listed companies are already required to provide shareholders the opportunity to grant electronic proxies to the independent proxy.

Institutional investors and proxy advisers have gained relevance over the past few years. In this context, the Investors’ Code introduced the duty for institutional investors to inform their shareholders about how they exercise their voting rights. The OaEC follows the same principle and requires pension funds to actually exercise their voting rights as regards certain agenda items, such as the election and compensation of board members. In addition, pension funds must disclose on an annual basis to their clients how they have exercised their voting rights.

28 Article 686b Draft CO. The National Council decided to include said provision in Article 686 Paragraph 2 bis.
29 Article 701c et seqq. Draft CO.
VI OUTLOOK

Swiss corporate law is undergoing significant revision. The key amendments will be the following:

a creating more liberal provisions for the establishment of corporations as well as provisions regarding the capital structure (for instance, the introduction of capital bands to create more flexibility for capital increases and decreases);

b improving corporate governance and shareholder rights;

c modernising shareholders’ meetings by the increased use of electronic and digital means;

d transferring the rules of the OaEC into the CO;

e implementing gender quotas;

f further smaller adaptations, for instance as regards provisions on corporate restructuring, reserves and own shares; and

g implementing transparency provisions for companies active in commodity trading similar to the newly adopted EU regulations.

30 After the revised Draft CO had been debated by the National Council in the summer of 2018, the Council of States was supposed to debate the Draft CO in the winter of 2018. However, its preparatory commission for legal affairs amended the draft in many ways (e.g., it eliminated the possibility for capital bands and went beyond the requirements stipulated in the OaEC in various respects). As a result, the Council of States rejected to debate the Draft CO, and instead sent it back to the commission for legal affairs, which then came up with new proposals. These new proposals are currently being discussed in the National Council and the Council of States.
I OVERVIEW OF GOVERNANCE REGIME

The United Kingdom (UK) system of corporate governance is generally seen as an effective model that has influenced many other jurisdictions in Europe and Asia. This helps to attract international companies wishing to gain access to a wide pool of investors, who are reassured by the governance obligations placed on issuers regardless of where their key business operations are located. In this chapter we focus on UK-incorporated companies with a premium listing on the Main Market of the London Stock Exchange. Requirements are relaxed, to a degree, for companies that are only able (or only choose) to obtain a standard listing, that are unlisted or that are not UK-incorporated companies.

The UK corporate governance system comprises laws, codes of practice and market guidance. Mandatory and default (i.e., opt-in or opt-out) rules and legal standards derive from common law, from statute (notably the Companies Act 2006 (Companies Act)) and from regulation (notably the Listing Rules and the Disclosure Guidance and Transparency Rules (DTRs) published by the Financial Conduct Authority (FCA), which is a statutory body). Some of these laws and regulations derive from EU law, but some are specific to the UK. The City Code on Takeovers and Mergers (Takeover Code) also has an important role to play in control-seeking transactions, and has statutory force. Each company’s constitution, which will also impose governance requirements, has legal effect as a statutory contract between the company and its members.

The most important code of practice is the UK Corporate Governance Code (the Code), which is published and updated periodically by the Financial Reporting Council (FRC), which is also a statutory body. The current edition of the Code was published in 2018 and, as of 1 January 2019, applies to all accounting periods. In parallel, the UK Stewardship Code (Stewardship Code) seeks to drive best practice in enhancing the quality of engagement between investors and companies, and applies to the institutional investor community and not to companies directly. It was recently revised by the FRC, with the revised version taking effect from 1 January 2020. Finally, guidelines from the institutional investor community supplement these laws, regulations and codes of practice.

Despite not being of relevance to the companies we are considering here, it is worth noting that a new set of corporate governance principles for large private companies was published in December 2018. The Wates Principles are designed to assist large private companies to comply with the new statutory requirement for all companies of a significant

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1 Murray Cox is a partner and Hayden Cooke is an associate at Slaughter and May. The authors would like to thank Imogen Green for her help in preparing this edition of the UK chapter.
size, which were not previously required to provide a corporate governance statement, to disclose their corporate governance arrangements. The Wates Principles introduce a more flexible approach to good corporate governance than the Code.

The bedrock of best practice corporate governance in the UK is a unitary board collectively responsible for the long-term success of that company. Core provisions include:

- a separate chair and CEO;
- a balance of executive and independent non-executive directors;
- strong, independent audit, nomination and remuneration committees;
- transparency on appointments and remuneration; and
- effective rights for shareholders (including a binding say on pay and without-cause removal rights), who are encouraged to engage with the companies in which they invest.

One defining feature of the Code is the comply or explain approach: rules for companies with a stock exchange listing (Listing Rules) require all companies either to comply with the Code or to explain why they do not. The Code is issued with an acknowledgement of flexibility; this is in recognition of the principle that no single governance regime would be appropriate, in its entirety, for all companies. This approach does, however, rely on shareholder engagement to challenge non-compliance where appropriate. Nevertheless, the FRC noted that 95 per cent of all FTSE 350 companies (the 350 largest UK-listed companies by market capitalisation) reported full compliance with the previous edition of the Code, or full compliance with all but one or two provisions, and there are encouraging steps being taken toward compliance with the latest edition of the Code. In many cases, non-compliance is due to circumstances rather than deliberate choice. This confirms that the provisions of the Code are widely adopted by companies despite the comply or explain philosophy.

The Code states that an explanation for non-compliance should set out the background, provide a clear rationale for the action being taken and explain the impact that action has had. Where non-compliance is intended to be limited in time, companies are required to indicate when they expect to conform to the relevant provision of the Code.

For the past few years, the UK system of corporate governance has, much like other systems around the world, been the subject of political and media scrutiny. Much focus has been on the responsibilities of business to a wider set of stakeholders in the context of some high-profile scandals, business failures and a shifting paradigm on corporate purpose. The revised Code reflects some of this debate; it envisages more companies becoming subject to its standards, removes certain exemptions for public companies outside the FTSE 350 and extends certain governance principles to large private companies. However, there remains, in many respects, a gulf between the baseline legal duties of companies and directors, and recent commentary around corporate purpose and governance.

II CORPORATE LEADERSHIP

i Board structure and practices

The UK system features a unitary board. There is no two-tier structure: executive directors and independent, non-executive directors instead act together as one board. The company’s powers are exercised by its board acting collectively, with a small number of decisions requiring shareholder approval. In practice, substantial managerial authority is delegated by the board to the company’s executives; the board appoints the executives and exercises an oversight function by approving decisions that do not require shareholder approval and that...
have not been fully delegated. Standing committees of the board typically include at least a nomination committee, audit committee and remuneration committee, but the creation of other standing committees, or ad hoc committees to exercise delegated powers, is permitted.

There is currently no co-determination principle in the UK requiring seats on the board to be reserved for employee representatives. However, as its most significant new proposal, the Code seeks to amplify the voice of workers in the boardroom. Companies can choose from three options to achieve this: a director appointed from the workforce, a formal workforce advisory panel or a designated non-executive director with specific responsibility for ensuring that the views of the workforce are represented to the board. Around 60 per cent of companies have taken the designated non-executive director approach, with the next most popular approach a combination of two or more of the above or alternative appropriate arrangements, such as employee forums.

The Code recommends that the board and its committees should have an appropriate balance of skills, experience, independence and knowledge of the company to enable them to discharge their respective duties and responsibilities effectively. At least half of the board, excluding the chairperson, is required to comprise individuals determined by the board to be independent. This way, no individual or small group of individuals can dominate the board’s decision-making. It is the CEO, however, who is responsible for delivering the agreed strategy and for the day-to-day running of the company’s business.

The criteria for determining whether a director may be regarded as independent are set out in the Code. A director will not be regarded as independent if that director:

a. has been an employee of the company or its group within the past five years;
b. has, or has had within the past three years, a material business relationship with the company;
c. has received or receives additional remuneration from the company apart from a director’s fee, participates in the company’s share option or a performance-related pay scheme, or is a member of the company’s pension scheme;
d. has close family ties with any of the company’s advisers, directors or senior employees;
e. holds cross-directorships or has significant links with other directors through involvement in other companies or bodies;
f. represents a significant shareholder; or
g. has served on the board for more than nine years from the date of their first election.

The Code requires that the board constitutes a nomination committee, an audit committee and a remuneration committee. The strength and independence of these committees – whose particular duties are addressed in the Code and in recommended terms of reference published by ICSA – is a key factor in ensuring effective corporate governance, although ultimate responsibility for areas addressed by these committees remains with the board collectively. Some boards also constitute a risk committee that is separate from the audit committee, and has responsibility for overseeing risk exposure and future risk strategy.

The Code recommends that the audit committee should comprise at least three directors, all of whom are independent and one of whom should have recent and relevant financial experience. The chairperson of the board should not be a member of the audit committee. FTSE 350 companies are required to put their audit engagement out to competitive tender at least every 10 years, and the audit committee oversees this process.

The nomination committee should comprise a majority of independent directors. The chairperson of the board can be a member of (and chair) the nomination committee,
but should not chair the committee when dealing with the appointment of their successor. The remuneration committee should comprise at least three independent directors. The chairperson of the board may sit on (but not chair) the remuneration committee, provided they were independent on appointment. Before appointment as chair of the remuneration committee, the appointee should have served on a remuneration committee for at least 12 months.

The separation of chairperson and CEO is one of the key checks and balances of the UK system. It has been recognised for some time that combining the roles increases the likelihood of one individual having unfettered decision-making powers. The Code recommends splitting the role of chairperson and CEO, and that the division of responsibilities between the two positions should be clearly established. If the roles of chairperson and CEO are combined (or if the CEO succeeds as chairperson), this must be publicly justified in accordance with the comply or explain principle, and the company should consult with major shareholders ahead of appointment, from whom it should expect close questioning.

**Executive pay**

The Code states that executive remuneration should be aligned to the company’s purpose and values. A significant proportion of executive directors’ remuneration should be structured to link rewards to the successful delivery of the company’s long-term strategy (but pay for non-executive directors should not include performance-related elements).

Levels of executive remuneration have been heavily criticised by the public and in the media in recent years. In October 2019, following the collapse of Thomas Cook, directors were widely criticised in the media for their large remuneration packages during the company’s final years. Standard Chartered also recently experienced 40 per cent of its shareholders voting against its new remuneration policy owing to a change in the methodology used to calculate executive pension allowances. The protest vote was the largest at a UK bank for five years.

Long-term incentive plans (LTIPs) have been the source of much scrutiny, and the Code now contains enhanced governance requirements for such plans. Among other things, there is a requirement for a five-year combined holding period between award and the participant receiving any economic benefit, and a requirement for companies to have clawback powers. The Code also requires additional disclosures to be made by the remuneration committee, for example, as to why the remuneration package is appropriate, how factors such as risk (behavioural and reputational) have been considered, and whether any discretion has been applied to the remuneration outcomes. The remuneration committee is also required to engage with shareholders and the workforce in setting executive remuneration, and to report on this engagement and its outcomes.

Shareholders of UK-incorporated, listed companies have a binding vote on companies’ directors’ remuneration policy. In broad terms, shareholders are required to approve, at least every three years, a policy setting limits and conditions for directors’ remuneration. If payments and awards made by the company to its directors are not consistent with the shareholder-approved policy, they are recoverable from the director in question, and the directors responsible for approving the unauthorised payment or award are liable to compensate the company. Shareholders have, in addition, an annual advisory (i.e., non-binding) vote on the implementation of the approved policy during the previous year. Companies are also obliged to publish a report on directors’ remuneration in their annual report, including the remuneration policy in the years it is being put forward for approval. This regime does not apply to employees or consultants who are not directors.

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On 10 June 2019, the amended EU Shareholder Rights Directive was implemented in the UK. Key changes include a new requirement to keep remuneration reports available on a company’s website for a period of 10 years and to disclose the annual change in each director’s remuneration to the annual change in average pay of the company’s employees over a five-year rolling period. Previously, the requirement was to keep remuneration reports available for one year, and only the CEO’s remuneration was compared to the average employee’s remuneration (although this requirement was, in itself, novel and relatively untested in the UK).

Where a company has 250 or more employees, it is also required to publish statutory calculations each year showing the size of the pay gap between male and female employees.

ii  Directors

The role of the independent director is seen as essential in providing a balance on the boards of listed companies, and the Code and related guidance emphasise the need for independent directors to be suitably experienced, committed and prepared to challenge the executive directors. The Code emphasises the need for the board to promote the long-term sustainable success of the company, generating value for shareholders and contributing to wider society. It is the board’s responsibility to establish the company’s purpose, values and strategy, aligning each with the culture of the company. The concept of purpose is a novel and much-discussed requirement of the Code and there is little in the way of guidance as to how a company should establish, articulate, monitor and report against a statement of purpose (to the extent it does not do those things already). Statements of purpose are necessarily unique to each company, but each should focus on the stakeholder considerations necessary to ensure the long-term sustainable success of that company (i.e., the derivative generation of economic value for shareholders). The FRC’s recent corporate governance review suggests that only 50 per cent of companies surveyed are currently articulating a purpose beyond generating a profit. The FRC expects investors to undertake closer analysis of the narrative used in company statements to assess a company’s approach to its workforce and stakeholders, including to determine whether there is evidence of a clear sense of corporate purpose, culture and values, and how these align with the company’s strategy.

The primary function of independent directors, according to the Code, is to scrutinise the performance of management and monitor the reporting of performance. The board should appoint an independent director to be the senior independent director to provide a sounding board for the chairperson and to serve as an intermediary for the other directors and shareholders when necessary. The senior independent director should be available to shareholders if they have concerns that contact through the normal channels of chairperson, CEO or other executive directors has failed to resolve, or for which such contact is inappropriate. The FRC’s Guidance on Board Effectiveness (2018) further emphasises the critical role of the senior independent director to help resolve significant issues when the board is under periods of stress. Independent directors should hold meetings without the executives being present both with the chairperson and, at least annually, without the chairperson (led by the senior independent director) to evaluate the chairperson’s performance.

