Corporate Governance

Contributing editor
Holly J Gregory

2017

GETTING THE DEAL THROUGH

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Corporate Governance 2017

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Sixteenth edition

Getting the Deal Through is delighted to publish the sixteenth edition of *Corporate Governance*, which is available in print, as an e-book and online at www.gettingthedealthrough.com.

Getting the Deal Through provides international expert analysis in key areas of law, practice and regulation for corporate counsel, cross-border legal practitioners, and company directors and officers.

Throughout this edition, and following the unique **Getting the Deal Through** format, the same key questions are answered by leading practitioners in each of the jurisdictions featured. Our coverage this year includes new chapters on Chile, Russia and Ukraine.

Getting the Deal Through titles are published annually in print. Please ensure you are referring to the latest edition or to the online version at www.gettingthedealthrough.com.

Every effort has been made to cover all matters of concern to readers. However, specific legal advice should always be sought from experienced local advisers.

Getting the Deal Through gratefully acknowledges the efforts of all the contributors to this volume, who were chosen for their recognised expertise. We also extend special thanks to the contributing editor, Holly J Gregory of Sidley Austin LLP, for her continued assistance with this volume.

GETTING THE
DEAL THROUGH

London
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Global overview

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Corporate governance remained a top priority in 2016, demonstrating both its importance and 'staying power' as an essential consideration for companies and their investors and advisers. In the following global overview, we endeavour to outline recent corporate governance developments, and to analyse their significance and likely near-term trajectory. Although our global overview outlines developments region-by-region, as a whole the overview highlights 'imports' and 'exports' of best practices and considerations among jurisdictions and the tendency for corporate governance standards to coalesce across jurisdictions.

United States

Shareholder activism

Shareholder activism faced significant financial and legal headwinds in 2016. Examples of these challenges include:

- Pershing Square's struggles with Valeant, which were both financial (the realisation of an over US$3 billion loss on its investment) and legal (a federal securities class action suit regarding their failed joint bid for Allergan);
- Eddie Lampert's losses with respect to his investment in Sears (with headlines even declaring 'How Sears Ruined its CEO Eddie Lampert's Hedge Fund');
- the US Department of Justice bringing an enforcement action against ValueAct for its failure to comply with the waiting period requirements under the Hart-Scott-Rodino Antitrust Improvements Act of 1976; and
- the US Securities and Exchange Commission (SEC) targeting activists for failing to adequately disclose beneficial holdings information.

In fact, after taking into account losses, withdrawals and redemptions, shareholder activist assets under management (AUM), as a percentage of total hedge fund AUM, declined in 2016 for the first time in several years, and activist hedge funds faced more withdrawals and redemptions than new investments for the first time since the financial crisis.

Against this backdrop, strong shareholder activist activity in the first quarter of 2017 has spurred a flurry of articles on shareholder activism's revival. So far in 2017, we have already seen:

- Jana Partners enter into a settlement agreement with Bristol-Myers Squibb and Tiffany & Co, and target Whole Foods;
- Carl Icahn and Nelson Peltz take large positions in Bristol-Myers Squibb and Procter & Gamble, respectively;
- Starboard Value target Tribune Media;
- Mantle Ridge enter into a settlement agreement with CSX Corporation; and
- Elliott Management enter into a settlement agreement with NRG Energy and target both BHP Billiton and Arconic (indirectly leading to the ouster of its CEO).

At the same time, we have also seen ValueAct announce plans to return US$1.25 billion to investors, stating that current valuations 'can only be justified by assuming cyclically high corporate margins will persist, a certainty of lower corporate tax rates and a risk-free rate that stays near all-time lows' and that ValueAct is sceptical of all of the above.

Although there is no doubt that shareholder activism is here to stay, we think that ValueAct's return of capital to investors is an important signal that the structural challenges of the asset class that were demonstrated in 2016 (eg, low investment diversification and liquidity challenges) may continue to cause headwinds in 2017, despite the announcement of new targets and settlements at the beginning of the year.

We also expect that there will be a continued focus on a target company's decision to settle with an activist. In the past few years, we have seen a rise in companies settling with activists in lieu of a full proxy fight, with 63 per cent of requests for board seats ending in settlement in 2016, up from 54 per cent in 2015. The value to a target company of a settlement agreement is often détente; in particular, the activist agreeing to a standstill. As more activist funds refuse to agree to meaningful standstills, we expect more target companies to ask 'what's in it for them' in agreeing to settlement agreements, which could have a potentially meaningful impact on market practice.

We will also be watching the New York City Pension Funds (NYCF) 'vote no' campaign against the election of one of NRG Energy's directors with interest. The director was one of the two nominees appointed to the NRG Energy board as a result of the company's settlement agreement with Elliott Management and Bluescape Energy Partners. NYCF argues that 'a deeply flawed process' allowed 'short-term activist investors' to appoint the director to the board and that the director's history of 'climate change denial' disqualifies him from sitting on NRG's board. In addition to appearing to be the first example of a large institutional investor criticising a shareholder activist settlement by launching a 'vote no' campaign, the campaign raises the interesting question of whether institutional investors will actively take the position that (at least for certain companies) some views per se disqualify someone from board service.

Universal proxy

In October 2016, the SEC proposed long-expected changes to the proxy rules to require, among other things, the use of universal proxy cards in the case of contested director elections at annual meetings. The universal proxy card would include the nominees of all parties to better simulate freedom in voting by allowing shareholders to vote for any combination of management and dissident nominees of their choice. Accordingly, each party in a contested election – management and one or more dissident shareholders – would distribute their own proxy materials but each proxy card would be required to include the nominees of all parties. At the time of writing, the fate of the SEC's universal proxy proposal is unclear. After soliciting public comment, the proposed rule is now under SEC review. Despite Carl Icahn's appointment as special adviser to President Trump, we think it is unlikely that the universal proxy will remain high on the SEC's agenda given the new SEC Chairman Jay Clayton, the composition of the rest of the SEC and the prohibition on its implementation by the Financial CHOICE Act of 2017 (a proposed alternative to the Dodd-Frank Act) (the Financial Choice Act, which was approved by the full House in June 2017). In any case, the universal proxy will not be in effect during the 2017 proxy season given the timing of the proposed rules.

SNAP and dual-class share structures

The SNAP initial public offering (IPO) sparked heated discussions on dual-class share structures. While dual-class share structures have existed for years, especially among telecommunication, media and technology companies, to preserve or provide voting power above economic participation levels, the SNAP voting structure (although not without precedent) has provoked a reaction which would go beyond addressing the SNAP situation. SNAP issued only non-voting shares in its IPO, retaining all voting power for its founders and a few pre-IPO investors. Following the SNAP IPO, the Council of Institutional Investors (CII) has asked that some major indices consider the possible exclusion of shares with no voting power from their core indices. In addition, reviving a proposal that the CII had previously made in 2012, in remarks before the SEC Investor Advisory Committee, the executive director of the CII asked the SEC to bar future no-vote share structures, and more significantly, require sunset provisions for differential common stock voting rights and consider enhanced board requirements to ensure that boards do not act as rubber stamps for founders, if the exchanges refused to bar dual-class voting structures.

Our view is that it is unfortunate that the SNAP IPO reaction has generated another wave of doctrinaire 'one size fits all' commentary on dual-class share structures. We believe any assessment of dual-class structures should be based on the specifics of the structure, the needs and governance profile of the company and, perhaps most importantly, the company's historic absolute and relative performance. We also think it is important, when developing a view on regulations or restrictions of dual-class structures to recognise the need for retail investors to have a sufficient range of investment choices in the public markets and the need for US markets to remain competitive with other countries, such as Hong Kong and Singapore, which are considering allowing dual-class structures to attract more public offerings.

Virtual annual meetings

In December 2016, the SEC granted 'no action' relief on HP's request to exclude a shareholder proposal from its proxy statement that would require the HP board to adopt a policy to initiate or restore in-person annual meetings. Although the granting of no-action relief was not unexpected, it did spark further discussion regarding virtual-only meetings as well as the attention of the NYC Comptroller, Scott Stringer, who in April 2017 announced that he would recommend that the NYCF vote against directors at companies that hold virtual-only annual meetings. In addition, Mr Stringer's office sent letters to the 17 companies in the S&P 500 that either held a virtual-only meeting in 2016 or have announced plans to hold such meetings in 2017, urging these companies to hold in-person or hybrid (in-person, with the option to join virtually) meetings.

The number of companies holding virtual-only meetings is small but growing, according to Broadridge Financial Solutions, Inc, the leading provider of these services; 154 companies conducted virtual-only meetings in 2016, up from 21 such meetings in 2012. This technology is not confined to the US. In 2016, Jimmy Choo plc was the first UK-listed company to hold a virtual-only annual meeting.

Given the limited number of companies that have shifted to a virtual-only format, we think it is still too early to assess the impact of a virtual-only format on shareholder engagement. The argument that a virtual-only format could be used to moot dissent or that something might be lost when management is no longer forced to be held accountable to shareholders face to face, could be constructively addressed with modifications to technology that make a virtual-only meeting more analogous to an in-person meeting rather than a requirement that meetings be held in person. Further, the reaction against virtual-only meetings assumes that traditional in-person meetings provide an adequate forum for a back-and-forth between a shareholder and management. In reality, these meetings are often dominated by the loudest voices in the room. By contrast, virtual-only meetings can provide the opportunity for questions from a wider range of shareholders to be addressed, with some companies continuing to answer and posting responses to questions, received during the meeting, after the meeting has concluded. We would also posit that resistance to virtual-only meetings too quickly dismisses the reality that a virtual-only format is being used successfully by companies on earnings conference calls and hints more of a generational divide and resistance to change than a legitimate concern about shareholder rights. It is difficult to argue that the future is not virtual.

14a-8 proposals: proxy access update, gender pay gap disclosure

A question at the top of the minds of many is whether the Rule 14a-8 regime will be overhauled by the Trump Administration. In April 2017, Representative Jeb Hensarling released a draft of the Financial Choice Act that includes changes to the shareholder proposal eligibility requirements. Currently, Rule 14a-8 requires a company to include a shareholder proposal in its proxy material if certain eligibility requirements are met (eg, that the shareholder owns at least US$2,000 or 1 per cent of securities entitled to vote on the proposal). Because of its low eligibility requirements, as currently constituted, Rule 14a-8 provides a low-cost mechanism for shareholders to provide 'feedback' on specific issues to management and the board. If enacted, the Financial Choice Act would eliminate the US$2,000 test, thus requiring a shareholder to hold at least 1 per cent of an issuer's securities entitled to vote on the proposal and increase the holding requirement from one year to three years. We anticipate that the proposed changes to the shareholder proposal eligibility requirements will elicit much opposition and debate. Despite the fact that only three individuals were responsible for approximately 70 per cent of the shareholder proposals brought by individual investors among Fortune 250 firms in 2016, we expect that the proposal will be viewed as an attempt to strip small shareholders of a valuable tool for engaging with large companies.

The potential power of the current Rule 14a-8 regime is demonstrated by the evolution of proxy access. Proxy access refers to the right of shareholders, who meet certain eligibility and procedural requirements, to include their nominees for director (subject to limitation) on a company's proxy card. In the span of only two years, proxy access has evolved from non-existent to widespread almost entirely as a result of successful (or threatened) Rule 14a-8 proposals. As of December 2016, just over 50 per cent of S&P 500 companies have adopted proxy access by-laws, a staggering development when compared to the mere six US companies that had such by-laws in December 2014. In 2016, we also witnessed the first proxy access director nomination, when the activist fund GAMCO Investors proposed a candidate for the board of the National Fuel Gas Company (NFG). GAMCO ultimately withdrew the nomination after NFG declared the nomination to be invalid on the basis that GAMCO did not satisfy NFG's proxy access by-law's 'passive investment' requirement. Even though the GAMCO nomination was withdrawn, we believe that it is noteworthy because it illustrates the importance of proxy access eligibility requirements, both for companies as they design and enforce such requirements, and for potential nominating shareholders as they plan their interactions with the companies they invest in.

Despite the rapid rate of proxy access adoption over the past two years, we continue to believe that proactively adopting proxy access does not immunise a company from a future proxy access proposal on more 'shareholder-friendly' terms and does not grant a company significantly greater freedom in choosing proxy access terms given that a relatively strong market consensus has developed on most terms. We also note that some market observers have commented that while the rapid adoption of proxy access should be applauded, the adoption of proxy access by-laws has been limited to the 'low-hanging fruit' (ie, those companies where there is least governance need for it) and has not made it to the companies whose shareholders, some believe, could most benefit from proxy access.

In the past few years we have also witnessed a rise in gender pay disparity shareholder proposals. While these proposals are not new, we believe that we may be approaching a tipping point. In April 2017, the NYC Comptroller announced that it had entered into settlement agreements with six healthcare and insurance companies (under which these companies agreed to disclose how they address gender pay equity) and that it had made similar proposals at three other insurance companies which would be going to a vote. While the NYC Comptroller has yet to announce a far-reaching campaign, we suspect that the success of this limited campaign and the prominence of gender-related issues generally (including the reaction to State Street's installation of the 'fearless girl' statue) could prompt others, if not the NYC Comptroller, to commence a broader effort to encourage companies to disclose information related to gender pay disparities or to make other gender-diversity related demands.

Cybersecurity

In March 2017, the Cybersecurity Disclosure Act of 2017 was introduced in the Senate. Similar to the 2015 version of this bill, the current bill would require the SEC to issue rules requiring companies to disclose in their annual reports whether any director has expertise or experience in cybersecurity and, if not, to disclose 'what other cybersecurity steps taken by the reporting company were taken into account by such persons responsible for identifying and evaluating nominees for any member of the governing body, such as a nominating committee'. The new SEC Chairman, Jay Clayton, who in private practice advised companies on cybersecurity matters, has publicly supported the bill. It is still too early to tell whether the current version of the bill will be more successful than the 2015 version, and as we noted last year, implementation in any event would likely not occur for years. However, we do not anticipate the issue of board fluency with cybersecurity matters going away. Due to the headline grabbing nature of data breaches, companies are well advised to regularly discuss cybersecurity at the board level and consider experience in overseeing cybersecurity matters to be a valuable credential for board membership.

Executive compensation

Dodd-Frank: executive compensation rulemaking at a standstill

Last year it was widely expected that the SEC would issue final rules implementing the clawback rule and the 'pay versus performance' and hedging disclosure rules of the Dodd-Frank Act. The SEC had proposed rules on these topics in 2015. In brief:

- the 'clawback' rule would require companies to implement clawback policies to recover incentive compensation received by current or former executive officers in the event of certain financial restatements;
- the 'pay versus performance' rule would require companies to provide in their SEC disclosure a new table, covering up to five years, that shows the relationship between compensation actually paid to the CEO and other named executive officers, to cumulative total shareholder return (TSR) of the company and its peer group; and
- the hedging rule would require companies to disclose whether employees, officers or directors are permitted to hedge the company's equity securities.

In addition, last year the consortium of regulators mandated by the Dodd-Frank Act to jointly issue guidelines or regulations that prohibit incentive compensation that the regulators determine encourages inappropriate risks by covered financial institutions reproposed a rule that was significantly more prescriptive than the rule that was originally proposed in 2011.

Most do not expect the Trump Administration to push for finalisation of any of these rules, especially given the perception that they are inconsistent with President Trump's Executive Order setting forth the core principles regulating the financial system, as well as the possibility that some of these rules will be amended or eliminated by the Financial Choice Act.