In practice, independent directors generally meet with the other directors for board meetings at least eight times per year in addition to attending committee meetings. They should (and often do) have direct access to all staff below board level and all advisers and operations, and receive information at an early stage (before executive directors have made key decisions). The Code provides that, as part of their role as members of a unitary board, independent directors should constructively challenge and help develop proposals on
strategy. On the other hand, a conscientious and independent standard of judgement, free of involvement in the daily affairs of the company, is seen as an independent director’s key contribution to the boardroom. In this regard, the board is required to determine annually whether a director is independent in character and judgement and whether there are relationships or circumstances that are likely to affect the director’s judgement.

Independent directors should also monitor the performance of management in meeting agreed performance objectives. They should satisfy themselves on the integrity of financial information and that financial controls and systems of risk management are robust and defensible. They are responsible for determining appropriate levels of remuneration of executive directors, and have a prime role in appointing and, where necessary, removing, executive directors, and in succession planning.

**Directors’ duties**

All directors, both executive and non-executive, owe the same fiduciary duties and a duty of care and skill to the company. These duties are derived from common law but have now been largely codified under the Companies Act. These statutory duties are:

- to act within their powers (i.e., in accordance with the company’s constitution);
- to exercise their powers in good faith in the manner they consider most likely to promote the success of the company for the benefit of its shareholders;
- to exercise independent judgement;
- to exercise reasonable care, skill and diligence;
- to avoid conflicts of interest;
- not to accept benefits from third parties; and
- to declare any interest in a proposed transaction or arrangement with the company.

These statutory duties must still, however, be interpreted and applied in accordance with the pre-existing common law duties. Indeed, in respect of some directors’ duties that have not been codified under the Companies Act, the common law rules remain the only relevant law. These include the duties not to fetter their discretion, not to make unauthorised profits by reason of their office and to keep the affairs of the company confidential.

UK law has adopted the enlightened shareholder approach to the orientation of its directors’ duties. The Companies Act requires directors, when deciding how to exercise the powers of the company, to have regard to:

- the likely consequences of any decision in the long term, the interests of the company’s employees, the need to foster the company’s business relationships with suppliers, customers and others, the impact of the company’s operations on the community and the environment, the desirability of the company maintaining a reputation for high standards of business conduct, and the need to act fairly as between members of the company.

Much recent discussion of corporate governance reform has centred on the duties companies owe to stakeholders. The Code now seeks to ensure that companies are more open and accountable to their stakeholders, and particularly their workforce. Recent legislation also requires large companies to report on how directors have discharged their duty to consider the above-mentioned stakeholders. None of these developments will authorise directors to prefer the interests of other stakeholders to those of the shareholders; nor will it give other
stakeholders any ability to hold directors legally accountable for their decisions. However, the recent trajectory of enhanced disclosures opens companies up to a new regime of public censure on such matters.

UK law takes a relatively strict approach to the enforcement of directors’ duties. For example, unauthorised self-dealing is not reviewed *ex post* against an entire fairness standard, as it might be in Delaware; rather, the transaction is in principle voidable at the instigation of the company without any inquiry into its fairness. Breach of duty is, in principle, actionable only by the company to which the duty is owed, and not by its shareholders or creditors. While a shareholder may bring a derivative action on behalf of the company in relation to actual or threatened breaches of duty, the UK legal system is not well suited to private enforcement of directors’ duties outside formal insolvency proceedings, so litigation by shareholders of a listed company alleging breach of duty by its directors is extremely rare.

In relation to control-seeking transactions (i.e., any proposed acquisition of 30 per cent or more of the voting rights), the Takeover Code requires shareholder approval for any proposed action by the directors that may result in any offer (or expected offer) for the company being frustrated, or in shareholders being denied the opportunity to accept or reject the offer on its merits. Shareholders are protected by the substantive and procedural rules regulating control transactions.

It would be extremely difficult for the board of a UK company unilaterally to adopt anything equivalent to a shareholder rights plan, or to issue shares to a white-knight bidder to block a hostile takeover. For better or worse, takeover regulation in the UK strongly favours the short-term interests of shareholders by depriving the board of anything other than the power to persuade shareholders to reject an unwanted offer. Changes to the Takeover Code from early 2018 do, however, give the board additional time for such persuasion, and require bidders to provide additional disclosures regarding their intentions for the target business (against which they can be held accountable after the takeover).

Other legislation imposes criminal and civil liability on directors, including health and workplace safety laws, environmental laws and competition and securities laws.

**Appointment, nomination, term of office and succession**

The Code provides that there should be a formal, rigorous and transparent procedure for the appointment of new directors to the board. The search for candidates should be conducted, and appointments made, on merit, against objective criteria and within that context should promote diversity of gender, social and ethnic backgrounds, cognitive and personal strengths. A nomination committee should lead the process for board appointments and make recommendations to the board. Independent directors should be appointed for specified terms subject to annual re-election. The Code prohibits the chairperson from remaining in post beyond nine years from the date of their first joining the board; however, this can be extended for a limited time, where necessary and with explanation, to facilitate effective succession and the development of a diverse board.

The Code states that all directors should be re-elected annually by shareholders. Each director’s election is voted on separately, with statute requiring majority rather than plurality voting (i.e., an ordinary majority of shareholders can vote against – and hence block – a director’s election). In theory, an ordinary majority of shareholders also has a statutory right to remove a director at any time and without cause, but annual re-election renders this right largely irrelevant in practice. Consequently, there is no concept of a staggered board under UK law.
The board should satisfy itself that plans are in place for the orderly succession of appointments to the board and to senior management with a suitably diverse pipeline, so as to maintain an appropriate balance of skills and experience within the company and on the board and to ensure progressive refreshing of the board.

Diversity

The Hampton-Alexander Review (most recently published in 2019) and the Parker Review (most recently published in 2020) have both made a series of recommendations for companies to further gender and ethnic diversity, respectively, at board level.

The Parker Review recommended that all FTSE 100 boards should have at least one non-white director by 2021, and the same for FTSE 250 boards by 2024. The 2016 Hampton-Alexander Review set a target of 33 per cent women on FTSE 350 boards and 33 per cent women in FTSE 100 executive leadership teams by 2020. Both also make a number of recommendations to facilitate attainment of those targets.

Recent additions to the Code seek to reflect these recommendations in asking boards to intensify their efforts. Nomination committees will be required to ensure a diverse pipeline for succession, and annual reports will be required to explain actions taken to increase diversity and inclusion, as well as their outcomes. The Code also recognises a wider concept of diversity, which covers gender, social and ethnic backgrounds, cognitive and personal strengths diversity. The Listing Rules already require that companies’ annual reports include a description of their diversity policy and its objectives, how it is being implemented and the results.

As of November 2019, the number of women on FTSE 100 boards exceeded 32 per cent (up from 12.5 per cent in 2011), but within the FTSE 350 there were still two all-male boards and 42 companies with only one woman on their board, with women still underrepresented in chair and CEO roles. Despite the seemingly modest target, representation of ethnic minorities on FTSE 100 boards actually fell from 9 per cent of boards in 2018 to 7.4 per cent in 2019, and the latest figures in the Parker Review show that 37 per cent of FTSE 100 companies and 69 per cent of FTSE 250 companies do not meet the Parker Review’s targets for ethnic diversity. Improved reporting on board and ethnic diversity was, however, praised by the most recent Parker Review.

III DISCLOSURE

Listed companies are subject to a wide range of periodic, ad hoc and event-driven disclosure obligations, many of which derive from, or have been harmonised under, EU law, and relate to the following key areas:

a financial and operating results of the company, together with certain elements of narrative reporting;
b share capital and voting rights;
c members of the board and key executives;
d directors’ remuneration;
e price-sensitive information (inside information);
f share dealing by insiders and significant shareholders;
g governance structure and policies (comply or explain);
h significant transactions; and
i transactions with related parties.
Companies are required to prepare and publish audited annual financial statements (prepared in accordance with EU-adopted international financial reporting standards) and to make these available to shareholders within four months of the financial year end and in time for the annual general meeting. These form part of the company’s annual report, which must include elements of narrative reporting along with the audited financial statements. The annual report must include a strategic report in addition to the directors’ report, the purpose of which is ‘to inform [shareholders] and help them assess how the directors have performed their duty’ to promote the success of the company. In addition to ‘a balanced and comprehensive analysis of [both] the development and the performance of the [company’s] business during the financial year, and the position of the [company’s] business at the end of that year’, the strategic report must contain a description of the principal risks and uncertainties affecting the company’s business, information about the gender split of its directors, managers and employees, trend information and disclosure about certain environmental matters.

The DTRs require the publication of a half-year report within three months of the end of the relevant six-month period containing a condensed set of (unaudited) financial statements and an interim management report. The interim management report must include details of any important events in the relevant period, the principal risks and uncertainties for the remaining six months and details of related-party transactions.

Companies are required to disclose promptly all dealings in their securities (including non-voting securities) by persons discharging managerial responsibilities (PDMRs) and certain connected persons. Companies are also required to take all reasonable steps to ensure that their PDMRs and persons connected with them comply with the Market Abuse Regulation on dealings in securities. In general, this prohibits all dealings during defined close periods (in the 30 days prior to the publication of certain interim or any annual reports) and at any time when a company is in possession of price-sensitive information, subject to certain exceptions. Even when not absolutely prohibited, dealings by PDMRs and their connected persons above a de minimis threshold must be notified to the company and the FCA.

A person acquiring 3 per cent of the voting rights in a company must notify the company, which is in turn required to make prompt disclosure to the market. Disclosure is also required thereafter whenever that person reaches, exceeds or falls below each additional 1 per cent threshold.

The Listing Rules require significant transactions by a listed company to be disclosed to shareholders. Moreover, Class 1 transactions (i.e., large (measured by reference to profits) assets, gross capital or consideration) require not only disclosure but also shareholder approval by simple majority resolution.

In addition to certain shareholder approval requirements under the Companies Act, the Listing Rules require independent shareholder approval by simple majority resolution for related-party transactions unless they fall within certain exceptions (e.g., small related-party transactions). Related parties include PDMRs and shareholders holding more than 10 per cent of the voting rights, and persons connected with them. The Listing Rules also require a proposal for approval of a related-party transaction to be accompanied by an independent fair and reasonable opinion, typically from an investment bank.

It is worth pausing here to note that the UK is awaiting the implementation of three independent reviews of the audit and financial reporting sector: the Kingman Review of the FRC, the Brydon Review of the quality and effectiveness of audit and the Competition and Markets Authority (CMA) study of the competitiveness and robustness of the statutory audit market. The Kingman Review recommended, among 82 other recommendations, that
the FRC be replaced as soon as possible with a new, independent regulator to be called the Audit, Reporting and Governance Authority. This recommendation was accepted by the government, which announced that the new regulator will be accountable to Parliament and have more extensive powers to better prevent corporate failures. Until the new regulator is in place, the government has begun work with the FRC to implement 48 of the other 82 recommendations. The CMA study has resulted in proposed legislation to separate audit from consulting services and, at the date of writing, both Deloitte and PwC have announced plans to reform their audit services. Lastly, the Brydon Review recommended implementing a new auditing standard, splitting the audit and accountancy professions and enhancing the shareholder role in the audit process. At the time of writing, it was not clear which of the Brydon Review’s recommendations would be implemented.

**IV CORPORATE RESPONSIBILITY**

From an internal company perspective, effective corporate responsibility means high standards of risk management, disclosure and transparency, compliance with best practice and effective monitoring. In the UK, a key principle of the Code requires a board to maintain sound systems for managing risk and internal control. It suggests that the board should review these systems at least annually, and consider how much risk the company can (and should) take. The FRC has published its Guidance on Risk Management, Internal Control and Related Financial and Business Reporting, which aims to:

- **a** bring together elements of best practice for risk management;
- **b** prompt boards to consider how to discharge their responsibilities in relation to the existing and emerging principal risks faced by companies;
- **c** reflect sound business practice, whereby risk management and internal controls are embedded in the business process by which a company pursues its objectives; and
- **d** highlight related reporting responsibilities.

At the same time, the Code was amended to require an explicit statement in the financial statements about whether the going concern basis of accounting has been adopted, and whether there are any material uncertainties about the company’s ability to continue to do so in future. Moreover, companies are also required to include in their annual report a broader statement about the board’s reasonable expectation as to the company’s viability, based on a robust assessment of the company’s principal risks and current position. This information should give investors a clear and broad view of solvency, liquidity, risk management and viability and is expected to be subjected to greater scrutiny by the FRC’s successor. The Investment Association advises that directors should consider, for example, the sustainability of dividends and how risks are prioritised. Auditing standards impose obligations on auditors to review and challenge these statements. It is worth noting that the Kingman Review considered the current approach to viability statements insufficiently effective and, if they cannot be made more effective, proposed giving serious consideration to abolishing them.
V SHAREHOLDERS

i Shareholder rights and powers

Under the Companies Act, shareholders have the power to challenge a board in several ways. As few as 100 shareholders or shareholders holding as little as 5 per cent of the voting rights (whichever is less) can requisition a meeting, and add any item to the agenda or add any item to the agenda for the company’s AGM; moreover, there is no minimum holding period to qualify. In practice, however, boards are relatively responsive to shareholder concerns, and such requisitions are rare because each director must submit to annual re-election, and because directors are in any event required to obtain shareholder approval for a number of matters, requiring relatively frequent engagement with the company’s main shareholders.

Under the Companies Act, shareholders must approve secondary share offerings by simple majority resolution, and in any event, shareholders enjoy statutory pre-emption rights on all secondary share offerings for cash, although they can approve the disapplication of these pre-emption rights by special resolution (i.e., 75 per cent of shares voted). In practice, shareholders typically give directors general authority to issue further shares for cash and on a non-pre-emptive basis within certain guidelines published by institutional investors (e.g., no more than 5 per cent of the company’s share capital in any year, and no more than 7.5 per cent on a rolling three-year basis (or an additional 5 per cent in connection with an acquisition or specified capital investment), and then subject to restrictions on the price at which the shares may be issued). Authority to issue further shares is typically renewed at each AGM or sought in relation to a specific transaction where equity funding is required.

Shareholders are also required to approve the terms of share incentive plans and Class 1 transactions such as major acquisitions or disposals (in each case by simple majority), related-party transactions (by simple majority of independent shareholders), as well as any changes to the company’s constitution or the rights attaching to their shares (by special resolution). Any proposal to acquire control (defined as 30 per cent or more of the voting rights) of a company subject to the Takeover Code requires an offer to be made to all shareholders on the same terms. Finally, shareholder approval (by way of simple majority) is required under the Companies Act for loans and other credit transactions, and for substantial property transactions, with directors and their connected persons (although in practice the provisions of the Listing Rules cover many more such related-party transactions).

When more than 20 per cent of votes have been cast against any board-recommended resolution or any such resolution has been withdrawn, the Code will require companies to announce what actions it intends to take to consult with shareholders in order to understand the reasons behind the result. There is then a requirement for the company to provide an update on the consultation and any remedial actions within six months of the vote, with a final summary included in the annual report. The Investment Association has also launched its Public Register to aggregate publicly available information regarding meetings of any FTSE all-share company following significant shareholder opposition to a proposed resolution.

A general shareholder equality principle pervades both UK company law and the Listing Rules. There is a one share, one vote norm, and distributions to shareholders (dividends, share repurchases, etc.) are required to be made anonymously on market and on tightly regulated terms unless shareholders waive these requirements. In principle, information must be made available simultaneously to all shareholders, although in practice it is possible to inform key shareholders of significant proposals in order to take soundings on a confidential basis, although this precludes shareholders from dealing in a company’s securities until the information has been made public or ceases to be price-sensitive.

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Shareholders’ duties and responsibilities

English law imposes little in the way of active duties or liabilities on shareholders. A majority shareholder does not owe any fiduciary duty to the company or to the other shareholders and is free to exercise its voting rights to advance its own interests, except where it is barred from doing so because of its interest in a proposed transaction or where, in relation to a proposed change to the company’s constitution, it is not voting bona fide in the interests of the company.

Certain non-binding expectations are placed on investors by institutional guidelines, the Code and the Stewardship Code. The Stewardship Code recognises the importance of environmental, social and governance factors to investors and the role that asset managers have to play in ensuring market integrity, minimising systematic risks and being stewards of the investments in their portfolios. Signatories must report annually on their stewardship activities and outcomes in a stewardship report. Large investors such as BlackRock and State Street are vocally increasing their engagement with portfolio companies on their environmental, social and governance (ESG) criteria, recognising the growing responsibilities of asset managers to foster long-term value, and the need for companies to develop their purpose and focus on creating stakeholder value. By way of example, TCI, one of the UK’s largest long-only hedge funds and activist shareholders, has recently stated that it will sell down its stakes in companies that do not have, and report against, a plan to reduce their carbon emissions. This is in line with a wider trend of expectations of enhanced ESG reporting by companies against often overlapping legal and voluntary reporting criteria.

The Listing Rules contain the concept of a controlling shareholder, who (either alone or together with others acting in concert with it) is able to control 30 per cent or more of the voting rights. Affected companies must enter into a relationship agreement with their controlling shareholder containing certain mandatory terms intended to ensure that the board will remain independent of improper influence by the controlling shareholder. Companies with a controlling shareholder are also subject to additional disclosure requirements, and certain matters require the approval of shareholders independent of the controlling shareholder.

Shareholder activism

While institutional investors have traditionally been reluctant to police the corporate governance regime, an increasing number have recently become more vocal. Where institutional investors do have criticisms, they are more likely to engage in private dialogue with the directors. In recent years, however, they have been increasingly involved in activist campaigns, alongside traditional activists such as hedge funds. What distinguishes shareholder activists is that they are prepared to air issues publicly to achieve change. Much activism is still concerned with securing board representation, encouraging M&A activity or building stakes; however, executive remuneration and perceived corporate governance failings are also increasingly focuses. Related-party arrangements, the independence of directors, failures to address shareholder concerns and overly generous bonus or exit remuneration packages have also been addressed by activists in recent years. ESG factors are increasingly a source of shareholder activism too. Partly in response to TCI’s letters, companies including Charter Communications, Airbus and Moody’s have vowed to improve their environmental disclosures. In the context of stranded assets, this is evidently shareholder activism targeted at preserving long-term shareholder value.
iv  Contact with shareholders

A company’s relations with its shareholders are also specifically addressed in the Code. Regular engagement with major shareholders in order to understand their views on governance and performance against strategy is encouraged. The Code also requires the chairperson to ensure that the board as a whole has a clear understanding of the views of shareholders. The board should keep in touch with shareholder opinion in whatever ways are most practical and efficient, using the AGM to communicate with investors and encourage their participation alongside more informal consultation throughout the year.

VI  OUTLOOK

The FRC set quite a chilling context for its most recent corporate governance review: ‘a continuing lack of trust in business, high-profile corporate failures, lingering concerns that companies gave little thought to long-term sustainability; and, more generally, the impact of companies on wider society’.

Against this background, businesses in the UK remain under pressure to actively demonstrate their social and environmental licence to operate. Political and media scrutiny remains intense, and the trajectory of enhanced disclosures suggests that these democratic pillars, coupled with enhanced shareholder engagement, will continue to police corporate and executive behaviour. It is no wonder that directors feel under siege as the mismatch between legal duties and social expectations continues.

The world is finally waking up to the threat that catastrophic climate change poses, and the shift in governance and business responses will be decisive. We expect a consolidation in the number of competing ESG reporting regimes to assist with this. Other themes to watch in the year ahead include the replacement of the FRC and any indications of corporate governance changes as the UK prepares for its exit from the EU.
Chapter 25

DELAWARE

Ellisa O Habbart

I \hspace{1em} OVERVIEW OF GOVERNANCE REGIME

i Sources of Delaware law

The position of Delaware law is illustrated by the fact that more than half of US public companies (including more than 66 per cent of the Fortune 500) are incorporated in the state. Delaware’s corporate governance regime draws from two bodies of law. The first is the General Corporation Law of the State of Delaware (DGCL), a statutory framework adopted by the Delaware legislature in 1899, substantially revised in 1967 and regularly amended to date. Updates and revisions are made each year by the Delaware legislature based on the recommendations of the Council of the Corporation Law Section of the Delaware State Bar Association. As a result, the DGCL is constantly under review by the most knowledgeable members of the Delaware Bar.

Judicial decisions comprise the second source of corporate governance law in Delaware. The state’s Court of Chancery (Chancery Court) is largely regarded as the nation’s premier business court. The Chancery Court is a court of equity, which consists of five expert judges chosen to adjudicate corporate and commercial disputes. Appeals from the Chancery Court are heard by the Delaware Supreme Court.

ii Enforcement of Delaware’s corporate governance regime

Derivative, direct, and class actions each provide a method for shareholders to seek redress against corporations and their directors and officers for alleged wrongdoing. Class actions are essentially an aggregation of direct claims being prosecuted by one or more persons as representatives of a group of shareholders. Direct claims involve an injury to the suing shareholder individually, as opposed to the corporation. Where there is an actual injury to the corporation to which any relief would flow, the cause of action must be brought by the corporation or by the shareholders derivatively if the corporation fails to act. In practice, the classification of a particular claim as derivative or direct may be challenging.

The classification of a claim is significant because a shareholder plaintiff may not proceed against a corporation with a derivative claim without first making a demand on the corporation to pursue the claim itself, unless the making of a demand would be futile. The Chancery Court will excuse the failure to make a demand based on futility if the complaint creates a reasonable doubt that the corporation’s directors are disinterested and independent or the challenged action was otherwise the product of valid business judgement.2 Under the first prong of the

1 Ellisa O Habbart is a partner at The Delaware Counsel Group LLC. This information is accurate as at March 2019.

well-known Aronson test, a director is interested if he or she sits on both sides of a transaction or derives a benefit from a transaction that is not shared by the corporation or all shareholders generally. Independence is lacking if the director’s decision is based on extraneous influences rather than the merits. When addressing Aronson’s second prong, the plaintiff must create a reasonable doubt that either the action was taken honestly and in good faith, or the board was adequately informed in making the decision. Demand also may be excused under the second prong of Aronson if a plaintiff properly pleads a waste claim.3

iii Nature of the corporate governance regime and recent developments

Delaware’s corporate governance regime is founded on the fundamental principle set forth in Section 141(a) of the DGCL that, unless otherwise provided in a corporation’s certificate of incorporation, the business and affairs of a corporation must be managed by or under the direction of its board of directors. Delaware decisional law reflects a constant tension between directors and shareholders over the shareholders’ desire to exert influence over corporate management and potentially usurp the board’s decision-making authority. Aside from the corporate electoral process and the reservation of the shareholders’ right to vote on various fundamental corporate actions,4 the board’s power is limited only by certain well established fiduciary obligations.

Notably, in 2016, the Delaware Supreme Court determined that the statutory basis for finding jurisdiction over Delaware directors and officers was more expansive than it has been interpreted to be by Delaware courts for over 30 years.5 Now, non-resident officers and directors of Delaware corporations are deemed to have consented to personal jurisdiction not only in any action against that director or officer for violation of a duty in that capacity, but also in all civil actions brought in Delaware by, on behalf of or against a Delaware corporation, in which the director or officer is a necessary or proper party.

II CORPORATE LEADERSHIP

i Board structure and practices

The board of directors must consist of at least one member, and all members must be natural persons.

Term of office

Under Section 141(b) of the DGCL, each director holds office until the director’s successor is elected and qualified, or until the director’s earlier resignation or removal. Typically, the term of each director is one year unless the board has been structured as classified. Pursuant to Section 141(d) of the DGCL, the certificate of incorporation, the initial by-laws of the company or a by-law adopted by the shareholders may divide the board into a maximum of three classes of directors who serve staggered terms. If three classes of directors are created, then only one class of directors stands for election each year.

3 See footnote 7.
4 These matters include amendments to the certificate of incorporation, certain mergers, sales of substantially all or all of the corporation’s assets and dissolution.
5 Hazout v. Tsang Mun Ting, 134 A.3d 274 (Del. 2016).
Qualifications

The DGCL does not specify any qualifications for directors other than that they be natural persons. However, pursuant to Section 141(b) of the DGCL and the common law, the certificate of incorporation and by-laws may prescribe reasonable director qualifications. The Delaware courts are likely to enforce qualifications that are reasonably related to the corporation’s business. Valid qualifications might include a minimum ownership requirement or experience in a certain field of business.

Board action

Directors act collectively, and all directors possess equivalent voting rights unless the certificate of incorporation otherwise provides. Any action may be taken by vote of a majority of the directors present at a meeting at which a quorum is present unless the certificate of incorporation or by-laws provide for a supermajority vote. Unless directors are restricted by the certificate of incorporation or by-laws, directors may act without a meeting by unanimous written or electronic consent, including email transmissions.

Committees

Certain managerial duties may be delegated by the board of directors to committees of the board consisting of one or more directors. Generally, a properly constituted board committee may exercise the full powers of the board of directors in the management of the business and affairs of the corporation with two significant exceptions:

a) a board committee cannot approve, adopt or recommend to shareholders any action or matter expressly required by the DGCL to be submitted to shareholders for a vote (other than the election or removal of directors); and
b) a board committee cannot adopt, amend or repeal any by-law.

Advisory committees of the corporation may include members who are not directors, but any such committee’s function must be purely advisory in nature.

Officers

Corporations must have such officers as established by the by-laws or by resolution of the board of directors. A court will generally uphold a delegation of authority to officers by a corporation’s board of directors unless the delegation is of a task specifically assigned by the DGCL to the board. However, if the delegation conflicts with some overriding public policy or provision of a corporation’s certificate of incorporation, it will not be upheld. Unauthorised acts of officers may be validated by ratification by the board of directors unless the acts are beyond the authority of the corporation.

Compensation

The board of directors may fix director compensation in the absence of restrictions in the certificate of incorporation or by-laws. The directors’ self-interested decision will be entitled to the protection afforded by the business judgement rule if the compensation plan has been approved by the corporation’s shareholders and contains well-defined, specific limits on potential self-dealing. Otherwise, if challenged, the board will have to show that the compensation arrangements are fair to the corporation by demonstrating that services of value are actually being rendered, and that the level of compensation for these services is similar.
to either industry standards or compensation at corporations of similar size and profitability. Shareholders’ approval may not guarantee judicial deference to business judgement when the shareholders only approve an upper limit and the directors are given discretion to determine compensation up to that limit.\textsuperscript{6} The board should also approve the compensation of executive officers of the corporation. As a matter of customary practice, most corporations delegate the responsibility for fixing executive compensation to outside directors. At a minimum, directors do not participate in the discussion of, or vote upon, their own compensation as officers or employees to minimise the appearance of self-dealing. Executive compensation decisions made by disinterested directors are generally upheld in the absence of waste.\textsuperscript{7}

**Takeover practice**

The responsibility for responding to takeovers is generally held to reside with the board of directors pursuant to the managerial authority provided in Section 141(a) of the DGCL. The board of directors has a fiduciary responsibility to advance the best interests of the corporation’s shareholders in responding to takeovers.

\section*{ii Directors}

**Fiduciary duties**

All directors of a Delaware corporation owe fiduciary duties of care and loyalty to the corporation and its shareholders. The courts have also recognised that directors have fiduciary duties of disclosure and good faith, which are not separate duties, but rather specific applications of the fiduciary duties of care and loyalty. These duties are owed by all directors to the corporation and shareholder body as a whole without regard to whether any director is an inside or outside director or was elected by a particular class of shareholders.