Say-on-pay

The fate of the already finalised say-on-pay and pay ratio disclosure rules is also unclear. While the former has been targeted for revision by the Financial Choice Act so that a shareholder vote would only be triggered when material changes are made to the compensation of an issuer's executives, since the rule was finalised in 2011 it has become well-accepted corporate governance practice. Additionally, many companies view the say-on-pay vote as a safety valve that allows shareholders to express their disapproval with executive pay practices without voting against incumbent directors. Given the support that the practice has with institutional investors and the advisory nature of the votes, we are sceptical that the say-on-pay rules will be meaningfully revised, at least in the short term.

Pay ratio disclosure

The prognosis for the pay ratio rule is less clear. Adopted in 2015 following more than 287,000 comments from the public, the final rule requires the following disclosures: median annual total compensation of all employees (not including the CEO); the annual total compensation of the CEO; and the ratio of the median annual total compensation of all employees to the annual total compensation of the CEO. While the rule is final, the compliance date begins in 2018 for companies with a fiscal year ending on 31 December and thus, unlike say-on-pay, the disclosure is not part of existing market practice.

In February 2017, then-acting SEC Chairman Piwowar asked for public comment on any 'unexpected challenges' that issuers have experienced as they prepare for compliance and whether any relief is needed. Comments to date mirror the criticism the rule faced prior to finalisation: that it imposes a substantial administrative burden on issuers and that the scope of individuals required to be included in the calculation is overly broad. It will be interesting to see whether the SEC opts to repeal the final rule or whether the rule will be modified to address the latest round of comments. At a minimum, the SEC may push back the compliance date to prevent unnecessary spending by issuers as they prepare to make the disclosures in 2018. Notwithstanding a March 2017 letter from several US Senators to Mr Piwowar, opposing any delay in the implementation of the pay ratio rule and a request by four Senators that Mr Piwowar be investigated for exceeding his authority by reopening the comment period, a delay is still possible. We also think it will be interesting to see if the SEC or other cities will be influenced by the decision of the city of Portland, Oregon to impose a surtax on companies where the pay ratio exceeds 100:1, with an additional surcharge where the ratio exceeds 250:1.

Clawbacks: enforcement under Sarbanes-Oxley and a push toward private ordering

Despite the presumed demise of the Dodd-Frank Act clawback rule, we expect to see an increased focus on the clawback of executive compensation. We predict that the source of this focus will be twofold: SEC enforcement actions and the scope of misconduct covered by existing company clawback policies. Section 304 of the Sarbanes-Oxley Act authorises the SEC to force a CEO or CFO to reimburse the company if incentive- or equity-based compensation was received during the 12 months following the issuance of misstated financial statements. While the scope of this tool is narrower than the rule proposed under the Dodd-Frank Act (it is limited to the CEO and CFO versus all executive officers and requires the SEC to demand a clawback instead of the company) this provision has become a potentially powerful tool for the SEC. As we noted last year, since the passage of the Sarbanes-Oxley Act in 2002, the clawback standard under section 304 has evolved from a fault-based standard to a strict liability approach. In August 2016, this approach was supported by the Ninth Circuit in *SEC v Jensen*, where the court found that section 304 allows the SEC to 'seek disgorgement from CEOs and CFOs even if the triggering restatement did not result from misconduct on the part of those officers'. We will be interested to see whether this endorsement will embolden the SEC to increase the frequency with which it brings clawback actions where neither the CEO nor the CFO committed the misconduct that triggered the restatement.

For many companies, the retail sales practices at Wells Fargo highlighted the importance of clawback policies. Wells Fargo used its policy to claw back millions following the revelation of the use of fake accounts and again after the completion of an independent investigation. While the size of the clawback attracted headlines, a closer look revealed that the 'clawback' was limited to compensation not yet paid to the CEO and the former executive responsible for the business division, prompting some to query whether the market standard on clawback policies needed to be expanded to empower companies to claw back compensation already paid in order for such policies to serve as a more effective deterrent for corporate malfeasance.

In this regard, recent research by Willis Towers Watson found that the clawback policies of most companies mirror the Sarbanes-Oxley section 304 standard and are only triggered following a material financial restatement, with large banks being the exception with policies that cover a broader range of actions and consequences, including misconduct that might cause reputational harm or a material failure of risk management. At least two companies will face shareholder proposals during the 2017 proxy season requesting that these companies broaden the scope of their existing policies. In the case of one company, the proposal urges the company to go beyond 'willful misconduct' and cover negligent or supervisory failures. We expect that the combination of the increasing validation of the SEC's strict liability interpretation of section 304 and the public scrutiny of clawback policies following the events at Wells Fargo will lead some companies to stress-test their existing policies and consider what should happen under potential misconduct scenarios.

Whistleblowers and confidentiality agreements

The scope of the anti-retaliation protections under the Dodd-Frank Act continues to divide the federal courts. As we reported last year, in 2015 the Second Circuit determined that employees are entitled to protection if they report securities-related wrongdoing internally without also reporting such misconduct to the SEC, which is at odds with a 2013 Fifth Circuit decision. In March 2017, the Ninth Circuit joined the Second Circuit and ruled that the Dodd-Frank Act covers employees who report concerns internally. The conclusion of the Second and Ninth Circuits potentially expands the scope of employer liability and reinforces the need for companies to create and enforce clear internal reporting procedures. We continue to believe that this issue will eventually find its way to the Supreme Court, given the growing circuit split and the ambiguity it creates for company policies and potential liability. We also note that the Financial Choice Act proposes to limit the scope of whistleblower awards by prohibiting co-conspirators from receiving such awards.

Following the first SEC enforcement action regarding confidentiality agreements that impede whistleblowing activity protected by the Dodd-Frank Act, we pointed to this issue as a possible area of focus of the SEC. We suggested that many companies would and should view the 2015 action as incentive to review their codes of conduct, company policies and employment agreements to ensure they contain express carveouts for reporting potential securities laws violations to, and cooperating with, regulators and law enforcement. Our prediction has been confirmed by the SEC. In an interview with the *Wall Street Journal*, the Chief of the SEC's Office of the Whistleblower stated that this issue 'is going to remain a focus of my office in 2017 and I expect that you will see additional cases brought under this authority'. While the recent enforcement actions implicated a wide range of companies (from Anheuser-Busch InBev to BlackRock), the message is consistent and clear: company policies, severance and other agreements that may be perceived as chilling the willingness of individuals to communicate directly with the SEC regarding possible securities law violations and come forward to the SEC will not be tolerated. Further, the Anheuser-Busch InBev inquiry illustrates that a formal company policy of encouraging whistleblowers will not cleanse an agreement that seeks to limit communications with the SEC. We will be interested to see whether the Trump Administration will continue to prioritise such actions.

Europe

Required environmental, social, employee and diversity disclosure

Starting in 2018, public interest companies (which includes large EU-listed companies, banks and insurers) with over 500 employees must include a non-financial statement in their annual report covering their policies and the main risks and outcomes relating to the following topics: environmental; social and employee; respect for human rights; anti-corruption and bribery issues; and diversity in their board of directors. This obligation stems from a December 2014 EU directive, which EU member states were required to implement by December 2016. In addition, under the directive, the relevant companies must include a description of the diversity policy applied to the company's administrative, management and supervisory functions with regard to age, gender, and educational and professional background. This description must include the objectives of the diversity policy, its implementation and results during the course of the reporting period. If a company does not have a diversity policy, the company must explain the lack of such a policy. The directive also requires that the European Commission provide non-binding guidelines to assist companies covered by the directive in the preparation of these new disclosures. In January 2016, the European Commission launched a four-month public consultation on the guidelines in an effort to receive input from stakeholders. The non-binding guidelines were scheduled to be released in spring 2017.

In recent years, ESG-related shareholder proposals have become increasingly frequent in the US. We are interested to watch how this newly required disclosure in the EU influences and inspires shareholder proposals in the US.

Shareholder rights in EU companies

In March 2017, the European Parliament voted to approve amendments to the existing EU Shareholders' Rights Directive. The directive applies to companies that have their registered office in an EU member state and whose shares trade on an EU regulated market. Under the new rules, shareholders of EU listed companies will have the right to vote on the remuneration awarded to company directors, first through a vote on the remuneration policy which lays down the framework within which remuneration can be awarded to directors, and second through a vote on the remuneration report describing the remuneration granted in the prior financial year. These rules are intended to enable a stronger link between executive remuneration and company performance. The vote on the remuneration policy will in principle be binding; however, EU member states will have the option under the new rules to opt for a non-binding advisory vote.

The new directive would also enable companies to identify their shareholders more easily and introduce rules that would make it easier for shareholders to exercise their rights, including the right to participate and vote in general meetings. Institutional investors and asset managers will also be required to develop and publicly disclose a policy describing how they integrate shareholder engagement in their investment strategies or explain why they have chosen not to do so. This will place onto an EU statutory footing what some countries already require through stewardship codes (such as the UK Stewardship Code).

The new directive was formally adopted by the European Council in May 2017 and EU member states have until 10 June 2017 to transpose the new requirements into national law. Because the UK may not be part of the EU by the time of that deadline, we do not yet know whether the UK will continue to apply this and other European legislation.

UK: narrative reporting on the impact of referendum to leave the EU

Following the referendum vote in favour of the UK leaving the EU, the Financial Reporting Council (FRC) provided guidance on how companies should approach the disclosure of the effect of Brexit in the narrative reporting section of their financial reports. While the FRC acknowledged that Brexit would not impact all businesses to the same extent, the FRC emphasised the need for high-quality narrative disclosures that convey management's view on the outlook of the business. The July 2016 guidance encouraged companies to consider the effect of Brexit, and its associated risks and uncertainties, on their business models and markets in which they operate. The FRC cautioned against the use of boilerplate disclosures. Although the impact of Brexit remains uncertain, the FRC guidance should be a reminder to all companies that while they are not expected to be fortune tellers, companies should be providing disclosure that is timely, informative and increasingly company-specific as the economic and political effects of Brexit become more certain.

UK: continued focus on executive remuneration

All signs point towards executive remuneration remaining in the spotlight in 2017. Last year, shareholders at three UK companies voted against executive pay reports presented for non-binding shareholder advisory approval, and shareholders at one UK company voted against the executive pay policy presented for binding shareholder approval. Approximately half of all FTSE 350 companies are expected to submit their executive pay policy to a binding vote in 2017. Binding votes on executive pay policies are required at least every three years for UK-incorporated listed companies, and in 2017 these votes come amid both UK government and institutional investor focus on excessive executive pay. Any vote against the executive pay policy by shareholders would mean that a company would have to continue to use its existing shareholder-approved executive pay policy.

In July 2016, shortly after becoming Prime Minister, Theresa May spoke of the 'unhealthy and growing gap between what [big] companies pay their workers and what they pay their bosses' and suggested that binding shareholder votes on remuneration should occur every year, not every three years as is currently the case. A wide-reaching green paper was later released by the UK government in November 2016 soliciting feedback on a number of issues related to corporate governance reform, including numerous proposals to ensure executive pay is better aligned with a company's long-term performance. Beyond increasing the frequency of binding votes on the executive pay policy, the green paper presents a number of reforms for discussion, including:

- requiring company pay policies include a cap on annual pay and requiring a binding vote if actual pay exceeds the cap;
- making all or some elements of the executive pay report subject to a binding vote;
- introducing stronger consequences for a company losing its annual advisory vote on the executive pay report;
- requiring institutional investors to disclose their votes on executive pay;
- facilitating and encouraging retail investors to exercise their individual right to vote and publicising the voting decisions of individual investors as a group; and
- requiring the disclosure of the pay ratio between the CEO and wider workforce.

The UK government is expected to publish the results of the consultation later in 2017. With the UK general election scheduled to take place in June 2017, the make-up of the next UK government is uncertain, however, we fully expect corporate governance reform and executive pay to remain a key area of focus.

Institutional investors are joining the chorus against perceived excessive executive pay with a number of institutional investor bodies and investors publishing policies or voting guidelines setting out their expectations around executive remuneration for 2017.

In January 2017, BlackRock sent a letter to the chairmen of all companies in the FTSE 350, demanding an end to executive pay that outpaces that of ordinary employees. The letter is critical of the use of benchmarking as a justification for generous compensation packages and calls for companies to provide more fulsome disclosure on their arrangements with compensation consultants. This letter comes after BlackRock announced before Parliament in December 2016 that it would vote against remuneration committee chairmen who fail to rein in executive pay.

Separately, in October 2016 the Investment Association, an association of institutional investors who manage over £5.7 trillion on behalf of clients in the UK and around the world, published revised principles of remuneration together with an open letter to the FTSE 350 outlining new shareholder expectations on executive pay that seek for these companies to, among other things:

- better justify executive pay and any increases;
- include maximum limits on each element of remuneration (including salary) in remuneration policies;
- disclose performance conditions for annual bonuses (or retrospective disclosure where such conditions are commercially sensitive);
- disclose pay ratios between the CEO and median employee;
- justify differences between pension contribution rates for executives and the general workforce; and
- implement clawback policies that allow for the forfeiture of unvested awards and recovery of monies already paid in circumstances that are clearly disclosed to shareholders.

Given the uncertainty that surrounds some of the executive compensation provisions of the Dodd-Frank Act, we will be interested to see whether institutional investors will seek to fill the void of US government regulation by exercising their vote to force SEC-regulated companies to justify and provide increased disclosures on their executive pay.

UK: corporate governance and stewardship codes

In February 2017, the FRC announced that it will undertake a 'fundamental review' of the UK Corporate Governance Code. This willingness to refresh the Corporate Governance Code comes as no surprise in light of the UK government's focus on corporate governance, illustrated by the corporate governance green paper released in 2016. As with prior updates to the Corporate Governance Code, the FRC will seek input from a range of stakeholders representing a wide variety of sectors. This consultation is expected to occur in the second half of 2017. In addition, the FRC announced that it is considering possible revisions to the UK Stewardship Code in 2018.

UK: diversity on boards and beyond

In November 2016, two UK government-sponsored commissions released their findings on the ethnic and gender diversity of UK boards. Both reports set voluntary targets and set forth recommendations for consideration by UK companies.

The Parker Review, which reports on the ethnic diversity of UK-listed companies, proposes that by 2021 each FTSE 100 board and by 2024 each FTSE 250 board should have at least one director of colour and these companies should identify and present for consideration at least one candidate of colour for each board vacancy. The Parker Review provides a two-prong path to reaching this goal: first that companies should focus on developing a pipeline of ethnically diverse candidates through mentorship and encouraging such candidates to assume leadership positions internally and with external organisations, and second the UK government and regulatory bodies should require companies to disclose their efforts to increase ethnic diversity on the board and within the organisation generally. As of March 2016, only about 1.5 per cent of the total director population among the FTSE 100 are UK citizen directors of colour. The Parker Review was published in consultation format and a report containing the final recommendations is expected to be published later in 2017.

The Hampton-Alexander Review follows up on the Davies Review for Women on Boards which in October 2015 proposed a voluntary target of a minimum of 33 per cent women's representation on the boards of FTSE 350 companies by 2020. The Hampton Alexander Review goes beyond boards and addresses the underrepresentation of women in leadership positions of FTSE 350 companies and proposes a voluntary target of a minimum of 33 per cent women's representation on the executive committees and direct reports to the executive committee of FTSE 350 companies by 2020. To reach these targets, the Hampton Alexander Review calls for a combination of voluntary disclosures by FTSE 350 companies along with the implementation of mandatory disclosure requirements by the UK government and the FRC through an amendment to the UK Corporate Governance Code. In addition, the Hampton Alexander Review calls for institutional investors to include gender balance in their assessment of corporate governance by, among other things, implementing a clear voting policy on gender balance that could include voting against the re-election of the chair of the board (or chair of the nomination committee) when a company does not have sufficient measures in place to address gender imbalance.