**Duty of care**

The duty of care requires that directors inform themselves using all material information reasonably available to them before making a business decision. This duty extends to the board’s delegation functions. However, directors are not expected to oversee every detail of day-to-day corporate activities, and may rely in good faith upon the records of the corporation and upon information, reports, opinions and statements of corporate officers and employees.

**Duty of loyalty**

Directors also owe a duty of loyalty to the corporation. The duty of loyalty mandates that a director cannot consider or represent interests other than the best interests of the corporation and its shareholders in making a business decision. Where a director has an interest in a decision that is different from or in addition to the interests of the corporation

\textsuperscript{6} *In re Investors Bancorp, Inc Stockholder Litig*, 177 A.3d 1208, 1211 (Del. 2017) (’When stockholders have approved an equity incentive plan that gives the directors discretion to grant themselves awards within general parameters, and a stockholder properly alleges that the directors inequitably exercised that discretion, then the ratification defence is unavailable to dismiss the suit, and the directors will be required to prove the fairness of the awards to the corporation.’)

\textsuperscript{7} See *Calma on Behalf of Citrix Systems, Inc v. Templeton*, 114 A.3d 563, 590 (Del. Ch. 2015) (’To state a claim for waste, it must be reasonably conceivable that the directors authorize[d] an exchange that [was] so one sided that no business person of ordinary, sound judgement could conclude that the corporation has received adequate consideration.’) (internal quotations and citations omitted).
and shareholders generally, the director is said to be an interested director. Interested directors should disclose the interest to the other members of the board and, if the interest is material, consider abstaining from any board vote on the matter.

The duty of loyalty also encompasses cases where the director fails to act in good faith.\(^8\) Bad faith may be shown where the director's conduct is motivated by an actual intent to do harm, or where the director intentionally acts with a purpose other than that of advancing the best interests of the corporation or with the intent to violate applicable law. Bad faith is also demonstrated where the director intentionally fails to act in the face of a known duty to act, thereby demonstrating a conscious disregard for his or her duties.

**Liability of directors**

Directors may be found to be personally liable for monetary damages if they breach their fiduciary duties of loyalty and care. Directors may be exculpated from paying monetary damages for liability arising from breach of the fiduciary duty of care if the corporation's certificate of incorporation contains an exculpatory provision authorised by Section 102(b)(7) of the DGCL. Whether a director will be found liable for breach of fiduciary duty depends largely on the standard of review applicable to the challenged action or decision of the director. However, the Delaware Supreme Court recently clarified that regardless of what standard of review applies, a plaintiff seeking only monetary damages against a director protected by an exculpatory provision must plead claims for breach of the duty of loyalty to survive a motion to dismiss.\(^9\)

**Standards of review**

Delaware has three standards of review for evaluating director decision-making: the business judgement rule, entire fairness and intermediate scrutiny.

**The business judgement rule**

The business judgement rule is the default standard of review. In general, the business judgement rule is a presumption that, in making a business decision on behalf of the corporation, the directors acted on an informed basis, in good faith and in the honest belief that the action taken was in the best interests of the company.\(^10\) When a court finds that the business judgement rule applies, the business decisions of disinterested directors will not be disturbed if they can be attributed to any rational business purpose.

**Entire fairness**

If the business judgement rule's presumption is rebutted, the burden generally shifts to the defendant directors to show the entire fairness of the transaction. The entire fairness standard is the most exacting standard of review applied by Delaware courts when reviewing a challenged transaction and has two elements: fair price and fair dealing.\(^11\) Fair price relates

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\(^8\) *Stone v. Ritter*, 911 A.2d 362, 370 (Del. 2006).

\(^9\) See *In re Cornerstone Therapeutics Inc. Stockholder Litig*, 115 A.3d 1173 (Del. 2015).


to the economic and financial considerations of a transaction. Fair dealing requires a review of when the transaction was timed, how it was initiated, structured, negotiated and disclosed to the directors, and how the approvals of the directors and the shareholders were obtained.

**Intermediate scrutiny**

**Unocal**

A Delaware court will apply an intermediate level of scrutiny in reviewing a board’s responses to takeovers that are defensive in nature under the Unocal enhanced scrutiny test. If this test applies, directors must show that they had 'reasonable grounds for believing that a danger to corporate policy and effectiveness existed' and that their action was 'reasonable in relation to the threat posed'. If the defensive action was neither preclusive nor coercive, the court will determine whether the directors have met their burden of showing that the response was within a range of reasonableness considering the threat posed.

**Revlon**

Intermediate scrutiny will also be applied to review a board’s actions in the context of transactions involving a change in control or a break-up of the corporation under Revlon. To meet this standard, the directors must focus on one primary objective – to secure the best value reasonably available for the shareholders. The Delaware courts have recognised that there is no single blueprint to follow in reaching the ultimate goal of maximising shareholder value. Thus, under Revlon, directors are generally free to select the path to value maximisation so long as they choose a reasonable route. For example, in C&J Energy Services, Inc. v. City of Miami General Employees, the Delaware Supreme Court reversed a Chancery Court decision that held that a board must conduct a pre-signing active solicitation process to satisfy its duties under Revlon. The Court found that so long as any bidder interested in paying more for the target company had a reasonable opportunity to do so, the company was not required to actively shop itself.

**Procedural protections may modify the standard of review**

In certain situations, the use of specific procedural protections will warrant the application of a more deferential standard of review. For example, transactions involving a conflicted controlling shareholder are generally subject to entire fairness. However, the business judgement standard of review will apply to such a transaction if, and only if, the transaction is conditioned on the approval of both an independent special committee of the board and a minority shareholder vote, and:

- the special committee is empowered to freely select its own advisers and to say no definitively;
- the special committee meets its duty of care in negotiating a fair price;
- the vote of the minority is informed; and

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13 *id* at 954.
14 *id* at 955.
16 107 A.3d 1049, 1067-69 (Del. 2014).
17 *id* at 1069.

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there is no coercion of the minority.18

Additionally, the business judgement standard of review will irrebuttably apply to a post-closing challenge of a transaction generally subject to enhanced scrutiny if a majority of disinterested, uncoerced and fully informed shareholders approved the transaction.19 Similarly, a transaction that involves a conflicted board of directors that would generally be subject to entire fairness will be subject to the irrebuttable application of the business judgement standard of review if a majority of disinterested, uncoerced and fully informed shareholders approved the transaction.20 If the challenged transaction involves a conflicted controlling shareholder, however, the shareholder vote will not result in the irrebuttable application of the business judgement standard of review.21 In transactions involving a conflicted controlling shareholder, the shareholder vote will merely shift the burden of persuasion from the controlling shareholder to the minority shareholders.22

**Indemnification**

Under Section 145 of the DGCL, a director may be indemnified for expenses incurred in defending derivative claims, and for expenses, judgements, fines and amounts paid in settlement incurred in connection with defending direct actions. However, if the director has been successful on the merits or otherwise in the defence of the proceeding, he or she is entitled to mandatory indemnification for expenses actually and reasonably incurred. To be indemnified in criminal actions or proceedings, the director must also have had no reason to believe that the challenged conduct was unlawful. Advancement of expenses to a director prior to the final disposition is also permitted if the director executes an undertaking to repay the monies advanced if it is ultimately determined that he or she is not entitled to indemnification. These rights cannot be eliminated by a corporation after a director’s period of service ends unless the individual knows at the time he or she chooses to serve that his or her rights will terminate or can be eliminated at a later time.23 Notably, indemnification and advancement rights apply only where the director has been sued ‘by reason of the fact’ that the director is or was a director of the corporation.24 This standard cannot be modified by contract.25

**Election of directors**

An annual meeting of shareholders of a Delaware corporation is mandated to elect directors. To permit an orderly period of solicitation of shareholder nominations prior to a meeting, many corporations have adopted provisions in their certificates of incorporation or by-laws

21 id. at *9.
22 id.
25 id.
to provide for advance notice of the nomination of directors by shareholders. Such provisions typically require that the shareholder making the nomination be a shareholder of record. The nominating shareholder must also submit specific information within a specified window to the corporation about himself or herself; the beneficial owner, if any, on whose behalf the nomination is being made; and about each of his or her director nominees. The information required typically includes all information about the nominee that would be required to be disclosed under federal securities laws and whether the nominating shareholder or the beneficial owner, if any, intends to solicit proxies from other shareholders. By-law provisions requiring advance notice of nominations have been found inequitable in specific factual circumstances.26

III DISCLOSURE

Under Delaware law, obligations relating to corporate disclosure are derived from common law fiduciary duties, not the DGCL. The duty of disclosure is a component of a director’s fiduciary duties of care and loyalty, and its scope and requirements depend on context. Corporate fiduciaries can breach their duty of disclosure by making a materially false statement, by omitting a material fact or by making a partial disclosure that is materially misleading. The duty of disclosure applies in a number of situations, including when directors seek shareholder action such as the ratification of director compensation.27

IV CORPORATE RESPONSIBILITY

In contrast to US federal law, Delaware does not have a statutory regime addressing risk management, compliance policies, whistle-blowing or other issues of corporate responsibility. Rather, Delaware relies on fiduciary duty law to encourage and enforce ethical behaviour by directors and officers of Delaware corporations.

A claim of breach of fiduciary duty that seeks to hold directors of a Delaware corporation liable for either knowingly causing the corporation to violate the law or for failing to establish an effective system for monitoring the corporation’s compliance with the law is rarely successful.28 Plaintiffs are faced with the difficult burden of establishing the necessary linkage between illegal conduct and a conscious board decision. If plaintiffs cannot point to a particular board decision demonstrating the board’s conscious decision to violate the law, the plaintiff must plead that the board deliberately failed to act after learning about incidents or occasions of possible illegality. Alternatively, plaintiffs could establish that the illegality occurred because the board abrogated its oversight function by failing to ensure that the corporation possessed an adequate compliance system. For example, a plaintiff might be successful if the board did not form an audit or other compliance committee.

Section 204 and Section 205 of the DGCL, which were adopted in 2014 and amended in 2015, act as powerful tools for current boards of Delaware corporations. These provisions grant

26 See, e.g., JANA Master Fund, Ltd v. CNET Networks, Inc, 954 A.2d 335 (Del. Ch. 2008).
27 The failure to disclose material information in this context will negate any effect a shareholder vote otherwise might have on the validity of the transaction or the applicable standard of review.
28 This type of claim is known colloquially as a Caremark claim, after the seminal decision by the Chancery Court in In re Caremark International Inc. See In re Caremark Intl Inc Derivative Litig, 698 A.2d 959 (Del. Ch. 1996).
boards the power to ratify, and the Chancery Court authority to validate, defective corporate acts that failed to comply with the DGCL or the corporation’s organisational documents. The Section 204 ratification procedure involves adopting resolutions, obtaining shareholder approval if such approval is legally required, and filing a certificate of validation in accordance with Section 103 of the DGCL. Under Section 205, the Chancery Court can determine the validity of any defective corporate act that has not been ratified or has been ratified effectively under Section 204, regardless of whether the defective corporate act would have been capable of ratification pursuant to Section 204.

V SHAREHOLDERS

i Shareholder rights and powers

Equality of voting rights

Unless otherwise provided in the certificate of incorporation, shareholders are entitled to one vote for each share of capital stock held by the shareholders pursuant to Section 212 of the DGCL. A common type of variation from the one vote per share rule is the creation of preferred stock with contingent voting rights. Generally, all holders of the same class or series of stock must have equivalent voting, dividend and other rights under the common law doctrine of equal treatment. However, the Chancery Court has upheld scaled and tenured voting patterns where specifically authorised by the certificate of incorporation, as well as other types of discrimination among holders of the same class or series of stock where the discrimination was not inequitable.29

Shareholders’ ability to influence the board

Generally, the shareholders’ ability to influence the board is limited to the power to elect and remove directors, with or without cause,30 and to approve or disapprove certain actions as required by the DGCL or as may be provided in the corporation’s certificate of incorporation. Shareholders may also exercise influence by dissolving the corporation without board approval if the written consent of all shareholders is obtained. A shareholder who owns 90 per cent or more of the outstanding shares of each class of capital stock of a Delaware corporation may force a short-form merger of the corporation without board or other shareholder approval under Section 253 of the DGCL. The only other significant power that shareholders may exercise without prior board action is the amendment of the corporation’s by-laws pursuant to Section 109 of the DGCL. The board may be given concurrent power to amend the by-laws in the corporation’s certificate of incorporation, and the certificate of incorporation or by-laws may impose supermajority voting requirements for shareholder amendments to the by-laws. However, in no case may the ability of the shareholders to amend the by-laws be completely eliminated.

30 Unless the corporation’s certificate of incorporation otherwise provides, in the case of a corporation whose board is classified, shareholders may effect such a removal only for cause.
Rights of dissenting shareholders

Aside from the right to an appraisal of the fair value of their shares by the Chancery Court in connection with certain types of mergers, shareholders do not enjoy dissenters’ rights under the DGCL. Generally, appraisal rights are triggered in connection with the merger of a listed company incorporated in Delaware if the shareholders of the corporation are required to accept in the merger consideration other than stock in the surviving corporation or publicly traded stock in another corporation. If the Chancery Court finds that the fair value of the shares is higher than the merger consideration and the petitioning shareholders have properly asserted their appraisal rights, then the shareholders are entitled to receive the difference between the merger price and the price determined by the Chancery Court to constitute fair value, plus interest.

In the past, Delaware courts have generally adopted the merger consideration as the best evidence of fair value of an entity’s shares. However, in the Chancery Court’s 2016 In re Appraisal of Dell Inc decision, appraisal petitioners of Dell Inc were awarded fair value for their shares that was significantly higher than the merger consideration paid to the other public shareholders in the merger. This rare decision can most likely be attributed to the unique set of facts presented to the court, which included:

a. the transaction at issue was a management buyout;
b. extensive and compelling evidence of a ‘valuation gap between the market’s perception and the target company’s operative reality’;
c. limited pre-signing competition for the target company;
d. the only active bidders were financial, rather than strategic, buyers; and
e. the special committee that negotiated the deal did not consider fair value – instead, it focused on the market price of the company’s common stock, and ‘negotiated without determining the value of its best alternative to a negotiated acquisition’.

Nevertheless, this decision makes clear that Delaware courts have broad discretion to determine share value based on the facts and circumstances of each individual appraisal action before deferring to the merger consideration as the best evidence of fair value. Consistent with earlier decisions, the Delaware Supreme Court reversed the Court of Chancery decision given, according to the Supreme Court, the Court of Chancery’s reasons for ignoring the deal price did not agree with the Supreme Court’s findings. As a result, but for situations where there is significant evidence to support a finding to the effect that there were defects in the market that justify a departure from deal price, it is still very relevant.

Shareholders’ duties and responsibilities

A controlling shareholder owes fiduciary duties to the shareholders of the corporation he or she controls. A controlling shareholder may not exercise control over the management and affairs of the corporation to his or her benefit and to the detriment of the corporation and the minority shareholders. Indeed, whenever a corporation enters into a transaction with, or at the behest of, its controlling shareholder, the applicable standard of review is normally entire fairness,

32 Delaware does not impose fiduciary duties or other obligations upon shareholders who are not controlling shareholders. A controlling shareholder may possess less than a majority of the corporation’s outstanding voting power and still be considered a controlling shareholder if the shareholder exercises actual domination and control of the corporation.
placing the burden of proof on the defendant to demonstrate the fair value and process of the transaction. This burden of proof is shifted to the plaintiffs if the controlling shareholder transaction is approved either by an independent and well-functioning special committee or by a majority of the minority shareholders.

iii Shareholder activism

Shareholder activism has increased significantly over the past decade, and Delaware has not been immune to its expanding influence. A Delaware corporation will often regulate shareholder activism by including defensive provisions in its certificate of incorporation and by-laws. These include advance notice by-laws, staggered board provisions, supermajority requirements for by-law amendments, and prohibitions on the shareholders’ ability to act by written consent and to fill vacancies on the board. These defences, often used in combination, allow corporations to effectively prevent or defeat hostile tender offers.

iv Takeover defences

See Section V.iii.

v Contact with shareholders

Communications between the board and the shareholders mainly occur in connection with the solicitation of the shareholders’ vote on matters in which the shareholders are required to act. Under Delaware law, when directors communicate with shareholders outside the context of seeking shareholder action, the directors’ fiduciary duty of disclosure still applies but on a more limited basis. In such circumstances, the directors must communicate with honesty. For example, if a director speaks through public statements made to the market, statements informing shareholders about the affairs of the corporation, or public filings required by the federal securities laws, he or she must not knowingly disseminate false information that results in injury to a shareholder.

VI OUTLOOK

The ongoing and active involvement of the members of the Delaware Bar in maintaining and recommending amendments to the DGCL, as well as the quality of Delaware’s courts and Office of the Secretary of State, are likely to ensure that Delaware remains the jurisdiction of choice for incorporation and adjudication of business disputes in the United States.

34 id.
36 In some cases, a board will employ a white-knight defence, which entails management of the target company recruiting a rival bidder that will save them from an initial, unfriendly offer or by offering a more attractive deal.
37 In re Wayport, Inc Litig, 76 A.3d 296, 315 (Del. Ch. 2013) (quotations and citations omitted).
I OVERVIEW OF GOVERNANCE REGIME

The sources of corporate governance law and regulation in the United States are varied and interrelated. There are four key sources: state corporate law (predominantly Delaware, in which over half of all US publicly traded corporations are incorporated); the federal 1933 Securities Act and 1934 Securities Exchange Act, and the regulations of the Securities and Exchange Commission (SEC) under those Acts; stock exchange listing rules (predominantly the New York Stock Exchange (NYSE) and the NASDAQ); and federal statutes in regard to particular areas of corporate practice (e.g., regulations promulgated by the Federal Reserve and other federal and state agencies with respect to banks and other financial institutions, and by other similar regulatory bodies in respect of communications, transportation and other regulated fields). Because of the federal system of US law, different sources of law are not always harmonised, and corporations are often subject to different obligations to federal and state governments, regulators at each level of government and demands of other relevant bodies, such as the applicable stock exchange. This mosaic of rules and regulations, and the mechanisms by which they are implemented and enforced, make for an environment of frequent change and evolution.

Securities laws and regulations are civilly enforced by the SEC, and the SEC must also grant clearance to certain important corporate disclosure documents (such as proxy statements and certain securities registration statements). Larger and older corporations with a history of securities law compliance are subject to fewer such pre-clearance requirements and may in certain cases file abbreviated forms of disclosure. Private investors may also bring actions under many provisions of the securities laws to recover damages for misstatements or omissions in public statements and in certain other circumstances. The Department of Justice prosecutes criminal violations of federal securities laws and SEC rules.

State law fiduciary duties of directors and officers are predominantly enforced by private actions led by plaintiffs’ lawyers. These private actions generally fall into one of two categories: class-action suits on behalf of a particular group of the corporation’s shareholders (typically all shareholders who bought or sold during a particular period or all unaffiliated shareholders), and derivative suits purportedly on behalf of the corporation itself. Putative class-action suits must satisfy the criteria under the Federal Rules of Civil Procedure or analogous provisions of state law before being permitted to proceed as a class action, including the numerosness of the class members, the commonality of legal and factual issues among members of the

1 Adam O Emmerich, William Savitt and Sebastian V Niles are partners and Kathleen Iannone Tatum is an associate at Wachtell, Lipton, Rosen & Katz.
class, the typicality of the claims or defences of the representative parties to the class and the
fairness and adequacy of the representative parties’ protection of the class interests. Derivative
suits, creatures of state corporate law, provide a mechanism by which shareholder plaintiffs
can in theory represent the corporation in suing the corporation’s own board of directors or
management, sometimes after complying with a ‘demand’ procedure in which the plaintiff
must request that the corporation file suit and be rebuffed. In certain circumstances, especially
when it can be shown that the board of directors is for some reason conflicted with respect to
the alleged breach of duty, this demand requirement is excused and the shareholder will be
permitted to pursue a claim in the corporation’s name without further enquiry.

The two primary US stock exchanges, the NYSE and the NASDAQ, each make rules
with which corporations must comply as a condition to being listed on these exchanges. These
listing rules address all aspects of corporate governance, including topics such as director
independence, the composition of various board committees, requirements to submit certain
matters to a vote of shareholders, regulation of dual-class stock structures and other special
voting rights, publication of and topics covered by corporate governance guidelines, and
even requirements related to the corporation’s public website. These rules are enforced by the
threat of public reprimand from the exchanges, temporary suspension of trading for repeat
offences and permanent delisting for perennially or egregiously non-compliant companies.

In addition, of increasing importance to the US corporate governance regime are the
proxy advisory firms (predominantly Institutional Shareholder Services (ISS) and, with lower
market share, Glass, Lewis & Co (Glass Lewis)) and the influence those proxy advisers have
on the institutional investor community, and the related prevailing and evolving views of
the institutional investor community. That community’s views have become particularly
influential as the shareholder base of the vast majority of US publicly traded corporations
consists of an overwhelming majority of institutional shareholders, including index funds,
pension funds and mutual funds. As a result, major institutional investors are increasingly
developing their own independent views on preferred governance practices.

While proxy advisory firms are not a source of law, their guidelines figure significantly
in the corporate governance landscape. These advisory firms exert pressure on corporations
to conform to governance standards they promulgate by issuing director election voting
recommendations to each publicly traded corporation’s shareholders based on the
corporation’s compliance with the advisory firm’s published standards. Perhaps because of
the problem of rational apathy – that is, because an individual shareholder bears all of the
costs of becoming an informed voter but shares the benefits with all other shareholders,
shareholders have little incentive to inform themselves – proxy advisory firms wield outsized
influence on corporate elections, especially among institutional investors such as pension
funds.2 One study found that a recommendation from ISS to withhold a favourable vote in
an uncontested director election correlates with a 20.9 per cent decline in favourable voting.3
In addition, a 2013 study sponsored by Stanford University found that companies were
altering their compensation programmes to comply with proxy advisory firms’ ever-evolving

2 See Michael J Segal, Trevor S Norwitz and Sebastian V Niles, ‘SEC Commissioner Critiques Reliance on
Proxy Advisory Firms’, Bank and Corporate Governance Law Reporter, Volume 51, Number 1 (2013).
3 Stephen Choi, Jill Fisch and Marcel Kahan, ‘The Power of Proxy Advisors: Myth or Reality?’, Emory Law
policies. The US Congress, the US Department of Labor and the SEC have raised questions regarding fiduciary responsibility in the context of the outsourcing of proxy voting decisions to proxy advisory firms. In 2019, the SEC announced proposed rules designed to enhance the accuracy and transparency of proxy voting advice provided by proxy advisory firms to investors, including increasing disclosure around material conflicts of interest in proxy voting advice, providing an opportunity for a period of review and feedback through which companies and other soliciting parties would be able to identify errors in the proxy voting advice and codifying that proxy advisor vote recommendations are considered proxy solicitations and are therefore subject to the anti-fraud provisions of Rule 14a-9 prohibiting any materially false or misleading statement. Significantly, certain major institutional investors, such as BlackRock Inc (which invests over US$6.9 trillion in client assets) and the Vanguard Group (which invests over US$4.5 trillion in client assets) have stated that they reach proxy voting decisions on the basis of their own internally developed guidelines, independent of proxy advisory firms, and have sought to engage directly and pragmatically with companies. These major institutions are uniquely positioned to use their influence to recalibrate the system to reduce reliance on proxy advisory firms.

The Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act), signed into law in July 2010, was passed in response to corporate governance practices perceived by some to have contributed to the 2008–2010 economic crisis. The Dodd-Frank Act requires additional disclosure in corporate proxies and non-binding shareholder votes on various questions of corporate governance (notably, related to executive compensation), and contemplates greater access for shareholder-proposed director nominees to the company proxy. More recently, in response to increasing company compliance costs, in 2018, the SEC adopted rule amendments to streamline disclosure requirements and reduce duplicative or overlapping disclosure obligations. In 2019, in furtherance of its aim to make SEC disclosure documents more relevant to investors while reducing the burden on issuers, the SEC proposed a set of amendments to the period disclosure requirements relating to a company’s business, legal proceedings and risk factors, which would eliminate certain prescriptive requirements in favour of flexible, principles-based guidelines and permit increased use of summaries, cross-references and hyperlinks in order to reduce repetition.

II CORPORATE LEADERSHIP

Under Delaware law, ‘The business and affairs of every corporation . . . shall be managed by or under the direction of a board of directors’. The corporation law of all other US states similarly assigns corporate managerial power to the board of directors.

i Board structure and practices

Boards of directors customarily organise committees to carry out specific functions without the presence of the entire board. State law generally permits most of the functions of the board of directors to be delegated to committees, and generally permits directors to rely on

5 Delaware General Corporation Law, Section 141(a).
6 See, e.g., Delaware General Corporation Law, Section 141(c)(2).
information, opinions, reports or statements presented to the board by its committees. 7 Boards are specifically required by federal securities law to have an audit committee with certain prescribed functions relating to the retention, compensation and oversight of the company’s independent auditor. Federal securities law and NYSE and NASDAQ listing rules also require listed companies to maintain compensation and nominating or corporate governance committees. Boards will often voluntarily establish additional committees: for example, a company in the technology sector might establish a technology committee comprising directors with the most applicable expertise to stay abreast of technological developments, and a company that has important relationships with labour unions might choose to establish a labour relations committee. By custom, many companies have established a risk committee (actually required of certain financial institutions by the Dodd-Frank Act), an executive committee, a finance committee, a public policy committee, or some subset thereof. Boards may also establish ad hoc committees in response to discrete or emergent developments.

A panoply of regulations and disclosure requirements affect the composition of boards of directors. Federal securities laws require all directors who serve on audit, compensation and nominating committees to be independent from the management of the company, and NYSE and NASDAQ listing rules require a majority of the board of directors to be independent. In addition, in 2018 California passed a law mandating female representation on the boards of publicly held companies based in the state. Companies are required by federal securities laws to disclose the experience, qualifications or skills of each director nominee that led the board to nominate that person to serve as a director. A company must also disclose whether and how its nominating committee considers diversity in identifying director nominees, and must make extensive disclosure about the nominating committee and how it functions.

Approximately half of large corporations in the United States have a common CEO and chair of the board of directors. Companies that have one person serving as both chair and CEO typically have a lead director with additional rights, responsibilities and compensation. In 2019, about 52 per cent of companies listed on the S&P 500 Index had separate chairs and CEOs, up from 29 per cent in 2005. ISS generally recommends a vote in favour of shareholder proposals requiring an independent chair, taking into consideration the company’s current board leadership structure (including whether the company maintains a strong lead director position), governance structure and practices (including overall board independence) and the company’s performance. In 2019, shareholders brought proposals at 60 companies to require an independent chair. These proposals enjoyed an average level of support of 30 per cent. Companies are also required to describe in their annual meeting proxy statements the leadership structure of their board of directors, such as whether the same person serves as chair and CEO, and to explain why the company has determined that its leadership structure is appropriate. To date, the governance trend is towards ensuring an independent board leadership structure through a lead independent director, as opposed to separating the CEO and chair functions in all companies.