We are particularly interested to see how institutional investors will respond to the call by the Hampton Alexander Review to use their vote to address concerns regarding gender diversity and whether this will embolden institutional investors to exercise such influence beyond FTSE-listed companies. Given the many variables that impact a company's ability to promote women and ethnically diverse candidates, we hope that such voting policies are nuanced and provide sufficient discretion.

In January 2017, the Pensions and Lifetime Savings Association (PLSA) published its 2017 corporate governance policy and voting guidelines where it recognised the positive progress in recent years towards meeting the Davies Review target of 33 per cent of women on boards but indicated that there is still considerable room for improvement in some cases. The PLSA noted that shareholders could consider a vote against the chair (or chair of the nomination committee) if there was no clear evidence that diversity is being sufficiently considered by the board, with progress towards the targets of 33 per cent women representation and one director of colour on the board acting as useful benchmarks.

It is also worth noting that, starting in 2018, large UK-listed companies will be required to include in their annual corporate governance statement a description of their diversity policy and the policy's objectives, how it is implemented and the policy's results in the reporting period (or an explanation of why the company does not have a diversity policy).

Asia

Hong Kong: dual-class structures

The debate regarding dual-class shares is not confined to the United States. Less than two years after the board of the Hong Kong Securities and Futures Commission (SFC) brought the market consultation on dual-class shares to an abrupt halt, it appears that the SFC is prepared to take a second look at this issue. As we have chronicled, the drive for dual-class structures on the Hong Kong Stock Exchange (HKEx) came after Alibaba's decision to launch its IPO, the largest in history, on the New York Stock Exchange instead of on the HKEx, after the HKEx refused to permit the use of weighted voting rights in the company's control structure. Following the Alibaba IPO, the HKEx issued a concept paper to solicit investors' views on permitting the use of dual-class structures with this paper to be followed by a second round of market consultations, when the SFC announced that it did not support primary listings with dual-class structures. After this unprecedented announcement, many (including ourselves) concluded that we would not see dual-class listings on the HKEx in the near term. However, in late 2016, the chief executive of the SFC surprised many by stating that the SFC had not ruled out the possibility of reviving discussions regarding dual-class share structures. This apparent reversal came after Alibaba announced that it would consider taking its online payment unit Ant Financial public in Hong Kong 'only if [Alibaba] think[s] the city is ready'. In early 2017, HKEx announced that it would issue a new consultation paper to solicit opinions on the establishment of a new trading board and that such discussions would cover the possible inclusion of dual-class structures on the new board.

As we noted last year, in halting the initial consultation on dual-class shares the SFC acknowledged that the discussion was spurred by competition from US exchanges for the listing of mainland China businesses. It also appears that another rival of the HKEx, Singapore, is poised to introduce dual-class shares after its Prime Minister approved the introduction of such structures.

Hong Kong: enforcement under the SFC and HKEx

Last year witnessed an increase in enforcement actions brought by the SFC and the HKEx. Based on recent statements by both regulators, it appears we can expect this increased activity will continue through 2017.

In December 2016, after a five-year break, the SFC re-launched its *Enforcement Report* newsletter and announced a new enforcement approach which will include a focus on high-priority cases that pose the 'greatest risk' to the Hong Kong markets and the use of specialist teams to cover such cases. The newsletter also highlighted enforcement priorities of the SFC with the top priority being corporate fraud and misfeasance, with such misconduct being linked to the loss of billions in market capitalisation and damage to the integrity and reputation of the Hong Kong markets. This new approach is in line with a speech given by the new head of the Enforcement Division of the SFC, Thomas Atkinson, in which he listed 'company-related issues' at the top of the SFC's priorities, noting that these issues often relate to companies located in China which present investigatory challenges since most of the evidence and witnesses are located in mainland China and not Hong Kong. His remarks ended by noting recent collaboration with mainland Chinese regulators with the aim of building a long-term relationship between the regulators of both jurisdictions.

In February 2017, the HKEx released a policy statement on the enforcement of the Listing Rules. While the policy statement unsurprisingly highlights the rationale behind enforcement: deterrence, education of the market, cultivation of a compliance culture and enhanced corporate governance, it also includes specific reminders to the directors and senior management of listed companies. These reminders, which include, among other things, an articulation that directors are expected to fulfil fiduciary duties and emphasise the importance of training and education strongly suggest that the HKEx is concerned that some of their issuers are not aware of the basics of corporate governance which are incorporated in the Listing Rules, with such concern primarily directed at mainland Chinese companies (which would be consistent with the remarks of the SFC enforcement head). We will be interested to see how these two regulators utilise their enforcement powers to address and educate listed companies and whether this will require closer collaboration with mainland Chinese authorities.

Japan: further implementation and refinement of reform

It has been two years since the implementation of the Corporate Governance Code in Japan. This mandatory code requires all companies listed on Japanese securities exchanges to submit corporate governance reports detailing their compliance with the code or explaining the reason for their non-compliance. The level of compliance by listed companies has increased since the inaugural reports were released in 2015. This progress is reflected in the December 2016 analysis by the Tokyo Stock Exchange of more than 2,500 governance reports, which found that 20 per cent (up from 11 per cent in 2015) of companies were in full compliance with the principles of the code. Of the companies that were not in full compliance, approximately 65 per cent (slightly down from 2015) were reported to be in compliance with at least 90 per cent of the principles. One principle which continues to have a high non-compliance rate is the obligation to evaluate the board and provide a summary of such evaluation (nearly 45 per cent of companies explain non-compliance with this principle). While such evaluations are commonplace in the US, this practice was not prevalent among Japanese companies prior to the implementation of the Corporate Governance Code. A lack of board evaluations may be attributable to the famously deferential Japanese corporate culture.

One of the practices closely associated with this culture of deference is the target of ISS Japan proxy voting guidelines. *Sodanyaku* or *komon* involves former senior executives (often former company presidents) serving in an advisory role for several years after the end of their formal employment by the company. This practice attracted headlines during the Toshiba accounting scandal, which revealed the behind-the-scenes influence of the former chairman on the current chairman of Toshiba. The presence of these senior advisers is thought to limit the willingness of current executives to make changes contrary to the policies established by the senior adviser out of deference to the adviser. While ISS admits that its recommendation to vote against the proposal of amendments creating new senior adviser positions will not impact most companies (since most already have such policies in place), we will see whether this policy will encourage companies to either abandon this practice or provide further disclosure about the role of such advisers.

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Japan: shareholder activism

The number of activist campaigns increased from nine in 2015 to 15 in 2016 with both foreign and Japanese activist funds increasingly targeting small-cap and mid-cap companies. We believe this trend is attributable to the Stewardship Code, which seeks to encourage shareholder engagement; recent high-profile successes such as Daniel Loeb's engagement with Seven & I Holdings (the parent of Seven-Eleven Japan); and the requirement under the Corporate Governance Code that companies annually evaluate and disclose the objective and rationale for cross-shareholding structures. Cross-shareholding structures exist when Japanese companies own controlling or substantial stakes in each other, such as between banks and their clients, insurance companies and policyholders and companies in the same sector or group. Adopted to strengthen the ties between companies, this practice makes it difficult for activists to gain support from such shareholders that often have close ties to management and are not inclined to support activist campaigns. While it is still too early to tell the pace with which this cross-shareholding disclosure requirement will result in the unwinding of these positions, we note one recent example of such unwinding in the February 2017 announcement that Fujitsu's biggest shareholder, Fuji Electric, plans to sell approximately US$1 billion of the electronics maker's stock, and Fujitsu plans to sell its 10 per cent stake in Fuji Electric as part of a plan to unwind their cross-shareholdings.

Brazil

As we previewed last year, the Brazilian Securities and Exchange Commission (CVM) led representatives from 11 self-regulatory capital market entities in developing a unified corporate governance code. Released in November 2016, the unified code follows the well-travelled 'comply or explain' format and covers issues such as board of director duties, remuneration and incentive structures, internal controls and conflicts of interest. The CVM is currently in the process of updating its rules in order to incorporate the principles and practices of the unified code.

In addition, the Novo Mercado listing of the BM&F Bovespa stock exchange, a listing created in 2000 and composed of 130 companies with 'higher' corporate governance standards, is in the process of tightening its regulations. Announced in March 2017, the proposed changes would require companies listed on the Novo Mercado to, among other things, have at minimum the greater of 20 per cent or two independent directors, establish an audit committee that includes at least one independent board member and one expert (with such committee producing an annual report), and maintain a minimum 25 per cent or 15 per cent free float.

Finally, in October 2016, the Associação de Investidores no Mercado de Capitais, an association of Brazilian institutional investors, released the country's first stewardship code. The code calls on investors to carefully manage and monitor the securities held for the benefit of others by operating in accordance with seven principles which include the implementation and disclosure of a stewardship programme, considering ESG factors when making investment decisions and the transparent exercise of voting rights through adequate disclosure and explanation of votes cast.

Austria

Eva Fischer

Wolf Theiss

Sources of corporate governance rules and practices

1 Primary sources of law, regulation and practice

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

The primary sources of law relating to corporate governance in Austria are:
- the Stock Corporation Act;
- the Commercial Code;
- the Takeover Act; and
- the Stock Exchange Act.

In addition, the Austrian Corporate Governance Code, prepared by the Austrian Working Group for Corporate Governance, provides a set of voluntary rules for good governance, distinguishing between L-rules (mandatory legal requirements), C-rules (comply or explain) and R-rules (recommendations). The Code is available in German and English on the website of the Working Group: www.corporate-governance.at. The latest amendment is dated January 2015.

According to the listing requirements for the prime market of the Vienna Stock Exchange, companies trading on the prime market of the Vienna Stock Exchange need to publish a declaration of adherence or non-adherence with respect to the Austrian Corporate Governance Code in their annual report and are required to publish such declaration on their website. EU companies may opt to adhere to another corporate governance code accepted in the EU.

Furthermore, the Commercial Code prescribes that joint-stock companies listed on a regulated market or companies having issued securities (other than stock) on a regulated market, and the stock of which are knowingly traded on a multilateral trading system, have to issue an annual corporate governance report with respect to the Austrian Corporate Governance Code or another code of the applicable listing place. The report also needs to state where such code is publicly available and in case of non-adherence to a code, reasons therefore need to be given.

Also non-listed companies may, and frequently do, voluntarily adhere to the Austrian Corporate Governance Code.

2 Responsible entities

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

The main governmental body responsible for enacting federal statutes relating to corporate governance is the Austrian federal parliament. Other influential bodies include the Austrian courts and the Austrian Working Group for Corporate Governance.

Enforcement of corporate governance rules primarily takes place before the Austrian courts via litigation. Furthermore, the Austrian Financial Market Authority has certain powers of supervision and enforcement relating to securities trading and listed entities.

The only noteworthy stakeholder is the Austrian Shareholder Association (www.iva.or.at) which, inter alia, represents shareholders in shareholders' meetings and in judicial and extrajudicial disputes, submits opinions on legislative proposals and organises road shows.

The rights and equitable treatment of shareholders

3 Shareholder powers

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

Shareholders may not directly appoint or remove the members of the management board, nor may they influence the management of the company. They may only exercise indirect control via the supervisory board, whose members are elected by the shareholders' meeting. (For employee participation on the supervisory board, see question 33.)

The members of the management board of an Austrian joint-stock corporation are appointed by resolution of the supervisory board for a maximum term of five years. Re-election is possible but subject to the written confirmation of the chairman of the supervisory board. The resolution needs to be passed by a double majority: a majority of votes cast, as well as a majority of the members elected by the shareholders (see question 33 with respect to employee participation on the supervisory board), thus preventing the employee representatives and a minority of shareholders teaming up and electing the members of the management board. The articles of association may provide for higher majorities but may not derogate from this double majority principle.

The members of the management board may be revoked from their position prior to the expiry of their term of service by resolution of the supervisory board only in three exceptional cases: severe breach of duty, habitual incompetence, and a vote of no confidence of the shareholders' meeting. The articles of association may neither increase nor decrease the reasons for revocation. The principle of double majority (see above) is also applicable for the revocation of members of the management board.

The members of the supervisory board are appointed by resolution of the shareholders' meeting with a simple majority (unless the articles of association provide for a higher majority). Members of the supervisory board may only be appointed for a maximum term ending with the shareholders' meeting deciding on the discharge from liability for the fourth year of office (the year of appointment is not taken into account), which results essentially in a term of up to five years. Members may be re-elected.

The members of the supervisory board may be revoked by resolution of the shareholders' meeting at any time before the expiry of their term of service and without stating any reasons. By law, the majority for such resolution is 75 per cent of the votes cast. The articles of association may provide for a different majority (higher or lower; minimum: simple majority).

4 Shareholder decisions

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

Certain important decisions are reserved to the competence of the shareholders' meeting, the most important of which are listed below:
- decisions on amendments of the articles of association;
- appointment and revocation of the members of the supervisory board (elected members, not members delegated by the works council – see question 33);
- lodging of claims against the members of the management board or members of the supervisory board;
- approving of the annual financial statements if the management board and the supervisory board refer this matter to the shareholders' meeting, or if the supervisory board has not approved the financial statements submitted by the management board;
- decisions on the distribution of profits;
- releasing the members of the management board and the supervisory board from liability for the financial year;
- appointment of the auditor for the financial year;
- decisions on an ordinary increase of the share capital or on a reduction of the share capital;
- transformation of a joint-stock company into a limited liability company;
- transformation of the company to the major shareholder, into a general partnership or limited partnership;
- decisions on a merger;
- decisions on spin-offs;
- decisions on the dissolution of the company;
- decisions on the squeeze-out of minority shareholders;
- decisions on an issuance of convertible bonds;
- decision on the transfer of all assets to another entity or person;
- profit-sharing agreements if they relate to at least 75 per cent of the company's profit; and
- business lease agreements according to which the company leases its business to another entity or person or according to which the company is running its business on account of another entity or person.

The articles of association may reserve further decisions to the shareholders' meeting.

The concept of non-binding resolutions is not common in Austria.

5 Disproportionate voting rights

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

In principle, every share grants a voting right to the shareholder proportionate to the participation in the share capital of the joint-stock corporation.

However, the articles of association may exclude the voting rights in relation to preferential shares, which shall not amount to more than one-third of the total share capital. Note that only the voting rights are excluded. The preferential shareholder enjoys all other shareholder rights. As compensation for such voting right exclusion, preferred shares entitle the shareholder to a preferential right for dividends.

Furthermore, the articles of association may limit the voting rights of a shareholder holding multiple shares by implementing voting caps (ie, the voting rights of a shareholder above a certain capital threshold or nominal value are suspended) or voting power adjustments (ie, shares of a certain nominal value grant full votes, while shares exceeding such threshold only have decreased voting powers).

Shares granting multiple voting rights (ie, more votes than their shares carry pro rata to their capital participation) are not permitted.

In its C-rule 2, the Austrian Corporate Governance Codex also stipulates that shares are to be construed in accordance with the 'one share, one vote' principle.

6 Shareholders' meetings and voting

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

Every shareholder may participate in shareholders' meetings of the company. In relation to listed joint-stock corporations, shareholders who hold shares as of the end of the tenth day prior to the meeting may attend the shareholders' meeting. Bearer shares need to be deposited on the record date, which must be evidenced by a bank confirmation in relation to the securities account. Listed companies that have issued registered shares only may deviate from such rule and provide in their articles of association that the day of the shareholders' meeting shall serve as the record date. In relation to non-listed joint-stock corporations, shareholders registered in the register of shareholders as of the beginning of the meeting are permitted to attend; however, the articles may (and often do) provide that the record date for listed companies will apply (record date as of the end of the tenth day prior to the meeting).

Shareholders' meetings are convened by the management board of a joint-stock corporation. The publication of such convocation must be made on the 28th day prior to an ordinary shareholders' meeting at the latest, otherwise on the 21st day prior to a non-ordinary shareholders' meeting at the latest. The articles of association may provide for longer periods, but not for shorter ones.

In shareholders' meetings, shareholders may exercise their rights either in person or by appointing a proxy acting on their behalf via power of attorney. The power needs to be signed (personal signature or secure electronic signature), or may be granted in text form (email, telefax) if the articles of association so provide. In the case of listed companies, the text form is always permitted. Furthermore, listed companies need to provide means of electronic communication for the submission of powers of attorney. If the articles of association do not provide for other means, the submission via telefax is admissible (minimum requirement).

Apart from participation in person, shareholders may also participate by means of electronic communication (eg, video communication, distant voting, broadcasting) if the articles of association so provide. Distant voting is defined as participation in the shareholders' meeting from any location via audio and possibly also visual two-way communication in real time. The shareholders' meeting takes place in a closed internet forum, where the shareholders can participate via webcam and microphone over a computer or other device and have the ability to participate (a virtual meeting). The shareholders' meeting of a listed joint-stock corporation may also be publicly broadcast if permitted by its articles of association.

Written shareholder resolutions (ie, passed outside of a shareholders' meeting) are not permitted for joint-stock corporations.

7 Shareholders and the board

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

A shareholders' meeting must be called if so requested by shareholders that hold at least 5 per cent of the share capital. Furthermore, the shareholders must request the convocation in writing and submit the agenda and the respective proposals for resolutions for each point on the agenda. The shareholders must explain the reasons for their request. The articles of association may provide for a less strict form as to the convocation of the shareholders' meeting and may provide for shareholders holding a lower percentage of the registered share capital being entitled to call a shareholders' meeting. The shareholders requesting the convocation must have been holding the shares for a minimum period of three months before the filing of the request and they are obligated to hold the shares at least until the decision upon such request. Where neither the management board nor the supervisory board complies with the request of the shareholders to call a shareholders' meeting, the competent court may empower the shareholders who requested the meeting to convene the shareholders' meeting.

A similar regime applies with respect to agenda items: shareholders holding at least 5 per cent of the share capital may request that certain agenda items be presented to the shareholders at a certain shareholders' meeting. Any such request must be accompanied by draft resolutions and reasons. Again, the articles of association may provide for a lower percentage of the registered share capital being entitled to such right and again the shareholders must have been holding the shares for a minimum period of three months before the filing of the request. The request needs to be taken into account if received by the company at least on the 21st day prior to an ordinary shareholders' meeting, or on the 19th day prior to any other shareholders' meeting.

Shareholders holding at least 1 per cent of the share capital of a listed company may deliver to the company, with respect to each agenda item, a proposal for a certain draft resolution and may demand under certain circumstances that such draft resolution has to be made available on the company's website, together with the name of the proposing shareholder, the reason for proposing the resolution and the statement, if any, of the management or supervisory board on the proposed resolution. The articles of association may provide for a lower percentage of the registered share capital being entitled to such right. The request needs to be taken into account if received by the company at least on the seventh working day prior to the relevant shareholders' meeting.

Shareholders may not directly appoint or remove the members of the management board who are appointed by the supervisory board. Shareholders may only indirectly influence the appointment of members of the management board through control via the supervisory board, whose members are elected by the shareholders' meeting. See question 3.

There is no right of the shareholders of Austrian joint-stock corporations to request that the management board circulate statements by dissident shareholders.

8 Controlling shareholders' duties

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

Under Austrian law shareholders of a joint-stock corporation owe a duty of loyalty to the company in relation to the exercise of their voting rights. In particular, an abusive exercise of such voting rights is prohibited. On this basis a resolution of the shareholders' meeting may be challenged by filing a contesting action. If the resulting judgment by the court renders the resolution null and void, such judgment shall be binding on all shareholders and the members of the management board and the supervisory board. The management board must immediately file for registration of the judgment with the competent commercial register. The judgment must be registered with the commercial register if the reversed resolution was registered.

Austrian law also provides a duty of loyalty among the shareholders. Such duty applies to both majority and minority shareholders, but the scope of the duty of loyalty increases with the influence on the company. Hence, the duty of loyalty of a majority shareholder weighs heavier than the duty of loyalty of a minority shareholder. Whether a claim for damages for breach of the duty of loyalty can be brought depends on the circumstances, but is generally possible.

9 Shareholder responsibility

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

In principle, shareholders are not personally liable for the acts or omissions of a joint-stock corporation. Personal liability of shareholders may be triggered if shareholders voluntarily assume liability (eg, by providing a guarantee to the company) or if they are personally liable in their capacity as a statutory body of the company (eg, if a shareholder is also a member of the management board). Only in very exceptional circumstances may the corporate veil be pierced.

Corporate control

10 Anti-takeover devices

Are anti-takeover devices permitted?

From the time the target company becomes aware of the bidder's intention to make a bid and until the publication of the results, and, if the takeover goes ahead, until the bid has been completed, the management board and the supervisory board of the target company may take concrete measures that might prevent or affect the bid only with the approval of the shareholders' meeting. This applies in particular to the issuance of securities that may prevent the bidder from acquiring control over the target company. However, the target company's management board is explicitly entitled to search for, approach and negotiate with other potential bidders ('white knight'). However, measures that the management board or the supervisory board of the target company were already obligated to carry out when the target company became aware of the bidder's intention to make a bid do not require the approval of the shareholders' meeting.

11 Issuance of new shares

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

According to Austrian law, the management is not entitled to issue new shares without any prior shareholder approval. However, the shareholders' meeting may resolve upon an authorisation to the management board to increase the share capital of the company within a defined scope, the 'authorised capital'. Such resolution requires a vote of 75 per cent of the represented capital (unless the articles of association provide for a higher majority) and the scope of the authorised capital needs to be included in the articles of association. The authorised capital may not exceed half of the registered capital of the company at the time of the authorisation and any authorisation is limited to a period of five years but may be prolonged repeatedly by the shareholders' meeting. The actual issuance of shares based on the authorised capital has to be approved by the supervisory board in each individual case.

In general, shareholders have the right to subscribe to newly issued shares pro rata to their participation in the share capital. This subscription right may only be excluded by resolution of the shareholders' meeting (at least 75 per cent majority vote of the represented capital is required, but the articles of association may require a higher majority) and has to be justified by the facts of each individual case (eg, in the case of contributions in-kind). Such justification has to be explained by the management board in a written statement presented to the shareholders' meeting. The exclusion of subscription rights is deemed as justified by law in case of new issues for stock option schemes for employees, managerial staff or members of the boards of the company.

12 Restrictions on the transfer of fully paid shares

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

With respect to registered shares, the articles of association may provide for a share transfer to require the prior approval of the company (ie, the management board if the articles of association do not assign such consent right to the supervisory board or the shareholders' meeting). Such consent may not be unreasonably withheld (ie, a share transfer cannot be excluded altogether) and the articles of association may provide for specific important reasons when a transfer is not permissible.

The transfer of bearer shares cannot be excluded.

13 Compulsory repurchase rules

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

The possibility for compulsory repurchases is limited as there are only limited instances in which a joint-stock corporation may acquire own shares. These include the following:

- if it is required to prevent the company from severe and immediate damage;

- if the acquisition is made without consideration or by a credit institution in execution of a purchase order;
- in the course of a universal succession;
- on the basis of an authorisation from the shareholders' meeting that does not exceed 30 months if these shares are intended to be offered for acquisition to employees, executives, members of the management board or the supervisory board of the company or an affiliate;
- if minority shareholders are to be compensated if provided for by law; and
- on the basis of a shareholder resolution to redeem shares pursuant to the provisions governing a reduction in the share capital.

Special rules exist with respect to the acquisition of own shares by banks or via the stock exchange.

The principle of equal treatment of shareholders is applicable, which may be complied with by the acquisition or sale of own shares on the stock exchange or by public offering. The total amount of such repurchase is in certain cases limited to 10 per cent of the registered share capital. Own shares do not entitle the company to any associated rights, and generally need to be sold within certain time frames (one or three years from acquisitions, depending on the grounds of acquisition).

14 Dissenters' rights

Do shareholders have appraisal rights?

In case of a merger or split-off whereby the corporate form of the company is changed from a joint-stock corporation into a limited liability company or vice versa, or in case of transformation from a joint-stock corporation into a limited liability company or vice versa, shareholders who object to the transaction have the right to exit against adequate cash compensation. The compensation is to be paid either by the company (if the requirements for own shares are met, see question 13) or by another party (eg, another shareholder). In addition, every shareholder has the right to demand the competent court to scrutinise the appropriateness of the cash compensation.

The right to demand review of the cash compensation by the competent court is also granted to a minority shareholder in case of a squeeze-out, irrespective of any objection in the shareholders' meeting.

The responsibilities of the board (supervisory)

15 Board structure

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

The two-tier corporate structure consisting of the management board and the supervisory board is mandatory for all Austrian joint-stock corporations, irrespective of listing.

16 Board's legal responsibilities

What are the board's primary legal responsibilities?

The management board of an Austrian stock corporation consists of one or more members whose main competence and responsibility is the company's day-to-day business and the determination of the company's business policy in line with the articles of association of the company and any guidelines or rules of procedure. The joint-stock corporation is represented by its management board members in all matters. The management board is responsible for keeping all required books and records and must also prepare the annual financial statements and the annual report.

The supervisory board's main task and duty is to supervise the management board. For that purpose it may request a report from the management board concerning company matters at any time. Furthermore, the supervisory board is entitled to inspect and review all books and accounts of the company as well as its assets, including cash accounts and stock in trade.

The supervisory board is also obliged to review and inspect the company's financial statements, the proposed profit distribution and the annual report, and has to approve the company's financial statements. The supervisory board must report to the shareholders' meeting on these matters.

Certain important transactions (ie, transactions exceeding a certain amount or that are outside the ordinary course of business) of the management board require the prior approval of the supervisory board.

17 Board obligees

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

An Austrian stock corporation is generally represented by its management board. The management board (and also the supervisory board) must act in the best interests of the company, which includes the interests of the shareholders and the company's employees, as well as the interests of law and the public. The benefit for the company must outrank their own interest and they must not abuse their corporate authority.

18 Enforcement action against directors

Can an enforcement action against directors be brought by, or on behalf of, those to whom duties are owed?

Members of the management board and members of the supervisory board who violate their duties are jointly liable to the company to reimburse the company for any damage resulting therefrom. They may be released from their liability by providing evidence that they have employed the care of a prudent and conscientious business manager.

The supervisory board members are competent to represent the company in a liability action against members of the management board. However, the supervisory board is obliged to file a claim if:

- the shareholders' meeting so resolves with simple majority;
- a minority of shareholders holding at least 10 per cent of the share capital of the company requests the initiation of a claim and if such claims alleged by the minority are not obviously unfounded; or
- facts have been detected in the audit report that results in claims for compensation and a minority of shareholders holding 5 per cent of the share capital requests the initiation of a claim.

If a liability action is lodged against members of the supervisory board, the company is represented by the management board. Alternatively, the shareholders' meeting may appoint another representative.

Finally, third parties may bring liability actions against the members of the management board or the supervisory board if they may be held liable under general conditions that apply for a liability in tort (claims for damages require a damage that has been caused by an intentional or negligent action or omission). The company is jointly liable along with the respective member of the supervisory board or the management board. If the affected third party claims and receives indemnification from the company, the company is entitled to claim indemnification from applicable members of the management board or members of the supervisory board.

19 Care and prudence

Do the board's duties include a care or prudence element?

The members of the management board and the supervisory board must act with 'the care and diligence of a prudent manager' when operating the business of the company or supervising the management of the company, as applicable. Austrian law applies a general, objective diligence standard when testing a board member's liability. This means that each management or supervisory board member has to be capable of fulfilling his or her statutory duties, which depend on the nature and size of the business of the company. Thus, no member of the management board or supervisory board member may rely on his or her lack of qualifications as an excuse. The assessment as to whether a specific conduct violates a fiduciary duty is to be examined from an ex ante perspective.

20 Board member duties

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

In principle, the duties of individual members of the board do not differ. However, depending on the skills and experience of a member of the management board, certain tasks may be allocated to the sole responsibility of an individual member. Such allocation of tasks may be made in the articles of association or by decision of the supervisory board (eg, by adopting internal rules and procedures). Special skills or experience of a supervisory board member may be taken into consideration by adopting internal rules or establishing supervisory board committees. For more details see question 21.

21 Delegation of board responsibilities

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

Competences allocated by law to a specific corporate body (ie, management board, supervisory board, shareholders' meeting) may, as a matter of principle, not be referred to or delegated to another corporate body. Each corporate body may consult another corporate body upon its own initiative and request approval to any transaction within its competence. Furthermore, each corporate body may delegate within the corporate body certain tasks or fields of responsibility to an individual member or a committee as set out in the following:

Management board
Management tasks (eg, certain geographic areas, certain divisions or areas of business) may be allocated to the sole responsibility of individual members. Alternatively, all or certain tasks may remain with the management board (ie, full board) as a collective body. The articles of association or the supervisory board may define the fields of responsibility and assign such fields to individual members of the management board. There are no Austrian statutory provisions that predefine the fields of responsibility. Fundamental decisions of the management have to be reached by the management board as a collective body. The management board is also responsible for passing resolutions with regard to all items that are not explicitly assigned to a single member. In addition, each member can request that decisions on any item are subject to a resolution of the management board as a collective body. Finally the management board may also adopt internal rules of procedures (which, however, may not limit any responsibility of a member of the management board vis-à-vis third parties).

Supervisory board
The supervisory board may, by adopting its internal rules of procedure, establish supervisory board committees and define the scope of competence of the respective committees. As in case of the management board, fundamental decisions of the supervisory board must be passed by the supervisory board as a collective body (eg, the approval of the annual financial statements). An audit committee is mandatory for listed companies, as well as non-listed companies of a certain size ('very large companies'). For more details regarding the audit committee and any committees required according to the Austrian Corporate Governance Code, see question 25.

22 Non-executive and independent directors

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

Owing to the two-tier system, there is no distinction between 'non-executive' and 'executive' directors under Austrian law.

Only the Austrian Corporate Governance Code provides for independency criteria of the supervisory board members. According to C-rule 53, the majority of members of the supervisory board elected by the shareholders' meeting shall be independent of the company and its management board. A member of the supervisory board is deemed independent if said member does not have any business or personal relations with the company or its management board that constitute a material conflict of interests and is therefore suited to influence the behaviour of the member. The supervisory board shall define, on the basis of this general rule, the criteria that constitute independence and shall publish them in the annual corporate governance report. The Austrian Corporate Governance Code contains guidelines in an annex that serves as further orientation as regards independency criteria. The corporate governance report must clearly explain which members of the supervisory board fulfil the independency criteria.

23 Board size and composition

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

Austrian law does not define any personal competences or professional qualifications that a management board member or supervisory board member must have (note that special requirements apply with respect to certain regulated industries, for example, banks). However, case law has developed certain criteria and professional standards that management board members and supervisory board members must possess.

Each member of the management board or supervisory board must be capable of fulfilling his or her statutory duties (ie, to manage the company with the care and diligence of a prudent manager and to supervise the managing board and the conduct of its business, as applicable). Consequently, the requirements and professional qualifications for members of the management board or supervisory board depend on the nature and size of the business of the company. They must have the ability of recognising difficult legal and economic relationships and of assessing their impacts on the corporation, as well as recognising (contingent) risks for the company.