Corporations are generally permitted by state corporate law to have classified, or staggered, boards of directors, in which roughly one-third of the directors are elected each year for three-year terms; however, classified boards have become substantially less common in recent years. With a classified board, shareholders can replace a majority of the directors only in two election cycles, so a classified board can promote the continuity and stability of a corporation’s long-term strategy, reduce a corporation’s vulnerability to abusive takeover tactics,

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7 See, e.g., Delaware General Corporation Law, Section 141(e).
and ensure that the institutional experience of the board of directors will not be swept away in a single lopsided election. On the other hand, classified boards historically have not halted well-priced, all-cash takeover bids. The percentage of S&P 500 companies with staggered boards has declined, to approximately 11 per cent in 2019, down from approximately 57 per cent in 2003. Shareholder proposals to declassify boards of directors enjoy strong support from shareholders: shareholders voted on such proposals at eight companies in 2019, and the proposals averaged approximately 80 per cent shareholder support. (Shareholders voted on 51 management-initiated proposals to declassify boards in 2019, and these averaged 99 per cent shareholder support.) However, corporations are more likely to implement a classified board in connection with an initial public offering (IPO). Despite an ISS policy of recommending a withhold vote for directors at the first public company annual meeting of a corporation that implements a classified board in connection with an IPO, in recent years more than half of IPO corporations implemented a classified board in connection with the offering, although some companies provide that the classified board will be declassified within several years of the IPO. Notwithstanding the trend towards removing classified boards, a 2013 empirical study confirmed that classified boards can enhance shareholder value.

Delaware law currently permits corporations to choose whether and how to afford insurgent director nominees access to a company's proxy statement, but rules implemented by the SEC enhance the ability of shareholders to propose providing groups of shareholders without control intent to nominate up to a certain portion (typically 25 per cent) of the company's entire board, known as proxy access. The interest in proxy access as a democratisation of corporate governance and voting has garnered increased strength. In late 2014, a group of pension funds announced a broad campaign to install proxy access at over 75 US publicly traded companies of diverse market capitalisations and across a variety of industry sectors. In 2019, shareholders at 30 companies voted on shareholder-initiated proposals to grant shareholders proxy access, and the proposals averaged 35 per cent support. These shareholder proxy access proposals typically seek to permit shareholders to nominate between 20 and 25 per cent of a company's entire board. Many companies are also either proactively revising by-laws to permit proxy access or submitting management-initiated proxy access proposals for shareholder consideration. Although shareholder proxy access is becoming more prevalent, it remains to be seen to what extent shareholders will seek to exercise proxy access rights.

Historically, brokers holding stock of a corporation on behalf of clients have voted that stock at their discretion when their clients do not provide specific voting instructions. However, the NYSE listing rules now prohibit broker discretionary voting for listed companies on certain topics including governance-related proposals, and the Dodd-Frank Act eliminated broker discretionary voting in elections related to the election of directors, executive compensation and any other significant matter as determined by the SEC. As a result, directors in uncontested elections have more difficulty achieving majority votes. Lack of broker discretionary voting also increases the influence of activist shareholders and the power of proxy advisory firms such as ISS. Further concentrating voting power in the hands of activists is the problem of empty voting, in which an activist uses derivatives and similar

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arrangements to purchase voting power without taking on commensurate economic exposure to the corporation’s stock – for example, by simultaneously purchasing and short-selling a stock, resulting in no net economic exposure or investment costs aside from transaction fees.

In uncontested elections, directors were historically selected by plurality vote, but in recent years, majority voting policies have been adopted by approximately 90 per cent of companies included in the S&P 500 Index. Under a majority voting policy, directors in uncontested elections must receive a majority of the votes cast, rather than the plurality required by Delaware law, and if they do not must tender their resignation, although Delaware courts will generally defer to a board’s business judgement on whether to accept or reject a resignation from a director in such circumstances. Because directors must win a plurality of votes regardless of a corporation’s majority voting policies, these policies have relatively less effect in the context of contested elections; their primary effect is to increase the power of withhold recommendations from ISS against incumbent directors running in uncontested elections.

ii Directors

Directors’ most basic and important responsibility is to exercise their business judgement in a manner they reasonably believe to be in the best interest of a corporation. In fulfilling that duty, directors must consider and reconcile the interests of various stakeholders and their impact on the business of the corporation. In exercising their duties of care and loyalty, directors are afforded the safe harbour of the business judgment rule in seeking to promote sustainable, long-term investment and environmental, social and governance (ESG) principles in a manner designed to enhance the long-term value of their companies.

In most situations, directors do not and should not manage the day-to-day operations of the corporation, but instead exercise oversight in reasonable reliance on the advice of management, outside consultants hired by the corporation and their own understanding of the corporation’s business. The courts will generally defer to decisions that boards make, granting them the ‘presumption that in making a business decision the directors of a corporation acted on an informed basis, in good faith, and in the honest belief that the action taken was in the best interests of the company’ – a presumption referred to as the business judgement rule.10 The business judgement rule applies to most decisions that a board of directors makes. When a shareholder challenges a board’s business judgement, ‘the court merely looks to see whether the business decision made was rational in the sense of being one logical approach to advancing the corporation’s objectives’.11 To obtain the protection of the business judgement rule, directors must satisfy their duty of care, which entails reviewing the available material facts, and their duty of loyalty, which requires the disinterest and independence of the directors. In practice, the business judgement rule will protect directors when the corporate records reflect that they reviewed and considered the facts available to them and the advice of their advisers and when the directors did not have a conflict of interest in the decision.

The board of directors should work with management to set an appropriate ‘tone at the top’ of the corporation to encourage conscientiousness, transparency, ethical behaviour and cooperation throughout the organisation. It should approve the company’s annual operating plan and guide its long-term strategy, and should monitor and periodically assess the corporation’s performance in terms of these goals. The board should monitor and evaluate

11 In re Dollar Thrifty Shareholder Litigation (Del. Ch. 8 September 2010).
its own performance as well, noting any deficiencies in its expertise and composition with an eye towards rectifying them with future director nominations. It should monitor the organisation’s risk management practices, as well as compliance with applicable law and best practices, set standards for corporate social responsibility, and oversee relations with regulators and the corporation’s various constituencies, which increasingly includes engaging directly in director-level dialogue with shareholders. It should evaluate the corporation’s CEO and senior management, and ensure that a succession plan is in place for the CEO and senior management, an issue that has received heightened focus in light of increased turnover rates and visible succession crises. When a company receives a proposal for a large transaction that creates a conflict – or the appearance of a conflict – between the interests of the corporation’s shareholders and its management, the board should take care to place itself at the centre of the transaction, and should consider the merits of a special committee of independent directors to oversee the company’s response to the proposal.

Directors enjoy substantial protection against personal liability for failures of board oversight. Under Delaware law, directors can be held personally liable for a failure to monitor only where there is ‘sustained or systemic failure of the board to exercise oversight – such as an utter failure to attempt to assure a reasonable information and reporting system exists’, which is a ‘demanding test’. Delaware courts have repeatedly emphasised that they will not impose liability under this standard unless directors have intentionally failed to implement any reporting system or controls or, having implemented such a system, intentionally refused to monitor the system or ignored any red flags that it raised. Proxy advisory firms and institutional investors have also been increasingly willing to wield the threat of withhold vote recommendations in response to perceived risk oversight failures or missteps.

III DISCLOSURE

Public corporations are subject to a disclosure regime that generally requires annual and quarterly reports, as well as current reports, to be filed following the occurrence of certain events, such as entry into material agreements, completion of significant acquisitions or dispositions of assets, and changes in officers or directors and amendments to the corporation’s charter or by-laws. Public disclosure is also required of certain transactions in the corporation’s securities by corporate insiders, such as officers and directors, and of material non-public information that a corporate insider has disclosed to certain individuals, such as stock analysts or shareholders. Additionally, the corporation must make significant disclosure whenever it solicits proxies for the votes of shareholders, as it must in connection with the election of directors or significant transactions, such as mergers or the sale of substantially all corporate assets.

Securities regulations require substantial annual disclosure of compensation awarded to the five named executive officers (NEOs) of a corporation, which are the CEO, CFO and the three other most highly compensated executive officers. The disclosure must describe all material elements of the NEOs’ compensation, including the overall objectives of the compensation programmes, the process for determining the amount of each element of compensation and the rationale underlying that process. Federal securities laws also require disclosure regarding the relationship between executive compensation and the company’s financial performance, the company’s policies governing hedging transactions of the

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company’s stock by employees and directors, and the ratio of the total compensation of the CEO to the median compensation of the company’s employees. In furtherance of the Dodd-Frank Act requirements, in 2015 the SEC adopted a rule requiring companies to disclose in registration statements, proxy statements and annual reports the ratio of CEO compensation to the median compensation of the company’s employees. The methodology for identifying the median employee compensation is not set forth in the rule, but is instead determined by each company.

IV CORPORATE RESPONSIBILITY

i Stakeholder governance

For several decades, there has been a prevailing assumption among many CEOs, directors, scholars, investors, asset managers and others that the sole purpose of corporations is to maximise value for shareholders. This exclusive focus on shareholder wealth maximisation has exacerbated pressure on corporations to take actions to maintain or boost the near-term stock price. Recently, there has been increasing concern about the negative consequences of shareholder primacy and the short-termism it has facilitated, as well as the longer-term impact on broader socioeconomic and sustainability issues. In 2019, the Business Roundtable issued a statement on the purpose of a corporation, signed by 181 public company CEOs, departing from its long-standing endorsement of shareholder primacy and embracing stakeholder governance, which posits that the fiduciary duty of management and the board of directors is to promote the long-term value of the corporation for the benefit of all its constituents, not solely to maximise shareholder wealth. Several prominent institutional investors, including BlackRock, Inc., the Vanguard Group and State Street Global Advisors, subsequently issued public statements similarly endorsing stakeholder governance.

Stakeholder governance is fully consistent with well-established principles of corporate law and the existing fiduciary framework for directors. Directors have a fiduciary duty to promote the best interests of the corporation, and in fulfilling that duty, directors exercise their business judgment in considering and reconciling the interests of various stakeholders and their impact on the business of the corporation. Indeed, the special genius of Delaware law in particular, and one of the primary reasons why it has become the indisputably pre-eminent jurisdictional choice of most major US public companies, is that it has been animated by a fundamental sense of pragmatism and its fiduciary duty framework has afforded corporations the breathing room they need to address evolving business challenges as well as expectations of shareholders. Companies and investors alike have been rethinking the ways in which they engage and have been providing robust and increasingly tailored disclosures about their approaches to strategy, purpose, and mission; board involvement, composition and practices; board oversight of strategy and risk management; the business case for long-term investments, reinvesting in the business and retraining employees, pursuing research and development, innovation, and other capital allocation priorities; sustainability, ESG and human capital matters; stakeholder and shareholder relations; corporate governance; and corporate culture.

ii Risk management

The board of directors should ensure that the corporation has a healthy and balanced attitude towards risk – keeping in mind that there is danger in excessive risk aversion, just as there is danger in excessive risk taking – and it should set standards for corporate risk management. Directors must identify key business risks, establish a system of board-level
compliance monitoring and reporting to oversee the management of these risks, and make a good-faith effort to ensure that the system is working effectively.\textsuperscript{13} When the corporation’s risk management functions raise a red flag, the board of directors should investigate the occurrence and see that the corporation takes measures appropriate to remedy any problems that it uncovers. The board should periodically review the effectiveness of the corporation’s risk management reporting functions (including how risks are identified and reported upward, how management responsibility for risk management is allocated and whether risk managers have access to the board of directors and senior management) and repair any deficiencies that it uncovers. In the United States, recent cybersecurity-related intrusions have brought heightened attention and scrutiny to questions of risk oversight and effective risk mitigation practices.

Some corporations have a dedicated board-level risk management committee, which the Dodd-Frank Act requires of certain publicly traded bank holding companies and non-bank financial holding companies, but most boards situate the risk management function at the audit committee, in response to a listing rule of the NYSE that requires the audit committee to discuss risk assessment and risk management policies. Companies are required to disclose in their annual proxy statement the extent of the board’s role in risk oversight activities and how the board administers its oversight function. The SEC has also issued specific guidance addressing when and how cybersecurity risks should be publicly disclosed. The reputational damage to boards and companies that fail to properly manage risk is a major threat, and ISS now includes specific reference to risk oversight as part of its criteria for choosing when to recommend withholding votes in uncontested director elections.

V SHAREHOLDERS

i Shareholder rights and powers

Shareholders are permitted to vote at annual and special meetings. State corporation law typically entitles shareholders to vote on matters including elections of directors, amendments to the corporation’s charter, transactions in which the corporation is acquired and sales of substantially all of the corporation’s assets. The NYSE requires a shareholder vote prior to the issuance of stock that will exceed 20 per cent of the voting power or common stock outstanding after the issuance. In addition, Rule 14a-8 under the federal Securities Exchange Act permits shareholders to propose and vote on additional non-binding resolutions, which typically concern issues of social justice or corporate responsibility. In 2019, shareholders voted on 170 proposals concerning ESG issues (with 31 proposals focused specifically on climate change and 61 focused on lobbying and political spending). ESG issues are becoming increasingly important to shareholders, with large institutional investors announcing a heightened focus on socially responsible investing and certain activist investors launching new funds with the same focus.

Corporations must also conduct a non-binding shareholder vote at least every three years to approve the compensation of their NEOs – votes that ISS policy also encourages – and an additional non-binding shareholder vote at least every six years to determine the frequency of these ‘say on pay’ votes.\textsuperscript{14} Non-binding advisory votes are also now required with

\textsuperscript{13} See, e.g., Marchand v. Barnhill, 212 A.3d 805 (Del. 2019).

\textsuperscript{14} For a discussion of effective shareholder engagement in the context of compensation policies, see Adam J Shapiro et al., ‘Compensation Season 2019,’ The Harvard Law School Forum on Corporate
respect to golden parachute compensation arrangements triggered by a merger or acquisition transaction. However, the Jumpstart Our Business Startups Act, or JOBS Act, signed into law in January 2012, exempts newly public ‘emerging growth companies’ from say on pay votes and certain other requirements for the earlier of five years or until the company meets specified size thresholds.