When appointing the members of the supervisory board, the shareholders' meeting must take due care to ensure the expertise and personal qualifications of the supervisory board members and a balanced composition with respect to the structure and the business of the company. Furthermore, reasonable attention is to be given to the aspect of diversity of the supervisory board with respect to the representation of both genders and age, and in the case of listed companies, also with a view to the internationality of the members. The shareholders' meeting and the supervisory board, as the case may be, must also ensure that no member of the supervisory board or the management board is considered for appointment who has been convicted by law for a criminal act that would compromise his or her professional reliability.

To some extent certain persons are excluded from different functions: management board members and employees of the company and management board members or directors of a subsidiary of the company cannot become supervisory board members. Individuals who are already members of the supervisory board of 10 (other) companies are also excluded. Furthermore, individuals who are already members of the supervisory board of eight listed companies are excluded from being on the supervisory board of another listed company. The position as chairman of the supervisory board is, for the purpose of determining the maximum number memberships, counted twice. The Austrian Corporate Governance Code provides in certain cases for stricter rules (eg, supervisory board members serving on the management board of a listed company may not hold more than four positions on supervisory boards (position of chairperson counts double) of stock corporations not belonging to the group).

The management board of an Austrian stock corporation consists of one or more members (natural persons), the articles of association may determine a specific number or range. A mandatory maximum number does not exist. Members of the management board are appointed or removed by the supervisory board. In general the supervisory board has to decide upon the appointments to fill vacancies or newly created directorships. However, in urgent cases (ie, if a sufficient number of members is not available to represent the company), the competent court may appoint an interim management board who will remain in office until a new member is appointed by the corporate body. Such interim management board is in general vested with the same rights and duties as a board appointed in the standard way.

The supervisory board consists of at least three natural persons. The articles of association may determine a higher number of board members (maximum 20 members of the supervisory board). The members of the supervisory board are appointed and removed by resolution of the shareholders' meeting.

According to the Austrian Corporate Governance Code, the nomination committee (ie, a committee of the supervisory board) submits proposals to the supervisory board for filling vacancies (see question 25). The company's works council's right to delegate members to the supervisory board has to be observed. For more information see question 33. Where fewer than three supervisory board members are appointed for a period of more than three months, the competent court may appoint further interim supervisory board members upon application of a member of the management board, a member of the supervisory board or a shareholder. The competent court may revoke the appointment of such interim supervisory board member once the conditions for the appointment are no longer met (ie, once the supervisory board has at least the required number of members who have been appointed in the standard way).

The name of each member of the management board and supervisory board, as well as the date of their appointment and, in the case of a management board member, the right to represent the company, is published in the publicly available commercial register. The Austrian Corporate Governance Code provides for further reporting and disclosing principles to be observed in the corporate governance report.

24 Board leadership

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

The Austrian Stock Corporation Act does not provide for a distinction between a CEO and other management board members. If the management board consists of more than one member, a chairman may be elected by the supervisory board who has a decisive vote in case of a tied vote, if the articles of association do not provide otherwise.

25 Board committees

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

An audit committee is mandatory for listed companies, as well as non-listed companies of a certain size ('very large companies') and requires at least one of its members to have certain accounting and reporting expertise ('financial expert'). The tasks of the audit committee are:

- monitoring the preparations for the accounting procedures;
- monitoring the effectiveness of the company-wide internal control system, if applicable, of the internal audit system and of the risk management system of the company;
- monitoring the work of the auditor (or group auditor);
- audit and preparation of the confirmation of the financial statements, of the proposal for the distribution of the profit, and of the report of the management board, if applicable, the corporate governance report, and reporting on this to the supervisory board;
- if applicable, audit of the consolidated financial statements and the group management report and reporting on this to the supervisory board of the parent company; and
- preparing a proposal for the selection of an auditor (group auditor) for the (consolidated) financial statements.

The Austrian Corporate Governance Code furthermore requires a nomination committee and a remuneration committee. The remuneration committee is chaired by the chairperson of the supervisory board.

The nomination committee submits proposals to the supervisory board for filling mandates that become free on the management board and deals with issues relating to successor planning.

The remuneration committee deals with the contents of employment contracts with management board members, ensures the implementation of Corporate Governance Code requirements on management board remuneration, and shall regularly review the remuneration policy applicable to management board members. According to the Corporate Governance Code, at least one member of the remuneration committee shall be required to have knowledge and experience in the area of remuneration policy.

26 Board meetings

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

There is no minimum requirement set by law with respect to the management board, as it is understood that it will meet frequently.

For the supervisory board, it is required that the board meets at least once every yearly quarter.

27 Board practices

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

The Austrian Corporate Governance Code provides for disclosure of board and committee practices in the annual corporate governance report (eg, which committees should be established, the number of committee meetings and activities of the committees). It also provides for rules on attendance of supervisory board meetings, such as, if a member of the supervisory board fails to attend half of the meetings of the supervisory board, this fact shall be stated in the corporate governance report (C-rule 58).

28 Remuneration of directors

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

The shareholders' meeting determines the remuneration of the supervisory board or the remuneration must be set out in the articles of association. The remuneration must be commensurate with the responsibilities and scope of work of the members as well as with the economic situation of the company. Members delegated by the works council do not receive additional remuneration since, as employees of the company, they are entitled to a salary and perform their services as members of the supervisory board as part of their regular employment. However, all members of the supervisory board, including employee representatives, are entitled to receive compensation for expenses (eg, travel costs). According to C-rule 51 of the Austrian Corporate Governance Code, there should be no stock option plans for members of the supervisory board (which are generally possible); should stock option plans be granted in exceptional cases, these must be decided in every detail by the shareholders' meeting. Usually, the remuneration is determined in advance by the shareholders' meeting for the entire term of office (essentially five years; see question 3). The conclusion of contracts with members of the supervisory board in which such members are committed to the performance of a service outside of their activities on the supervisory board for the company or a subsidiary for a remuneration not of minor value shall require the consent of the supervisory board. This also applies to contracts with companies in which a member of the supervisory board has a considerable economic interest. According to C-rule 49 of the Austrian Corporate Governance Code, the company must disclose in the annual corporate governance report the object and remuneration of such contracts (summary permitted). According to C-rule 47 of the Austrian Corporate Governance Code, the granting of loans by the enterprise to members of the supervisory board must not be permitted outside the scope of its ordinary business activity.

The remuneration of the members of the management board is determined by decision of the supervisory board. The supervisory board must ensure that the total remuneration of the members of the management board (salaries, shares in profits, expense reimbursements, insurance premiums, commissions, incentive-linked remuneration commitments and any other types of payment) are commensurate with the tasks and performance of each individual member of the management board, the situation of the company, the usual level of remuneration and must also take measures to create incentives to promote behaviour supportive of the long-term development of the company. This applies accordingly to pension payments, survivor's pensions and similar income. Furthermore, the Austrian Corporate Governance Code provides further details as regards fixed and variable components of compensation, severance payments and stock options (C-rules). The members of the management board are appointed by the supervisory board and may be revoked prior to the lapse of their term of office only in exceptional circumstances (see question 3). All transactions between the company or a group company and the members of the management board or any persons with whom the management board members have a close relationship must be in line with common business practice. Such transactions and their conditions must be approved in advance by the supervisory board with the exception of routine daily business transactions.

29 Remuneration of senior management

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

There are no specific laws regulating remuneration of senior management or transactions between the company and senior managers (save for loans, see immediately below). C-rule 28a of the Austrian Corporate Governance Code, however, provides that certain C-rules governing the remuneration of members of the management board shall also be applied in case of new remuneration systems of senior management staff. Loans to certain senior managers and persons in a close relationship with such senior managers require the prior approval of the supervisory board with the exception of loans that do not exceed the amount of one monthly salary.

30 D&O liability insurance

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

Owing to the increasing challenges for directors' and officers' due care standard posed by the legislature and the courts, the market of D&O liability insurance is becoming increasingly important in Austria. Typically, D&O liability insurance covers risks due to directors' or officers' misconduct, often a 'company reimbursement', criminal liability coverage and occasionally 'entity coverage'. D&O insurance is commonly used to cover both management board and supervisory board members. The company is allowed to pay the premiums.

31 Indemnification of directors and officers

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

Joint-stock companies are not permitted to indemnify board members against third-party liability in advance.

32 Exculpation of directors and officers

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

A joint-stock corporation may not waive or settle claims for damages against members of the management board prior to the expiry of five years from the date when the claim arose and only if the shareholders' meeting consents thereto, and no minority object whose aggregate holding equals or exceeds 20 per cent of the share capital.

A special rule exists with respect to the foundation of the company: a joint-stock corporation may not waive or settle claims for damages against the founding shareholders, the members of the management board and the supervisory board and any other liable persons prior to the expiry of five years from the date of registration of the company in the commercial register and only if the shareholders' meeting consents thereto and no minority objects whose aggregate holding equals or exceeds 20 per cent of the share capital.

33 Employees

What role do employees play in corporate governance?

According to the Labour Relations Act, the company's works council may delegate one member to the supervisory board for every two members elected by the shareholders; in case of an uneven number of supervisory board members, the works council may delegate an additional member. This means that essentially one-third of the supervisory board consists of employee representatives. This rule is mandatory and cannot be altered by shareholder resolution. The supervisory board consists of a minimum number of three members elected by the shareholders, resulting in the right of the works council to delegate two members. The maximum number of supervisory board members elected by the shareholders is 20, resulting in the works council being entitled to delegate another 10 members.

Employee representation also applies to all committees of the supervisory board, except for meetings and votes relating to the relationship between the company and the management board members with the exception of resolutions on the appointment or revocation of an appointment of a member of the management board and on the granting of stocks options of the company.

34 Board and director evaluations

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

The members of the management board and the supervisory board must act with 'the care and diligence of a prudent manager' when managing the business of the company or supervising the management of the company, as applicable. An evaluation of the members of the management board or the supervisory board is, in principle, made every year within the annual general meeting in which one item of the agenda relates to the discharge of the management board and the supervisory board members from their liability for the preceding business year. Such discharge does not release the board members from potential liability but can be regarded as an expression of trust. The granting of the discharge – as part of the annual general meeting – is published as part of the minutes of the annual general meeting in the commercial register and is therefore publicly available.

Furthermore, in practice many companies run evaluation procedures as part of their general HR routine, which also extends to the management board.

Disclosure and transparency

35 Corporate charter and by-laws

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

The articles of association (and any updated version thereof) have to be filed with the commercial register and are, therefore, publicly available. Documents filed from 1 January 2007 are available online (access to the database is not free of charge, however). Documents filed before such date are available in hard copy at the county court of the place where the company has its registered seat (again, the court charges for the cost of copying). Also note that because some courts implemented the online registrations earlier than the legal deadline of 1 January 2007, it can be the case that documents filed prior to such date are also available online.

The same applies to the minutes of shareholder meetings and certain other corporate documents (eg, merger agreements, sample signature sheets of board members, etc). These documents also have to be filed with the commercial register so are publicly available.

36 Company information

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

Austrian joint-stock corporations are obliged to file and register the following information with the commercial register:

- commercial register number;
- company name;
- legal form;
- corporate seat and business address;
- line of business;
- branches;
- articles of association;
- name and date of birth of members of the management board and the supervisory board;
- amount of share capital, increases and reductions thereof, types of issued shares (value shares or bearer shares) and, if applicable, the amount of bearer shares;
- annual financial statements, management reports and interim reports; and
- mergers, demergers and conversions.

In relation to listed joint-stock corporations, additional disclosure obligations apply such as the preparation of a corporate governance report and additional information to be included in the management report as regards controlling rights pertaining to or restrictions on its shares. In addition, certain transactions or information have to be disclosed pursuant to the Austrian Stock Exchange Act (eg, insider information that directly relates to the listed joint-stock corporation and is not publicly known (ad hoc disclosure)), as well as purchase and sale of the company's shares by its directors (directors' dealing).

Hot topics

37 Say-on-pay

Do shareholders have an advisory or other vote regarding executive remuneration? How frequently may they vote?

The shareholders' meeting determines the remuneration of the supervisory board or the remuneration shall be set out in the articles of association. Usually, the remuneration is determined in advance by the shareholders' meeting for the entire term of office (essentially five years, see question 3); however, theoretically there is no limitation as regards how often the shareholder meeting may vote on this.

With respect to the remuneration of the management board, the shareholders may only exercise indirect control via the supervisory board as the supervisory board is the competent body to determine the remuneration of the members of the management board.

38 Shareholder-nominated directors

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

The shareholders cannot nominate the members of the management board; the members are appointed by the supervisory board and their appointment may be revoked prior to the lapse of their term of office only in exceptional circumstances (see question 3). However, there are no specific rules of procedure for the appointment of the members of the management board. In practice, the articles of associations or the by-laws of the supervisory board provide for a nomination procedure. According to C-rule 41 of the Austrian Corporate Governance Code, the supervisory board sets up a nomination committee that submits proposals to the supervisory board for the filling of vacant management board positions and deals with issues relating to successor planning.

39 Shareholder engagement

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

Depending on the size of the company and its shareholder structure, the interaction between the shareholders and the company may be limited to participation in the shareholders' meeting (ie, in case of listed companies with a rather large number of 'unknown' shareholders) or more intensive (ie, in smaller companies with a limited number of shareholders who are known by the company). On a general level, the supervisory board members represent the relevant shareholders' interests and the supervisory board serves as the platform for discussions between the supervisory board and the management board. Whether other lines of communication with the shareholders are kept is dependent on the shareholder structure. However, normally shareholder relationships are handled by the management board and not by senior management or outside counsel.

A shareholder may also act as a contracting party vis-à-vis its company (ie, conclusion of service agreements between the company and its shareholder). The articles of association or internal rules may impose strict rules concerning the engagement of shareholders. Any contracts with shareholders are subject to strict Austrian capital maintenance rules: distributions to shareholders may be made only in accordance with statutory requirements (eg, payment of dividends out of the annual distributable profits of the company; formal capital decrease). The entire assets of the company are bound by such capital maintenance rules and any (open or disguised) transfer of cash, assets, the performance of services, or the granting of security to or for the benefit of direct or indirect shareholders or even affiliated sister companies violates capital maintenance unless an adequate arm's-length consideration is received by the company. Any payment violating capital maintenance rules may render a transaction null and void and may give rise to a claim to the company for recoupment of the paid-out capital. In addition, violations of the capital maintenance rule may also give rise to personal liability of the managing directors involved in such transaction and will also give rise to a tax claim (ie, any such payment will be treated as a dividend and be taxed accordingly).

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Sources of corporate governance rules and practices

1 Primary sources of law, regulation and practice

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

Brazil is a civil law country (as opposed to common law jurisdictions), where certain regulations and best practices are not incorporated into the country's pyramidal body of law.

As a general rule, companies adhere to the following laws:
- the Corporations Law (Law No. 6,404/1976) specifically governs corporations and may supplementarily govern limited liability companies (LLCs). Said law regulates shareholder rights, board structures, duties and responsibilities, among others;
- the Civil Code (Law No. 10,406/2002) governs an extensive amount of civil law topics, including a specific section on all existing corporate structures under Brazilian law and simple corporate governance rules applicable to these structures;
- the Securities Law (Law No. 6,385/1976), which created the Brazilian Securities Commission (CVM), the regulatory body that governs the securities exchange market, its surveillance, as well as providing specific guidelines and rules pertaining to listed companies; and
- the Financial System and Institutions (Law No. 4,595/1964) establishes the legal framework of financial institutions in Brazil and its governing entity, the Monetary Council (CMN), which is responsible for providing the guidelines with which these institutions must comply.