**ii Shareholders’ duties and responsibilities**

Under Regulation 13D of the Securities Exchange Act, shareholders or groups of shareholders acting in concert who acquire over 5 per cent of a company’s stock must publicly disclose their ownership stake within the next 10 days. Schedule 13D requires disclosure of the shareholder’s or group’s investment purposes, including any plans or proposals relating to significant transactions involving the company. The disclosure statement must also be amended promptly to reflect any material changes to information previously disclosed. Passive investors acquiring over 5 per cent of a company’s stock who certify that the securities were not acquired, and are not held, with the purpose or effect of changing or influencing control of the issuer may instead disclose ownership on a short-form Schedule 13G, the disclosure requirements of which are less onerous than those of the long-form Schedule 13D.

**iii Shareholder activism**

Hostile takeovers and shareholder activism – the capture of corporate control or influence over corporate policy by discrete groups of shareholders, typically to subjugate a corporation’s long-term strategy in pursuit of short-term profits or the return of capital to shareholders – are a significant threat to US corporations.¹⁵ In addition to cultivating strong relationships with its long-term institutional shareholder base, dealing with unsolicited offers and pressure from shareholder activists is more art than science.¹⁶

**iv Takeover defences**

A critically important tool for enabling boards of directors to discharge their fiduciary duties in the face of the threat of hostile takeovers and shareholder activism under current law remains the shareholder rights plan, or ‘poison pill’.

The shareholder rights plan entails a dividend of special rights to each of the corporation’s shareholders. In the event that a shareholder amasses equity ownership in excess of a predetermined threshold – often 10 to 15 per cent (with perhaps a higher threshold used for passive institutional investors) – without the approval of the board of directors, the rights held by every other shareholder trigger and convert into the right to purchase stock of the corporation at a price substantially below the current market value. Alternatively, most rights plans provide that the board of directors may instead choose to exchange one share of

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common stock for each right held by shareholders other than the hostile bidder or activist shareholder. Either way, the result of this conversion or exchange is that the ownership position of the triggering shareholder is substantially diluted.

The rights plan is the only structural takeover defence that allows a board to resist a hostile takeover attempt, and it has also been deployed in numerous activism situations. While it does not provide complete immunity from a takeover, it allows the board to control the process and provides the corporation with leverage to bargain for a higher acquisition price and the power to reject underpriced or otherwise inappropriate bids. It is also implemented exclusively by the board of directors and does not require shareholder approval, so it can be put in place in very short order.

The principal disadvantage of the rights plan is that ISS will typically recommend a withhold vote for all directors after the adoption of a rights plan that the company does not subject to shareholder ratification within a year of adoption. As a result, and because a rights plan can be adopted quickly, most corporations adopt a rights plan only after a takeover threat appears – and prior to that time, the plan is ‘kept on the shelf’.

Keeping a rights plan on the shelf offers almost all of the protection of an active rights plan without any risk from an adverse ISS recommendation, but it can leave a corporation vulnerable to stealth acquisitions, in which an activist shareholder purchases just under 5 per cent of a company’s stock, and then buys as much as possible on the open market within the next 10 days. Because Regulation 13D under the Securities Exchange Act gives shareholders 10 days after acquiring over 5 per cent of a company’s stock to publicly disclose their ownership stake, this technique can result in an acquisition of a substantial portion of a company’s equity before it is ever disclosed.17 Similarly, Regulation 13D patrols a narrow beat with regard to derivatives. While all interests must be disclosed after a shareholder crosses the 5 per cent threshold, only some derivative interests are counted towards that threshold – generally, only those that are settled in kind (for stock of the corporation rather than for cash from the derivatives counterparty), and only those that can be exercised within the next 60 days.18 However, because an activist may accumulate its position in a corporation, without public disclosure, the board of directors may not have any warning of the activist’s behaviour, and there is thus some risk that a company may not be able to adopt a rights plan in time to avoid a significant accumulation of stock in unfriendly and opportunistic hands.

Other defences against activist shareholders include a classified board of directors, limiting shareholders’ ability to call a special meeting, adopting an advance notice by-law that requires rigorous disclosure of a shareholder’s holdings and other interests in a corporation


18 Regulation 13D discourages shareholders from employing contracts or arrangements that divest beneficial ownership of a security as part of a plan or scheme to evade the reporting requirements of Section 13(d) of the Securities Exchange Act by counting the securities towards the 5 per cent threshold (Securities Exchange Act Rule 13d-3(b)). One court applied this provision to impute beneficial ownership to a shareholder of securities in which the shareholder had acquired derivative interests: CSX Corp v. Children’s Inv Fund Management, 562 F. Supp. 2d 511 (S.D.N.Y. 2008). Still, no bright-line rule has emerged to determine when a shareholder’s use of derivative instruments is suspicious enough to constitute such a plan or scheme to evade the reporting requirements, so the case offers only marginal protection from raiders and activist shareholders.
to nominate a director candidate or propose other items of business at a special or annual meeting, and limiting shareholders’ ability to act by written consent (70 per cent of S&P 500 companies prohibit shareholder action by written consent).

Overall, the availability of takeover defences has been steadily eroded over the years, predominantly as a result of shareholder activism led by ISS, union and public pension funds and academics. Today, only 1 per cent of S&P 500 companies have a rights plan in effect, down from 45 per cent in 2005 and 60 per cent in 2000. In 2019, shareholders at 27 companies voted on proposals to grant shareholders the right to call special meetings or to decrease the requirements to call a special meeting, with an average level of support of 45 per cent, and shareholders at 37 companies voted on proposals to grant shareholders the right to act by written consent or to decrease the requirements to act by written consent, with an average level of support of 40 per cent.

v Contact with shareholders
Shareholder relations have become increasingly complicated as a result of activist trends and have required greater attention at the board level, prompting a renewed focus on the proper role of direct dialogue between boards and shareholders, as well as the benefits and disadvantages of more open, regular lines of communication. Shareholder engagement is increasing, as both companies and institutional investors have sought to engage in more regular dialogue on corporate governance matters. A report by the EY Center for Board Matters at Ernst & Young LLP reported that 91 per cent of Fortune 100 companies included disclosures about their shareholder engagement efforts in their 2019 proxy statements, compared with 82 per cent in 2016.19 Recent disclosure reform efforts have also sought to require institutional shareholders to report their share positions on a more current basis as of the end of each quarter than is now the case, as well as suggesting more frequent reporting. Management generally serves as the primary caretaker of shareholder relationships, with the board providing oversight as to the presence of an effective shareholder relations programme. However, institutional investors are increasingly voicing their expectation that companies should provide access to independent directors. Some activists have also been seeking direct dialogue generally with companies in which they invest, independent of whether operational or other performance issues exist. In 2016, a group of large public companies and investors jointly developed and endorsed a set of principles on corporate governance that, among other things, called for active engagement with shareholders on key issues. Similarly, in 2018, BlackRock called for a new model of shareholder engagement based on year-round discussions among management, the board and shareholders about long-term value creation and long-term corporate contribution to society at large. Where shareholders request direct communications with the board, it may be desirable for directors, in appropriate circumstances and following consultation with management, to accommodate those requests. The policies and arrangements best suited for any given company will depend on, among other things, the preferences of directors, the nature and extent of existing relationships with major shareholders, the expressed preferences of those shareholders, and the structure and staffing of the company’s existing shareholder relations programme.

In 2000, the SEC promulgated Regulation FD to prevent companies from selectively disclosing material and non-public information to large investors and analysts. Under

19 EY Center for Board Matters, ‘Five takeaways from the 2019 proxy season’ (July 2019).
Regulation FD, certain employees of a company – including directors, officers, public relations or investor relations professionals, and others with similar responsibilities or who regularly communicate with market professionals or shareholders – may intentionally disclose material non-public information about a company only if the material is simultaneously disclosed to the public. If they disclose the information unintentionally, the same information must promptly be disclosed publicly. Disclosures made to the press and disclosures made in the ordinary course of business (e.g., customary communications with distributors or customers) are exempted. Intentional disclosures include disclosures in which the employee was reckless in not knowing that the information is material and non-public.

Information is considered material if there is a substantial likelihood that a reasonable investor would consider the information important when making investment decisions, and if the information adds significantly to the total mix of information available. Even if information is quantitatively insignificant, it may still be considered qualitatively material, and information is more likely to be deemed material in hindsight in light of subsequent reaction by the market. The SEC has issued guidance that certain categories of information are particularly likely to be considered material – among them, information related to earnings; corporate events such as mergers, bankruptcy, tender offers or changes in control; and products, discoveries and developments with respect to material contracts, customers or suppliers. While purported clarifications to previously announced information can themselves be considered material and non-public, ‘Regulation FD does not require that corporate officials only utter verbatim statements that were previously publicly made’. 20

Regulation FD makes unscripted dialogues between company officials and individual analysts and shareholders risky. 21 While it is unusual for companies to prohibit such meetings altogether, they should be approached carefully and by professional spokespeople only. Boards of directors should adopt corporate governance guidelines that ensure that the company’s media strategy is executed only through approved channels, and with the understanding that analysts and shareholders will often engage in such private dialogues with the hope of ferreting out exactly the sort of information that Regulation FD forbids company officials from disclosing in such a forum.

VI OUTLOOK

Corporate governance in the United States has changed dramatically over the past 30 years, and will undoubtedly continue to evolve in significant ways in the coming years. In particular, the SEC has increased its focus on ‘proxy plumbing’, including with respect to the accuracy, transparency and efficiency of the voting process; shareholder communications and retail participation in the voting process; and misalignment of voting power and economic interests (including through empty voting strategies involving purchasing voting securities and then hedging away the economic exposure with derivatives). The SEC has indicated that it is continuing to review the role of proxy advisory firms such as ISS and Glass Lewis in the voting process, which, in light of ISS’s substantial influence in the evolution of corporate governance norms over the past several decades, may have long-term and far-reaching implications. The SEC has also received many proposals for the reform of the Regulation

13D reporting regime, including to encompass additional forms of economic interests and to close the 10-day reporting window that raiders have used in recent years to facilitate stealth acquisitions of control blocks without paying a premium. Similarly, in 2016, legislation was introduced in the Senate seeking amendments to Regulation 13D that would require greater transparency from investors accumulating large positions in public securities.

At the state level, the courts of Delaware have been refining the fiduciary duty rules applicable to conflict transactions and the review of merger and acquisition proposals in recent years, often to increase the scrutiny directors will face in connection with such transactions and, more generally, to recalibrate the relative power of shareholders and directors.

Spurred on by the accounting scandals of the early 2000s and the financial crisis at the end of the past decade, the political and public appetite for ever more corporate governance remains strong. However, we have recently seen a heightened awareness of short-termist pressures in the markets and their impact on boards of directors charged with guiding a company’s strategy to achieve long-term value creation, including an increased focus on the extent to which new corporate governance reforms may exacerbate, rather than ameliorate, short-termist pressures. The Business Roundtable’s statement on the purpose of the corporation exemplifies the widespread acceptance by companies and institutional shareholders that corporations must consider the interests not only of shareholders, but also those of employees, customers, suppliers, the environment, communities and other constituencies that are critical to the success of the corporation. Indeed, there has been an awakening to the idea that corporate governance is not just about the allocation of decision-making authority and accountability as between corporations and shareholders; instead, it is being reconceived in light of the broader purpose and role of corporations as engines of the economy, ladders of socioeconomic mobility, innovators of technological progress and key stakeholders in environmental sustainability.

Shareholder engagement practices have significantly evolved as well, with the frequency and depth of engagement increasing alongside a more fundamental rethinking of the nature of relationships with shareholders and the role that these relationships play in supporting – or undermining – board efforts to take long-term perspectives. A central aspect of the continuing debate is whether initiatives styled as governance reforms operate to shift the locus of control over the corporate enterprise from those with direct knowledge, involvement in and fiduciary responsibilities for the enterprise towards entities lacking those attributes, and whether imposing some form of duties, regulations or mandated best practices on such entities is needed.

In many respects, the relentless drive to adopt corporate governance mandates seems to have reached a plateau in the United States, with essentially all of the prescribed best practices – including say on pay, the dismantling of takeover defences, majority voting in the election of directors and the declassification of board structures – having been codified in rules and regulations or voluntarily adopted by a majority of S&P 500 companies. Whether this portends a new era of more nuanced corporate governance debates, where the focus has shifted from ‘check the box’ policies to more complex questions, such as striking the right balance in recruiting directors with complementary skill sets and diverse perspectives, and tailoring the board’s role in overseeing risk management to the specific needs of the company, remains to be seen.

Continued debate over, and the evolution of, US governance rules thus appear likely.
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She has advised on noteworthy public–private partnership (PPP) and infrastructure projects such as the national identification card PPP, a PPP for the development of a floating dry dock, the Volta Lake Transport Company’s US$300 million Eastern Corridor multi-modal transport project as well as on the proposed construction of a new LPG pipeline from the port of Tema to the Tema Oil Refinery. She is experienced in advising on various aspects of construction projects, including planning, permitting and finance, and has advised local and international developers on the construction of significant real estate projects in Ghana, including the Mövenpick Ambassador Hotel, the first mixed-use hotel project of its kind in Ghana, and One Airport Square, the first certified green office building in Ghana.

In the energy and oil and gas space, she has advised on various matters. Recently, she has advised on the establishment of off-grid solar energy companies in Ghana, and on the pre-feasibility study of private sector participation in the Electricity Company of Ghana, which is the largest electricity distribution company in Ghana. She currently advises Puma Energy (an affiliate of Trafigura), one of the largest bulk distributors of petroleum products in Ghana, on a range of commercial matters, as well as other local and international oil and gas sector players involved in bunkering and other activities.

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In his advisory role to large companies, Paulo was a member of their corporate governance and corporate sustainability and ethics committees as an expert, and prepared several legal opinions for management and supervisory bodies. Paulo is also a member of the corporate bodies of several Portuguese companies.

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Danil graduated from the international law department of the Moscow State Institute of International Relations (MGIMO) and joined the firm in 2007.