The set of regulations and best practices below, although in some cases not as enforceable as the aforementioned laws, are also widely adopted and disseminated in Brazil:
- CVM rulings, opinions, joint committee decisions, and directive releases. Highly enforceable and mandatory for listed corporations;
- B3 – Brasil, Bolsa e Balcão listing rules and corporate governance guidelines applicable according to the companies' listing segment in the Brazilian exchange market (Novo Mercado, Level 2, Level 1). Highly enforceable and mandatory for listed corporations, B3 is the new legal entity resulting from the merger between BM&FBovespa (exchange market) and CETIP (clearing house); and
- the Brazilian Institute of Corporate Governance (IBGC) Code of Best Practices (guidelines and recommendations) and the Brazilian Financial and Capital Markets Association (ANBIMA) guidelines (market self-regulation).

Corporations and LLCs are the most common and widely used corporate structure in Brazil. LLCs are governed by the Civil Code and may choose to be supplementarily governed by the Corporations Law. Corporations are entirely governed by the Corporations Law.

Our answers to the questions below will primarily refer to corporations, considered as more sophisticated entities and subject to stricter corporate governance surveillance.

2 Responsible entities

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

The primary government agencies or entities responsible for making and enforcing corporate governance rules are:
- CMN: although it has no supervisory powers, it is responsible for issuing the general guidelines and rules to be observed by CVM;
- CVM is responsible for business conduct, market regulation and surveillance of listed companies, and has powers to investigate, impose sanctions, as well as prohibit improper market conduct;
- the Council of Appeal of the Financial System is responsible for judging appeals filed against sanctions rendered by CVM; and
- B3 Market Arbitration Court (CAM) is responsible for settling corporate disputes related to the securities market. CAM is applicable to listed companies with specific corporate governance rules under the Novo Mercado, Nivel 2 and Bovespa Mais listing segments.

In Brazil, except for a few investors associations, there are no well-known shareholder groups or proxy advisory groups whose views are often considered.

The rights and equitable treatment of shareholders

3 Shareholder powers

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

Listed corporations and those with authorised capital (even if not listed) must mandatorily have a board of directors. In other cases, the board of directors is optional and is usually adopted only when there is more than one group of shareholders (eg, joint ventures, corporations that receive private equity investment). All corporations, however, must have a board of executive officers.

If the corporation has a single-tier board structure (board of executive officers only), their members will be appointed and removed by the shareholders. If the corporation has a double-tier board structure, the board of directors will be elected and removed by the shareholders and the board of officers will be elected and removed by the board of directors.

Shareholders may freely appoint and remove directors (or officers, as the case may be) by majority vote. The by-laws of closely held corporations may set higher quorums for board elections.

4 Shareholder decisions

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

In Brazil, all shareholder votes are binding. Non-binding shareholder votes do not apply.

The following decisions are reserved to shareholders:
- amendment to the by-laws;
- election and removal of directors or officers;
- annual approval of the company's accounts and financial statements;
- issuance of debentures;
- suspension of shareholder rights;
- valuation of shareholders' assets for the purpose of paying-up share capital;
- issuance of founder shares or participation certificates;
- merger, spin-off, dissolution or liquidation, and appointment of the liquidator, as well as approval of the liquidator's accounts; and
- bankruptcy or financial reorganisation.

5 Disproportionate voting rights

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

As a general rule, each common share is entitled to one vote. Preferred shares are usually non-voting but are granted certain dividend and liquidation preferences. The by-laws may limit the number of votes a shareholder is entitled to and plural voting is not allowed, regardless of the type of shares. Also, the by-laws may grant holders of preferred shares the right to vote on a number of topics, such as company valuation, its merger or spin-off, among others.

Some form of disproportionate or limited voting may occur under some circumstances. For instance, electing board members, holders of common shares that own at least 10 per cent of the share capital may cast multiple votes proportionally to the number of board members being elected. Also, shareholders of listed companies holding 15 per cent of voting shares or 10 per cent of non-voting shares or shares with restricted voting rights have the right to elect a board member and his or her substitute in a separate election at a shareholders' meeting.

6 Shareholders' meetings and voting

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

Shareholders duly invested in their capacity have no special requirements to participate in general meetings or votes and may be represented by proxy. The appointed proxy must be a lawyer, a shareholder or a director or officer.

The Corporations Law does not expressly authorise resolutions to be passed by written consent but, in practice, closely held corporations do act by written consent by having shareholders representing 100 per cent of the shares sign the relevant meeting minutes.

Total virtual meetings are still not allowed, but proxy voting and remote voting has been increasingly adopted in listed companies. In 2015, CVM established a distant voting mechanism to be gradually adopted by listed companies.

7 Shareholders and the board

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

Yes, shareholders are able to require meetings to be convened. As a general rule, meetings are called by the directors or officers, but may be called by the shareholders when directors or officers fail to do so under the events required by law or upon the shareholders' request to approve certain matters.

Resolutions and director nominations may be put to vote against the wishes of the board. Shareholders' meetings will approve resolutions or director nominations or dismissals pursuant to the quorum established by law or by-laws.

Listed companies adopting the recent remote voting procedures must grant certain minority shareholders the right to request the introduction of matters in the shareholders' meeting agenda. This request may not be unreasonably denied.

There are no specific provisions in the Corporations Law granting shareholders the right to require the board to circulate statements by dissident shareholders. Nevertheless, minutes of shareholders' meetings record all matters put to vote, including the votes of dissident shareholders. Dissident shareholders may also submit a written voting statement to be filed by the corporation.

8 Controlling shareholders' duties

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

Controlling shareholders have a duty to use their power to fulfil the company's business goals. The Corporations Law lists a number of acts that are considered an abuse of power by controlling shareholders, such as conflict of interest voting, voting against the company's best interest, election of notoriously unqualified managers, approval of irregular accounts, and approval of amendments to by-laws intended to harm minority shareholders. These acts are subject to enforcement action and also subject the controlling shareholders to liability for damages.

9 Shareholder responsibility

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

As a general rule, shareholders' responsibility is limited to the issue price of subscribed shares held by each shareholder in the corporation.

In exceptional cases of fraud and commingling of assets, the law expressly allows third parties to pierce the corporate veil whenever corporate assets are insufficient to cover the company's debts and obligations. Shareholders that practise any acts in violation of the law or by-laws, whether for self-advantage or the advantage of a third party, will be held jointly liable alongside the directors or officers for the performance of these unlawful acts.

Corporate control

10 Anti-takeover devices

Are anti-takeover devices permitted?

Yes. The Corporations Law sets forth tag-along rights in the event of listed corporations' change of control. In the event of a direct or indirect takeover of a listed corporation, the acquirer is obligated to conduct a public offering for all voting shares at a price per share equivalent to 80 per cent of the price per share to be paid by the acquirer to the controlling shareholder. For listed corporations in the Novo Mercado and Level 2 segments, price per share must be 100 per cent of the price paid to the controlling shareholder and the tender offer must be extended to all remaining shareholders.

Some corporations with widespread capital ownership and no defined controlling shareholder insert 'poison pills' in their by-laws with the purpose of preventing control takeovers. Basically, if an acquirer intends to purchase more than a certain percentage of shares, as limited by the by-laws, the acquirer must conduct a tender offer for the remaining shareholders. This has caused considerable controversy in Brazil. The IBGC Code of Best Practice recommends taking the utmost care in the adoption of poison pills to ensure that they do not prevent non-hostile takeover from happening.

11 Issuance of new shares

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

The board may only issue new shares without shareholder approval if the company's by-laws set forth an authorised capital amount and grant the board powers to do so.

Shareholders have pre-emptive rights to acquire newly issued shares, proportionally to the number of shares they hold. The law grants shareholders at least 30 days to exercise their pre-emptive rights. Pre-emptive rights may be excluded by listed corporations in case of public placements on the stock market.

12 Restrictions on the transfer of fully paid shares

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

Transfer restrictions may apply in the event shareholders are bound by a shareholders' agreement, such as drag-along and tag-along rights, put and call options, lock-up provisions and right of first refusal. Shares subject to a shareholders' agreement cannot be traded on the stock market.

13 Compulsory repurchase rules

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

In general, corporations may not trade with their own shares, with certain exceptions provided by law, such as redemption, amortisation or repurchases for treasury or cancellation of shares. Listed corporations are subject to additional requirements determined by the CVM.

Redemption and amortisation may be compulsory if so determined by the by-laws or by the shareholders' meeting. Redemption or amortisation that does not cover all shares of the same class shall be carried out by drawing lots.

14 Dissenters' rights

Do shareholders have appraisal rights?

Yes. Subject to few exceptions, dissenting shareholders are entitled to withdraw from the corporation and be reimbursed in the event of:

- transformation of the company into a different corporate structure (eg, from corporation to LLC);
- merger or spin-off;
- share merger;
- inclusion of an arbitration clause in the by-laws;
- creation of preferred shares and changes to their advantages and conditions;
- reduction of the mandatory dividend;
- a change in the company's corporate purpose; or
- if the company becomes part of a conglomerate or companies belonging to the same economic group.

Generally, share value will be based on the company's net worth and may only be below this amount if the reimbursement is based on the company's economic value, when authorised in the by-laws.

The responsibilities of the board (supervisory)

15 Board structure

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

See question 3.

In listed companies, a two-tier board structure is mandatory.

The board of directors is the collective decision-making body responsible for the company's general guidelines and how it conducts its business; whereas the board of officers is responsible for executing and carrying out decisions approved by the directors. In any case, the corporation will be legally represented before third parties by the signature of officers only.

Directors may also act as officers (at most one-third of the board members).

16 Board's legal responsibilities

What are the board's primary legal responsibilities?

The board of directors' primary legal responsibilities are:

- to establish the company's general guidelines and how it conducts business;
- to elect and dismiss the officers, as well as establish their duties, pursuant to law and the by-laws;
- to oversee the officers' management;
- to call a shareholders' meeting when deemed necessary or to approve the company's annual accounts and management reports;
- to render an opinion on acts or agreements to be executed by the officers, on behalf of the company, if the by-laws so require;
- to approve the issuance of shares or warrants, if permitted under the by-laws;
- to authorise the sale of non-current assets, real property liens and guarantees to third-party obligations, unless the by-laws set forth otherwise; and
- to elect and dismiss independent auditors.

The board of officers' primary legal responsibility is to conduct the corporation's day-to-day management. Specific duties may be determined by the by-laws and the board of directors. As long as it is within their powers and in accordance with by-laws' provisions, officers may constitute proxies to act on behalf of the corporation.

17 Board obligees

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

As a general rule, a director or an officer must always perform his or her duties in the company's best interest. The Corporations Law expressly assigns board members the following duties:

- Diligence and care: to act with the same duty and care that he or she would act under if conducting his or her own business affairs.
- Loyalty: to maintain the company's business as confidential, not disclosing any business information that may be used to obtain a personal or third-party advantage.
- Inform: in listed corporations, board members must disclose the amount of the corporation's (or related companies') securities that he or she holds and report to the market relevant information that may affect the purchase or sale of the company's securities.
- Conflict of interest: to refrain from intervening in any transaction that conflicts with the corporation's interest.

Hierarchically and in simplistic terms, the board of directors is subordinated and owes legal duties to the shareholders; whereas the board of officers is subordinated and owes legal duties to the directors.

18 Enforcement action against directors

Can an enforcement action against directors be brought by, or on behalf of, those to whom duties are owed?

An enforcement action can be brought against directors or officers for damages caused to the corporation. The company is the primary legitimate party for filing such action upon its approval at a shareholders' meeting by majority vote. If the action is not approved by the shareholders' meeting, any shareholder holding at least 5 per cent of the capital stock may file it directly.

19 Care and prudence

Do the board's duties include a care or prudence element?

See question 17.

20 Board member duties

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

The duties set forth by law apply to all individual board members, regardless of their skills and experience. See question 17.

In listed corporations, duties may be restricted by the corporation's by-laws, which may establish specific attributions and responsibilities for specific management members.

21 Delegation of board responsibilities

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

No board member's legal duties and responsibilities may be delegated to another board or management body, either created by law or the by-laws. However, corporations may, upon the officers' signature, appoint proxies to act on their behalf.

22 Non-executive and independent directors

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

The Corporations Law does not set any minimum number of independent directors.

However, in the Novo Mercado segment at least 20 per cent of the listed corporations' board members must be independent. A director is deemed independent if he or she:
- has no ties to the corporation, other than an equity interest;
- is not a controlling shareholder, spouse or close family member (to the second degree) of a controlling shareholder, nor has any ties to any company or entity related to a controlling shareholder;
- has not been an employee or officer of the corporation, or of the controlling shareholder, or of a subsidiary of the company in the past three years;
- is not a direct or indirect supplier or buyer of goods or services, to an extent that would imply loss of independence;
- is not an employee or senior manager of any company that is a service or product provider or consumer of the corporation to an extent that would imply loss of independence;
- is not a spouse or close family member (to the second degree) of any senior manager of the corporation; and
- is not entitled to any payment by the corporation other than the consideration earned as director.

The IBGC Code of Best Practice recommends the majority of the board to be composed of independent directors.

23 Board size and composition

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

The Corporations Law determines the board to have a minimum of three members, but there is no maximum number set by law. The number of members, or a range between a minimum and maximum number of members, must be set forth in the by-laws.

The board of listed corporations in the Novo Mercado segment must have at least five members.

The IBGC Code of Best Practice recommends an odd number of members, between five and eleven.

The size of the board usually varies according to the size and complexity of the corporation, capital distribution (defined control or not), whether committees need to be created and other needs.

In case of a vacancy in the board of directors, the other board members may appoint the substitute to occupy the position until the following shareholders' meeting.

The by-laws must determine how board of officers' vacancies are filled.

The Corporations Law requires that board members:
- have a good reputation;
- have not been convicted of any bankruptcy offence, fraud, bribery, corruption, misappropriation of public funds or embezzlement, crimes against the national economy or public property, nor subject to any criminal sanction which precludes access to public office;
- do not occupy any position in a competing company, unless this is waived by a shareholders' meeting;
- do not have a conflicting interest with the corporation, unless this is waived by a shareholders' meeting; or
- in the case of listed companies, have not been declared by CVM to be unable to occupy a board seat.

There is no legal requirement concerning diversity or expertise, but the IBGC Code of Best Practice recommends both.

Board members and officers must provide the company with a domicile address where they can receive service of process concerning their acts. In the case of listed corporations, they must also inform their share ownership (number, type and class).

Composition of the board of directors and of the board of officers is public, as the corporate documents that appoint their members are filed with the Board of Trade and published in local and official newspapers.

In the case of listed corporations, the curriculum vitae of all managers must also be disclosed and made available to the public.

24 Board leadership

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

The Corporations Law does not require the separation or joining of the functions of chairman and CEO, allowing some flexibility to corporations in general.

However, the IBGC Code of Best Practice recommends the separation of those functions and, according to the IBGC, the CEO should not be a member of the board of directors (but should participate in the meetings when invited).

For listed corporations in the Novo Mercado and Level 2 segments, separation is mandatory (except on an exceptional and transitional basis, in case of vacancy).

25 Board committees

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

There are no mandatory board committees, but large corporations usually set committees, either in the by-laws or by means of internal rules of the board of directors. The most frequent committees are: audit, human resources and remuneration, risk, finance, strategy and governance.

Committees have advisory functions and no decisive power. Their recommendations are not binding on the decisions of the board.

Corporations that decide to set committees usually follow the IGBC guidelines, which recommend that committees:
- should preferably be formed by board members only;
- should have at least three members, and must have at least one expert in his or her area of expertise (if there is no specialist, external experts should be invited); and
- should not be comprised of the corporations' executives, although they may be invited to some meetings.

Listed companies that have set an audit committee must annually disclose their financial statements, together with the committee's opinion.

26 Board meetings

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

There is no minimum number of board meetings required, but at least one, to approve the annual financial statements to be submitted to the shareholders' meeting, must be held.