ELLISA O HABBART
The Delaware Counsel Group LLC
Ms Habbart leads The Delaware Counsel Group and assists lawyers globally on transactions and governance issues with a Delaware connection. Outside counsel and in-house counsel of Fortune 100 companies, major financial institutions and private equity firms worldwide rely on Ms Habbart as their guide on Delaware law. A significant portion of Ms Habbart’s representations involve cross-border transactions. Typical representations include fund formations, mergers and acquisitions, joint ventures, recapitalisations, financings and new equity issuances. In addition to helping to implement such transactions and rendering legal opinions, Ms Habbart regularly advises management on governance issues relating to significant transactions and issues that arise during the life of a business entity.

Ms Habbart is top ranked in Chambers USA as one of America’s leading business lawyers in the Delaware corporate and mergers and acquisitions law section, and by Who’s Who Legal: Corporate Governance. According to Chambers, clients report that she ‘has expert knowledge in the field but is still commercially sensitive to what the client aims to achieve’, and is ‘very plugged in to Delaware legal developments’. She is also rated ‘AV’ by Martindale-Hubbell.

Ms Habbart is one of only 26 lawyers appointed to the Council of the Section of Corporation Law of the Delaware State Bar Association, the group responsible for monitoring and recommending amendments to the Delaware General Corporation Law. She is also the Corporate and M&A Law Committee’s representative on the Economic Sanctions working group of the International Bar Association’s Legal Policy and Research Unit, which develops and implements innovative strategies and initiatives relevant to business and the law, the global legal profession and the broader global community. She is the former vice chair of the Corporate and M&A Committee Corporate Governance Subcommittee and holds significant leadership positions in the American Bar Association.

Ms Habbart’s publications include a chapter on Delaware law in the Partnerships, Joint Ventures and Strategic Alliances; Delaware Limited Liability Company Forms and Practice Manual, which is updated annually; the US chapter of the Treasury Shares Guide; the Delaware chapter in Private Fund Dispute Resolution; the IBA’s Directors and Officers Checklist; and the first in-depth analysis of the Uniform Law Commission Uniform Statutory Trust Act in the American Bar Association publication The Business Lawyer.

Prior to founding The Delaware Counsel Group LLC, Ms Habbart was an associate and partner with Prickett Jones & Elliott and was the partner in charge of the Delaware office of Stradley Ronon Stevens & Young. In addition to her Juris Doctor, Ms Habbart has a master’s degree in taxation.
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Mitsuhiro Harada has been a partner in the M&A and corporate group at Nishimura & Asahi since 2010 and was previously seconded to the US international law firm Sullivan & Cromwell LLP in New York for one year. Mr Harada has represented both Japanese and non-Japanese buyers or sellers in numerous cross-border commercial transactions in various industries, including stock and asset acquisitions, private equity and venture capital investments and strategic alliances. Mr Harada also has been involved in acquisitions and joint ventures in and outside Japan, especially in the South East Asian countries.

Mr Harada graduated from the University of Tokyo (LLB) in 1999 and gained his LLM from New York University School of Law in 2006. He was admitted to the Japanese Bar in 2000 and the New York Bar in 2007.

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Min Yung Hong has been an attorney at Kim & Chang since 2007. He practises in a wide range of corporate and finance law areas and various regulations of listed companies, with a focus on corporate governance, insolvency and restructuring, mergers and acquisitions, banking, securities and capital markets.

Mr Hong represents financial and non-financial clients in relation to the restructuring of corporate governance, which typically includes the establishment of financial or non-financial holding companies or de facto holding companies through mergers or spin-offs of related companies.

Mr Hong also represents debtor companies in relation to the pre-workout and workout proceedings that are managed by creditor financial institutions, and rehabilitation proceedings governed by the Korean courts. A thorough understanding of local bankruptcy law and the commercial interests of both creditors and debtors are keys to the successful rehabilitation or financial normalisation of debtors.

Mr Hong received an LLM degree from the University of San Diego, School of Law in 2014, and his bachelor's degree in business administration from Seoul National University in 2006. He attended the Judicial Research and Training Institute of the Supreme Court of Korea in 2006. He was admitted to the Korean Bar in 2007.

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Elke Janssens focuses on corporate law and corporate governance. She advises listed companies and has assisted in several public offerings. Elke also regularly acts in negotiations for M&A transactions and restructurings.

Elke received her law degree from the Vrije Universiteit Brussel (VUB) in 1996. She obtained a master's degree in business law from the Université libre de Bruxelles (ULB) in 1998 and a master's in management from VUB in 2001. She completed coursework in the executive MBA programme at the Solvay Business School from 2006 to 2007. Elke was admitted to the Brussels Bar in 1997 and is a partner at NautaDutilh.

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Mr Jeon represents many large business groups in Korea in relation to their restructuring of corporate governance, which typically includes the establishment of holding companies or de facto holding companies through mergers or spin-offs of related companies.

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Kee Yeng’s areas of practice encompass mergers and acquisitions (for both public and private companies), equity capital markets and corporate advisory work for financial institutions and public companies listed on the Singapore Exchange. Kee Yeng has advised sovereign funds, private equity firms and multinational corporates in an extensive range of domestic and cross-border transactions including public takeovers, private acquisitions and joint ventures. She is also actively involved in the listing of structured warrant programmes on the Singapore Exchange.

Kee Yeng has been recognised for her work in Corporate/M&A in *Chambers Global*, *Chambers Asia-Pacific* and *IFLR1000*. She has also been recommended by *The Legal 500 Asia Pacific* for public mergers and acquisitions.

Prior to joining the firm, she served as a justices’ law clerk and as an assistant registrar with the Supreme Court of Singapore. Kee Yeng joined the firm in 2007 and has been a partner since 2009.

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Ryan specialises in public and private M&A and general corporate and commercial law. He has advised JSE-listed and multinational clients on a variety of national and cross-border mandates. He has worked in particular in the energy and natural resources, education, mining, hospitality and private security sectors. His expertise extends to B-BBEE transactions, corporate reorganisations, corporate governance, shareholder activism and takeovers.

In 2018, Ryan spent six months on a StrongerTogether secondment to the London office of Freshfields Bruckhaus Deringer.

Ryan holds BA and LLB degrees from the University of Cape Town and an LLM from the University of Florida, USA.
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Prior to joining Kim & Chang, Mr Lee worked at prominent law firms in New York and Silicon Valley.

Mr Lee is a frequent speaker on the topics of M&A, venture capital and IP matters, and he was a speaker at Stanford University’s US-Asia Technology Management Center School of

Mr Lee received his JD from the University of Pennsylvania Law School in 2004, and his BA from Seoul National University in 2000. He also received a certificate in business and public policy from the University of Pennsylvania, The Wharton School in 2004. He is admitted to the New York and Californian Bars.

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Andrew is a senior partner, and previously co-head, of the corporate mergers & acquisitions department at Allen & Gledhill. He has advised clients on numerous market-leading corporate and merger and acquisition transactions. He also advises clients on corporate governance, regulatory and compliance matters. His clients include MNCs, listed and non-listed companies, financial institutions and private equity firms.

Andrew was called to the Singapore Bar in 1986. He was an associate with the firm in 1988/89 before spending time as an investment banker. He rejoined the firm in 1993 as a partner.

Andrew serves on the board of trustees of the National University of Singapore. He currently is a director of Singapore Press Holdings Limited, Jurong Engineering Limited and Singex Holdings Pte Ltd. He is also a Fellow of the Singapore Institute of Directors, and a member of the National University of Singapore Law Advisory Council.

He is consistently recognised for his leading expertise in various publications including *Chambers Global*, *Chambers Asia-Pacific*, *IFLR1000*, *The Legal 500 Asia Pacific*, *Best Lawyers* and *Who's Who Legal*.

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Didier Martin is one of the leading specialists on French public tender offers, securities law and privatisations. He devotes a significant part of his time to litigation in various areas such as securities law and takeovers, white-collar crime and bankruptcy.

He has published numerous books and articles on a wide variety of corporate law subjects, with a particular emphasis on French tender offers, including the reference works *Les Offres Publiques d’Acquisition*, *Les Sociétés Holdings* and *Mergers & Acquisitions in France*. He is also responsible for the drafting and publication of the commentaries on the French Monetary and Financial Code (updated each year).

He is a member of various committees and associations, including the Financial Transactions Committee of the MEDEF and ANSA (major French business associations), as well as the Haut Comité Juridique de la Place Financière, created by the stock exchange authority (AMF) and the Banque de France.

Mr Martin is also co-president of the Commission Europe (within the Club des Juristes – a leading French legal think tank).
About the Authors

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Mr Nakayama obtained his LLB from the University of Tokyo in 2004, and his LLM degree and the certificate of merit award in mergers and acquisitions from the University of Michigan Law School in 2012. Mr Nakayama was admitted to the Japanese Bar in 2005 and the New York Bar in 2013.

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Daniel Pardede is a partner in the mergers and acquisitions practice group, with more than 10 years of legal practice experience. He has assisted multinational clients in cross-border transactions, and has been involved in handling various legal corporate and commercial issues, varying from corporate and licensing day-to-day work to assisting in providing advisory services to clients in relation to corporate and commercial issues. He has also been involved in mergers and acquisitions work, as well as corporate restructurings and asset disposals, has assisted major clients in a number of high profile transactions, and has dealt with government authorities such as the Indonesian Investment Coordinating Board (BKPM). He has advised a wide range of domestic and international clients across various industry sectors, including TMT, real estate, plantation, manufacturing and trading.

Daniel is praised by clients for being ‘good’ and having ‘strong experience’, ‘good at leading the legal team, very helpful and understand[s] how to solve the problem’. Mr Pardede has an ‘excellent understanding [of] our business and issues and he is able to provide feasible and practical solutions’. ‘Daniel is more of a business partner for us than an outsource lawyer. We are truly happy to be working with him’ and he gives ‘top level service’ according to *IFLR1000* and the 2019 and 2018 editions of *Asialaw Profiles*.

Daniel is listed as one of 10 Indonesia’s legal industry’s Rising Stars by *Asian Legal Business* (2019).

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Linda advises clients mainly on mergers and acquisitions, whereby she has experience in both domestic and cross-border transactions. In addition, she advises on shareholder agreement arrangements as well as general corporate and business law matters. Linda has worked with the firm since her graduation from the University of Helsinki in 2015.
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Her recent work with the firm includes advising the Ghana and Burkina Faso governments on the legal and regulatory framework for the Railway Interconnectivity Project, and international petroleum companies seeking to set up local subsidiaries and joint ventures on regulatory compliance and governance issues.

Ewurabena obtained her bachelor of laws (LLB) degree from Kwame Nkrumah University of Science and Technology and a qualifying certificate in law from the Ghana School of Law. She also holds an LLM degree from Columbia University in New York where she served as the Board Secretary to the Law in Africa Student Society. Ewurabena is licensed to practise law in Ghana and the State of New York.

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Clemens Philipp Schindler is a founding partner of Schindler Attorneys. Before establishing the firm, he spent six years as a partner at Wolf Theiss, where he led some of the firm’s most prestigious transactions and headed its Brazil operations. Prior to that, he practised with Haarmann Hemmelrath in Munich and Vienna, as well as with Wachtell Lipton Rosen & Katz in New York. Mr Schindler’s practice focuses on corporate and tax advice in relation to public and private M&A, private equity and corporate reorganisations (such as mergers, spin-offs and migrations), most of which have a cross-border element. Mr Schindler is ranked by international legal directories such as Best Lawyers, Chambers Global, Chambers Europe, The Legal 500, IFLR1000 and Who’s Who Legal. The German legal directory JUVE singles him out as one of Austria’s top 20 corporate and M&A lawyers, while the Austrian business journal Trend named him among the country’s top 10 both M&A as well as tax experts. Besides the listings for the Austrian market, both Chambers Global and Chambers Europe acknowledge his Brazilian expertise in a special ranking.

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Paul was awarded ‘Ireland Corporate Lawyer of the Year 2016’ by Client Choice. He is recommended by a number of leading publications and directories, including Best Lawyers, *Who’s Who Legal*, *Chambers Global*, *The Legal 500*, *IFLR1000* and *Chambers Europe*.

‘A leading individual . . . very experienced and knowledgeable’ (*The Legal 500* 2018); ‘Exceptional lawyer with great commercial and legal abilities . . . his knowledge of technical and commercial realities is very strong’ (*Chambers Global* 2018); ‘A very experienced lawyer. He displays very sound judgment and commercial understanding’ (*IFLR1000* 2018); ‘Top-class for capital markets . . . very accomplished, very articulate: good commercially and technically. Very calming, competent, a good communicator, efficient and proactive’ (*Chambers Global* 2017).

He has been a partner with the firm since 1996; managed A&L Goodbody’s London office from 1999 to 2004; served as head of the firm’s corporate department between 2005 and 2010, and as chairman of the firm between 2010 and 2016; and continues actively to serve clients on a range of corporate and commercial law matters. Paul also carries management responsibility for a number of the firm’s key relationships.

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Ms Wilkenhuysen received her law degree from the University of Leuven in 1991, a master’s degree in business and tax law from the Free University of Brussels in 1993, and an LLM from Duke University School of Law in 1996. She joined NautaDutilh in 1997 and became a partner in 2007.

Ms Wilkenhuysen is a frequent writer and speaker, and has published various books and articles on selected topics of corporate law. She is also a member of the International Bar Association, the European Private Equity and Venture Capital Association and the Duke Alumni Association.

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Richard graduated from the National University of Singapore with an LLB (Hons) degree. He joined Allen & Gledhill on a scholarship in 1995 and became a partner in 2000. During his time at Allen & Gledhill, he undertook a secondment as regional legal counsel for the CNBC Asia and National Geographic cable channels in Singapore, and later with General Electric International Inc, in Hong Kong. He also had a one-year stint in the London office of Linklaters, where he gained considerable experience on cross-border transactions.
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