The Corporations Law and usually the by-laws set a list of matters that require board approval and, therefore, extraordinary board meetings are quite often convened to resolve on those matters.

The IBGC Code of Best Practice recommends that the chairman propose an annual schedule with the dates of the ordinary meetings, the frequency of which should not be greater than once a month.

27 Board practices

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

Several rules applicable to the board of directors are set in the by-laws and, therefore, are public. That includes number of members, term of office, appointment of the chairman, procedures in case of vacancy,

Update and trends

The adoption of remote voting procedures at shareholders' meetings of listed corporations is the most remarkable development in corporate governance. In 2017, it became mandatory for corporations with shares that are more actively traded in the stock exchange, as determined by B3. In a nutshell, the remote voting procedure intends to increase minority shareholders' participation in shareholders' meetings, allowing shareholders to vote remotely upon submission of a voting form made available prior to the meeting. Shareholders holding a certain minimum percentage of shares (this percentage varies according to the capital stock) may even suggest the inclusion of matters in the meeting agenda. This suggestion may not be unreasonably denied. From 2018 onwards, adoption of remote voting procedures will be mandatory for all corporations listed in the A category (basically those that trade shares on the stock exchange).

meeting mechanism (call, resolution quorums, virtual meetings, minutes of meetings).

Minutes of board meetings with the purpose of being effective before third parties must be filed with the Board of Trade and published in local and official newspapers (in the case of listed corporations, they are also disclosed on CVM's and B3's websites). Minutes of meetings may contain a summary of only the resolutions passed.

The Reference Form that is annually filed before CVM by listed corporations contains more detailed information on the board structure, composition and practices.

28 Remuneration of directors

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

The shareholders' meeting must annually approve the global or individual remuneration of all managers (board of directors and board of officers). Shareholders usually approve a global cap for the year, which must provide for fixed and variable compensation and benefits. Individual remuneration is usually set by the board of directors under the global cap approved by the shareholders' meeting, according to human resources policies, career plans and advice from the remuneration committee, if installed.

Listed corporations must disclose more detailed information on management's remuneration in the Reference Form annually filed before CVM.

The by-laws must determine the term of office of directors and officers, which term must not exceed three years, re-election admitted. Listed corporations in the segment Novo Mercado are subject to stricter rules: the term of office of all directors must be unified and limited to two years, re-election admitted.

Directors and officers may not borrow money or assets from the corporation nor use its assets, services or take advantage of their position for their own benefit or for the benefit of a company in which they have an interest or of a third party, without the prior approval of a shareholders' meeting or of the board of directors. Also, directors and officers may not receive any type of direct or indirect personal advantage from third parties, without the by-laws or a shareholders' meeting authorising so.

29 Remuneration of senior management

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

See question 28.

30 D&O liability insurance

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

D&O insurance is permitted and common practice among larger companies (premiums are quite expensive for small and medium-sized companies). D&O insurance has recently been regulated by the Brazilian Insurance Agency and, according to such recent regulation, the company pays the insurance premium at no cost to the directors and officers.

31 Indemnification of directors and officers

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

There are no constraints, provided directors and officers act in the ordinary course of business and in due compliance of the law and of the by-laws.

Given that managers in Brazil (mainly officers) can quite frequently be involved as a defendant in lawsuits brought against companies (tax and labour claims in particular), companies generally assume responsibility for the debt and do not hold their directors and officers personally responsible.

32 Exculpation of directors and officers

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

A director or an officer is not personally liable for the commitments he or she undertakes on behalf of the corporation in the ordinary course of business. However, he or she will be liable for losses caused to the corporation in case he or she acts with negligence or wilful misconduct or in violation of the law or of the by-laws. There is no possible exculpation through amendments of the by-laws or other shareholder action.

A director or an officer is not liable for unlawful acts of the other directors or officers, except if acting in connivance with them, or if he or she neglects to investigate such acts or if, despite being aware of those unlawful acts, he or she fails to act to prevent them.

A dissenting director or officer may be exempt from liability when he or she records his or her dissent in the meeting minutes of the relevant management body (board of directors or board of officers), or when he or she immediately informs the other directors or officers, or the shareholders' meeting, about his or her dissent in writing.

In listed corporations, manager liability may be restricted to managers who, under the by-laws, have specific responsibility for the performance of such duties.

33 Employees

What role do employees play in corporate governance?

The Corporations Law expressly sets forth that a corporation has a social role and, to that effect, all managers (directors and officers) may authorise reasonable gratuitous acts to the benefit of the employees or of the community to which the corporation belongs.

The by-laws may require the board to have an employee representative, chosen by employees, but this is not customary practice, except for state-owned corporations and for some privatised corporations, in which case the employees' representative seat on the board is mandatory.

34 Board and director evaluations

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

Neither the Corporations Law, CVM regulations nor listing rules require any evaluation of the board, its committees or directors.

The Corporations Law establishes that directors shall be held liable for losses caused to the corporation as a result of unlawful practices.

Notwithstanding the lack of legal requirement, the IBGC Code of Best Practice recommends that the board be evaluated. Such evaluation may be carried out by board members, assisted by executives, other stakeholders or external advisers. The scope of the evaluation should include the board itself, as a collective body, committees (if installed), chairman, board members individually, and governance secretariat (if any). The IBGC Code does not provide a specific period to conduct board evaluations, but recommends the board to disclose information on the evaluation process and a summary of the main identified issues to be improved, as well as corrective measures implemented, so as to allow shareholders to have a proper understanding of its operations.

Disclosure and transparency

35 Corporate charter and by-laws

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

Corporations' by-laws and minutes of shareholders' meetings are filed before the Board of Trade and published on local and official newspapers. The board of directors' or board of officers' meeting minutes must be filed before the Board of Trade (and then made public) only if intended to become effective before third parties. Therefore, strategic and sensitive matters discussed at board meetings may to a certain extent be kept confidential.

Copies of documents filed before the Board of Trade may be requested by any third party.

36 Company information

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

Besides the corporate documents that become public once filed before the Board of Trade (see question 35), listed corporations have several disclosure requirements set by CVM and B3, such as:

- annual financial statements filed by 31 March;
- quarterly financial statements filed by the end of May, August and November;
- Reference Form (CVM form with complete information on the company) filed by 31 May – to be updated throughout the year in case of certain changes;
- releases on relevant facts that may impact the corporation's shares trade price, upon occurrence; and
- minutes of shareholders' meetings, board meetings and corporate acts in general, upon occurrence.

The Reference Form is a listed corporation's most comprehensive public document, and along with the financial statements, is the primary reference to understand a company's business. It addresses, among other issues:

- financials;
- risk factors;
- company's history;
- operations, activities, products, markets;
- economic group;
- assets;
- management discussion and analysis;
- projections (not mandatory);
- corporate governance;
- management remuneration;
- human resources;
- share control structure;
- issued securities; and
- trading and disclosure policies.

Hot topics

37 Say-on-pay

Do shareholders have an advisory or other vote regarding executive remuneration? How frequently may they vote?

The shareholders' meeting must annually approve all managers' global or individual remuneration, including directors and officers.

See question 28.

38 Shareholder-nominated directors

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

Shareholders representing at least 10 per cent 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.

Also, shareholders of listed companies, holding 15 per cent of voting shares or 10 per cent of non-voting shares (or shares with restricted voting rights) have the right to elect a board member, in a separate election at a shareholders' meeting. If neither the holders of voting shares nor the holders of non-voting shares achieve the relevant minimum percentages, they may aggregate their shares to jointly elect a director, provided they jointly achieve 10 per cent.

According to CVM regulations, listed corporations that adopt remote voting procedures at the shareholders' meeting called to elect board members must grant shareholders (holding a minimum percentage of shares that varies according to the corporation's capital stock) the opportunity to indicate candidates and to include them in the shareholders' meeting materials, at the corporation's expense. The remote voting procedure is not yet mandatory for all listed companies.

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39 Shareholder engagement

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

Most Brazilian companies, including listed ones, have a defined controlling shareholder (or a group of shareholders bound by a shareholders' agreement). Widespread and decentralised corporate control is still an exception in Brazil. In this sense, controlling shareholders still have a considerable influence in the corporation's management decisions and, to some extent, boards are still tied to majority shareholders' guidelines. But minority shareholders, particularly institutional investors, have been increasingly active and engaged, demanding greater transparency.

Listed corporations must have an investor relations (IR) officer, appointed by the board of directors among the senior management members. The IR officer is legally responsible for disclosing to investors, to CVM and to stock exchanges transparent, timely and reliable information on the corporation's businesses. Larger corporations typically have a structured IR department, coordinated by the IR officer.

Shareholder engagement typically occurs during the annual meeting season, upon disclosure of the annual financial statements and in preparation for board elections. Larger corporations often organise conference calls with investors and market analysts to discuss and explain the corporation's results.

Chile

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Sources of corporate governance rules and practices

1 Primary sources of law, regulation and practice

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

The main statutes applicable to corporate governance are:
- Law 18,045 (Securities Act);
- Law 18,046 (Corporations Act);
- Decree 702 of Ministry of Hacienda, 2011, rules of Corporations Act (Rules); and
- Decree Law 3,538, Securities and Insurances Superintendence (SVS) organic law.

Additionally, the SVS has issued the General Rule Number 385, dated 8 June 2015 (GRN 385), which obliges listed corporations to annually inform the SVS and the general public about the corporate governance, social responsibility and sustainable development practices adopted by them under a 'comply or explain' scheme.

Likewise, other regulations regarding corporate governance have been issued by several institutions for the specific entities they oversee:
- in 2008, the Superintendence of Pensions issued special norms on the matter, applicable to Private Pension Fund Administrators;
- in 2011, the SVS issued the General Rule Number 309, stating the corporate governance principles for insurance and reinsurance companies;
- in 2013 the Superintendence of Banks and Financial Institutions introduced certain matters of corporate governance in its Updated Rules Digest;
- in that same year, the Health Superintendence issued a circular letter applicable to Isapres (private health insurances); and
- the Social Security Superintendence has also issued circular letters, in relation to Family Welfare Funds (2015) and Mutual Benefits Societies of Employees (2017).

As a general rule, listed companies shall comply with all listing rules. However, GRN 385 follows the 'comply or explain' principle, meaning that listed companies are not obliged to comply with all practices included in the GRN 385, but to inform which practices have been adopted and how they have been implemented or to explain why a practice is not suited for or desirable to the company interest given its reality.

Finally, this chapter refers to corporate governance general rules in listed corporations and closed corporations, but partnerships limited by shares or special norms for other type of legal entities are not included.

2 Responsible entities

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

The SVS is the authority in charge of overseeing the Chilean capital market. The SVS has the authority to issue instructions and orders to apply and allow compliance of relevant laws and rules, to solve inquiries and petitions, and to investigate claims made by shareholders, investors or other legitimate interested parties. The SVS will be replaced by a new Financial Market Commission, which will have the above-mentioned authorities. Additionally, for specific types of corporations, the relevant authority may issue rules related to corporate governance.

Despite the fact that it is a common practice that certain authorities, such as the SVS, develop a consultation process with the general public for new regulations to be passed, there is no well-known shareholders' group or proxy advisory firm whose views are often considered. Some advisory firms have rendered their opinion and made some recommendations about certain Chilean corporate governance issues, but the authorities are not bound to consider their opinion. In recent years, activist shareholders have appeared in the Chilean market, but as stated above, authorities are not obliged to consider their requests.

The rights and equitable treatment of shareholders

3 Shareholder powers

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

Directors are appointed and removed by shareholders acting in shareholders' meetings. In order to revoke the board, all members must be removed at once. Shareholders may not remove one or more directors. Consequently, the number of votes required to elect a director will depend on their number and, as a general rule, to remove the whole board, 50 per cent plus one vote of the shares with voting rights are needed.

The board of directors is obliged to purse actions agreed by shareholders' meetings, whose matters are listed in the Corporations Act and in certain cases in company by-laws.

Directors appointed by a shareholders' group have the same duties towards the company and other shareholders as the remaining directors, not being able to infringe their duty with them to defend the interest of the shareholders' group that elected them.

4 Shareholder decisions

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

The following decisions are reserved to shareholders:
- Ordinary shareholders' meeting (occurs once a year at a predetermined time):
  - reviews the company's situation and auditor's report, the approval or rejection of the annual report, the balance sheet and financial statements;
  - profit distributions;
  - appointment or revocations of directors and auditors; and
  - any other matter of social interest that is not covered in the matters of the extraordinary shareholders' meeting.
- Extraordinary shareholders' meeting (occurs at any time when the social needs require it):

- company's dissolution;
- company's transformation, merger or division and amendments to by-laws;
- bonds convertible in shares or debentures issuance;
- sale of relevant assets;
- granting of guarantees to secure third-party obligations (excepted for affiliates where the board approval is enough); and
- any other matter that shall be decided by a shareholders' meeting.

In Chile, the concept of the non-binding shareholder vote does not exist.

5 Disproportionate voting rights

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

Chile follows the rule 'one share, one vote', being that the shares with multiple votes are prohibited by the Corporations Act, but shares with limited or no voting rights are allowed. As a general rule, even unpaid shares have voting rights, except if the articles of incorporation express the contrary. Shares owned by the same company do not have voting rights.

Most of the time, shares without voting rights or with limited votes are associated with certain preferences, for example, to elect a higher number of directors or to have the right for a higher proportion of company profits. If the company does not comply with preferences, shares will keep their voting rights while preferences are not fully respected.

6 Shareholders' meetings and voting

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

Shareholders have to be registered in the company's shareholders' registry to participate in a meeting. In listed companies, shareholders have to be registered at least five business days prior to the shareholders' meeting, and in closed corporations, at the beginning of the meeting.

Even shareholders with non-voting shares and directors are authorised to participate in shareholders' meetings with the right to speak.

Shareholders may attend meetings personally or be represented by a third party, who may or may not be a shareholder. The proxy form has to comply with certain requirements in order to be valid, and the company has the right to qualify such proxies.

Shareholders cannot act by written consent without a meeting.

All matters shall be subject to independent voting unless they are approved by unanimous decision. Voting shall be developed through a system that secures the simultaneous issuance of votes or its issuance in secret. Scrutiny must be carried out in a single public act, and in both cases, it shall be publicly known how each shareholder voted.

According to article 64, section 3 of the Corporations Act, the SVS may authorise, for listed corporations, distance voting systems. Those systems have to protect shareholders' rights and the voting process. SVS's General Rule Number 273 has authorised the following systems: ballot, voting by electronic device and distance voting. The latter has to comply with authentication, access control, confidentiality, integrity and no-rejection principles.

The GRN 385 asks if the corporation has a system that allows:

- shareholders to remotely participate in shareholders' meetings and voting, at the same time as those physically present;
- shareholders to remotely observe in real time what is happening in the meeting; and
- the general public to be informed in real time of the agreements reached by the meeting or with a time difference of less than five minutes.

Despite the fact that distance voting systems are permitted, to the best of our knowledge Chilean listed companies have not implemented them for the following reasons: the Chilean stock market is highly concentrated, most of the inverstors are located in Santiago, the majority of the meetings take place in this city; and proxies are commonly used.

7 Shareholders and the board

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

Resolutions and directors' nominations have to be put forward for voting even when against the wishes of the board. The board does not have the authority to limit the decisions to be made at the shareholders' meeting.

Shareholders that own more than 10 per cent of outstanding shares with voting rights may request the board of directors to convene an ordinary or extraordinary shareholders' meeting, expressing in their request the matters to be discussed at the meeting.

Shareholders who own more than 10 per cent of voting shares may formulate comments and propositions: related to the company's business and to require their inclusion in the annual report; and related to the matters put up for vote by the board in shareholders' meetings and to include them in the information to be sent to shareholders.

All shareholders have the right to speak in the meeting, thus their opinion (dissenting or not) shall be heard. Meeting deliberation and agreements shall be included in the relevant book's minutes, and in listed corporations the most recent minutes of the meetings have to be available on the company's website for shareholders. Additionally, books may be inspected by shareholders prior to the ordinary shareholders' meeting.

8 Controlling shareholders' duties

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

Article 30 of the Corporations Act establishes, as a general rule, that shareholders have to exercise their rights respecting the company and others shareholders' rights. The Corporations Act does not establish special duties for controlling shareholders, but they shall exercise their rights with due respect for the limits imposed by other shareholders and company rights. Hence, controlling shareholders may not abuse their control position to obtain benefit at other shareholders' or the company's expense.

Enforcement actions that may be brought against controlling shareholders will depend on the abuse committed or the law infringed. Other shareholders and the company may claim damages under civil law or using the derivative action described in question 18 below.

9 Shareholder responsibility

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

No, as a general rule corporations limit the shareholders' liabilities, being responsible up to the amount they have agreed to pay in for subscribed shares only. Consequently, the only obligation that shareholders have with the company is to pay the capital corresponding to their shares, not being obliged to return the benefits received.

Corporate control

10 Anti-takeover devices

Are anti-takeover devices permitted?

In Chile, the majority of companies have a controlling shareholder, thus there is no need for specific defences. The shareholder is the only person in charge of deciding about the sale of his or her shares. Therefore, if a person wants to take control of the company he or she will have to negotiate with the controller and then follow the special procedure established by law for the public offerings for the acquisition of shares, known as 'OPA'.

Eventually, by-laws may include certain anti-takeover devices as long as they are not contrary to the applicable law.

11 Issuance of new shares

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

All matters related to company capital (increase, decrease, issuance of new shares, shares privilege, vote restrictions, etc) have to be approved by the relevant shareholders' meeting. Consequently, the board is not allowed to issue new shares without shareholders' approval.

Article 25 of the Corporations Act states the general rule regarding pre-emptive rights to acquire newly issued shares. Any shares or any other securities that will in the future give rights over company shares shall be offered, at least once, preferably to each shareholder on a pro rata basis of the shares owned. However, there are certain limited exceptions to pre-emptive rights, such as: capital increase percentage destined to stock options for employees of the company or its affiliates and capital increase due to merger by absorption to the absorbent company's shareholders, among others.

The pre-emptive right can be renounced or transferred – to other shareholders or third parties – by the relevant shareholder during a term of 30 days and with the formalities established by the Corporations Act and its Rules. If the shareholder does not express his or her opinion during that term it will be understood that he or she renounces his or her right.

Shares not subscribed by shareholders cannot be offered to third parties at inferior value or in better conditions. In listed corporations, this restriction applies for a period of 30 days after the expiry of the option term. After that, the stocks may be offered to third parties at different prices and conditions if the offer is made through a stock exchange.

12 Restrictions on the transfer of fully paid shares

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

In listed corporations, company by-laws cannot contain restrictions to free disposing of shares. Nevertheless, shareholders' agreements that establish restrictions or certain rights over company shares are allowed. In order to be able to exercise the rights contained in the shareholders' agreements before third parties, the agreement shall be deposited in the company, made available to other shareholders and third parties and noted in the shareholders' registry of the company. The shareholders' agreements will not affect the company's duty to register the share transfer.

Common restrictions included in shareholders' agreement are tag-along, drag-along and right of first refusal, among others.

13 Compulsory repurchase rules

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

Yes, under certain and limited circumstances the company may repurchase its own shares. Those cases are:

(i) due to a withdrawal right exercised by shareholders;
(ii) as result of a merger with another company that is a shareholder of the absorbent company;
(iii) if it allows for compliance with a capital decrease agreement, when the market price of the stocks is lower than the rescue value to be paid to shareholders; or
(iv) when a shareholders' meeting agreed on that following certain conditions and requirements.

These situations can only be temporal, for example, in cases (i) and (ii) the stocks have to be sold by the company in a stock exchange within one year of their acquisition; and in (iv) within 24 months or five years if the stocks are destined to be employees' compensation plans. If stocks are not sold during the term, the capital will be automatically decreased.

The cases described in (i) and (ii) are mandatory.

14 Dissenters' rights

Do shareholders have appraisal rights?

Yes, article 69 and the following articles in the Corporations Act give dissenting shareholders the right to withdraw from the company and be paid for their shares.

The withdrawal right is granted to a dissenting shareholder, meaning a shareholder who opposes in the same meeting the agreement reached by the shareholders or, who being absent at that meeting informs the company about his or her disagreement within 30 days counted from the meeting's date. The right is granted to all shareholders, even to those that own non-voting shares. Shareholders who attended the meeting – personally or represented – but refrain from voting, will not have the withdrawal right.

Matters that grant withdrawal rights are: company transformation, merger, sales of certain corporate and affiliates assets, the granting of certain guarantees for third-party obligations, in listed companies, for minority shareholders, when a shareholder acquires more than 95 per cent of shares, the cancellation of the company's registration in the Securities Registry kept by the SVS, among others.

The value that the company shall pay to the dissenter shareholder for his or her shares is: for listed companies – the market price, and for closed corporations – the book value.

The dissenting shareholder may renounce his or her withdrawal right before the company pays the stock value. Once the price is paid, the stocks have to be registered in the shareholders' registry under the company's name.

The board of directors may convene a shareholders' meeting, during a certain period of time specified by law, to reconsider or ratify the agreement that originates the withdrawal right. If the meeting revokes the original agreement, the withdrawal right will expire.

The responsibilities of the board (supervisory)

15 Board structure

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

Corporations are managed by a board of directors appointed by the shareholders' meeting. In Chile, the only allowed board structure is one-tier. Even when the law does not expressly state that it is a unitary board, there is no discussion about this.

16 Board's legal responsibilities

What are the board's primary legal responsibilities?

The board of directors is in charge of managing the company and represents it judicially and extrajudicially, for the compliance of its purpose, being invested with all the managing and disposal authorities that law or the by-laws not established as authorities of the shareholders' meeting.

Directors have to exercise their function in complying with their fiduciary duties. Their main duties are:

- the duty to be informed (and the right to request certain information);
- the duty of care, having to comply with the standard of conduct set by law; and
- the duty of loyalty, which includes:
  - the duty of confidentiality; and
  - the duty to respect the business opportunity of the company.

The director has to be loyal to the company in the exercise of his or her functions and cannot compete or damage it with his or her actions.

17 Board obligees

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

The board of directors represents the company, owing its legal duties to the company and its shareholders.

Directors appointed by a group or class of shareholders have the same duties towards the company and the rest of the shareholders as the remaining directors, not being able to infringe their duties under the pretext of defending the interest of those who have appointed them.

18 Enforcement action against directors

Can an enforcement action against directors be brought by, or on behalf of, those to whom duties are owed?

Yes, shareholders who represent at least 5 per cent of the outstanding shares or any director may sue, on behalf of the company, those responsible, including directors, for any damage caused to the company due to infringement of the Corporations Act, its rules, by-laws, or norms issued by the board or by the SVS. This action is known as derivative action.

19 Care and prudence

Do the board's duties include a care or prudence element?

Directors have to exercise their functions in compliance with the fiduciary duties imposed by law, one of them being the duty of care. Directors shall use, in the exercise of their functions, the care and diligence that people ordinarily employ in their own businesses. This corresponds to the ordinary standard of care (*culpa leve*) defined by Chilean civil law.

The duty of care obliges every director to regularly follow and decide about managing issues, requesting all the information needed for this purpose, with the convenient collaboration or assistance from management, to actively participate in the board and committees, attend the meetings, request board meetings and that certain matters be reviewed by the board, opposed to illegal acts, among others.

Directors will be jointly and severally liable for damages caused to the corporation and its shareholders due to any guilty and fraudulent actions.

20 Board member duties

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

Directors' functions are collectively exercised in meetings duly constituted. Therefore, individual acts of directors do not constitute an act of the board, nor of the company and are not binding for the company unless the board, acting as such, delegates some specific functions.

Directors are jointly and severally liable for damages caused to the shareholders and the company due to their negligent and fraudulent actions. To protect his or her responsibility, the director has to oppose the act or agreement and the opposition shall be recorded in the minutes of the relevant directors' meeting and shall be informed to shareholders in the next ordinary shareholders' meeting.

21 Delegation of board responsibilities

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

Individually considered directors are not allowed to delegate their personal functions as directors. However, the board may delegate part of its functions to senior executives, managers, lawyers, one director or directors' commissions and, for specifically determined purposes, to other persons.

22 Non-executive and independent directors

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

Given the characteristics of the Chilean stock market, which is highly concentrated, independence does not refer to management but to the relation to controlling shareholders.

Listed corporations that have: a market capitalisation equal to or higher than the equivalent of 1.5 million UF (US$59 million approximately, as of 31 May 2017); and at least 12.5 per cent of the issued shares with voting rights, are owned by shareholders that individually control or own less that 10 per cent of such shares, have to appoint at least one independent director and constitute a directors' committee.

The independence concept was amended by Law 20,382 passed in 2009. Before the reform, a director was independent if he or she had been elected without controlling shareholders' votes.

Currently, a person shall not be considered as independent if at any moment during the last 18 months:

(i) they maintained any economic, professional, credit or commercial connection, interest or dependency of relevant volume and nature, with the company, the other companies from the same group, its controller, the senior management of any of them, or has been director, CEO, manager, senior executive or consultant of them;
(ii) they maintained certain family relationships with the persons above-mentioned;
(iii) they have been director, CEO, manager or senior executive of a non-profit organisation that has received contributions or donations from the persons indicated in (i);
(iv) they have been a partner or shareholder who owned or controlled, directly or indirectly, 10 per cent or more of the capital;
(v) they have been a director, CEO, manager or senior executive of an entity that has rendered legal or consultant services, for relevant amounts, or an external auditor of the persons indicated in (i); or
(vi) they have been a partner or shareholder who owned or controlled, directly or indirectly, 10 per cent or more of the capital, directors, CEO, managers or senior executives of the main company's competitors, suppliers or clients.

The main difference in responsibility of independent directors is that they shall be members of the directors' committee that is further described in question 25. As explained in question 24, executive directors are not allowed.

23 Board size and composition

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

The size of the board is determined in the company's by-laws establishing an invariable number of directors. If shareholders want to modify the number of directors or to create a new directorship, a by-laws amendment has to be agreed on at the relevant shareholders' meeting and must comply with all the formalities. There is one exception for companies that have to appoint independent directors and the directors' committee, in which case if its by-laws consider less than seven members, the ordinary shareholders' meeting has to appoint seven directors.

The minimum number of seats depends on the type of corporation. Closed corporations shall have at least three directors, listed companies at least five, and corporations that shall designate an independent director and establish a directors' committee shall have at least seven directors. If the respective by-laws do not set the number of board members, the legal minimum shall apply.

The Corporations Act does not set a maximum number of directors. However, special laws may establish special minimum and maximum and other requirements for special corporations (eg, banks).

By-laws may establish substitute directors in the same number of principals. If they do, each principal director shall have his or her substitute. Substitutes will replace principals permanently in case of vacancy or temporarily in case of absence. If the vacancy of a director and his or her substitute occurs, the whole board has to be renewed in the next ordinary shareholders' meeting. In the meantime, the board may appoint a substitute. There are special rules for vacancies of independent directors.

The following persons cannot be appointed as board members:

- minors (aged less than 18 years old);
- directors who have been revoked due to the rejection of the balance sheet by a shareholders' meeting;
- persons with certain criminal records (including bankruptcy crime); and

- authorities regarding entities that they, directly and in accordance with the law, supervise or control.

There are other restrictions to being a director of listed corporations or their affiliates, such as being a senator, congressman, state ministry, SVS officer, stockbroker, etc.

Except for independence in certain cases, there are no required criteria that individual directors or the board as a whole must fulfil.

General Rule Number 30 (GRN 30), issued by the SVS, which contains the ongoing information that listed corporations have to disclose, states a disclosure requirement relating to board composition. The annual report shall contain information about diversity in the board of directors, informing about the number of directors by: gender; nationality; age range; and years as director. Also, it shall include information about profession or occupation of directors appointed during the last two years.

Additionally, the GRN 385 asks if the company has established a system to inform shareholders about:
- the diversity of capacity, conditions, experience and vision that is needed in the board;
- the maximum number of other boards in which it is appropriate that company directors participate;
- the candidate's experience and profession; and
- if the candidate during the last 18 months, has or has had any contractual, commercial or any other kind of relationship with the company's controller, main competitors or suppliers.

24 Board leadership

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

The CEO position is incompatible with the board chairman position and with being auditor or accountant of the company; and in listed corporations is also incompatible with being a board member.

There is flexibility on the board leadership being the chairman elected by directors. In case of a tie, it will be decided by a ballot.

25 Board committees

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

There is only one mandatory board committee for listed corporations that complies with the requirements described in question 22. This directors' committee is a mix of accounting and compensation committees.

The directors' committee has the following main faculties and duties:
- to review the external auditors' reports, the balance sheet and the financial statements;
- to propose to the board the name of external auditors and the risk rating agency;
- to review and issue a report about related-party transactions;
- to review the remuneration and compensation plans for the CEO, senior executives and other employees;
- to inform the board about the convenience of hiring auditors for services other than external auditing; and
- to prepare the annual report about its work, including recommendations for shareholders.

The directors' committee shall be composed of at least three members and the majority of them shall be independent. If there are more than three independent directors, the board shall decide, by unanimous decision, who will be on the committee. In case of disagreement, preference shall be given to those directors who have been appointed with more votes from shareholders that own or control less than 10 per cent of shares. If there is only one independent director, he or she will appoint the other members of the committee. The president of the board may not integrate the committee or subcommittees unless they are independent.

Finally, by-laws may establish other different committees, their functions and composition requirements and corporations may voluntarily establish the directors' committee.

26 Board meetings

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

Yes, in listed corporations the board of directors shall meet in ordinary meetings at least once a month. The company's by-laws may establish a higher frequency or other specific requirements.

The GRN 385 asks if the board has established a minimum number of ordinary meetings.

27 Board practices

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

No, there is no disclosure required. However, the minutes and the books, among other company documents, shall be available at the company's offices for shareholders' review during 15 days prior to the ordinary shareholders' meeting.

Additionally, the GRN 385 asks if the board of directors meet, at least quarterly, with the external auditing company, risk management unit, internal auditing unit, compliance officer, corporate responsibility and sustainable development units, or their equivalents, to analyse relevant aspects of the functions developed by them.

28 Remuneration of directors

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

A company's by-laws must determine if directors shall be remunerated or not. If they are, every year the ordinary shareholders' meeting shall fix in advance the compensation's amount to be paid to directors. Any other relevant payment made to the directors for functions different to the director's position has to be authorised or approved with the relevant formalities.

Additionally, the annual report shall contain all remunerations received by directors during the prior year, including those for other functions than the director position, representation allowances, bonus and any other payment.

The members of the directors' committee shall be remunerated. The remuneration shall be fixed, every year, by the ordinary shareholders' meeting, in accordance with their functions. The remuneration shall not be less than the remuneration that any regular board member receives plus one-third of its amount.

As a common practice, directors' remunerations are composed of a fixed fee and a variable part, which depends on the company's results.

29 Remuneration of senior management

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

As a common practice, the board of directors determines the remuneration of most senior management. In Chile, there is no say-on-pay by shareholders on this matter. GRN 30 states that the annual report has to state the remunerations paid to senior management as well as the compensation plans and special benefits for them.

GRN 385 asks if salary structures and polices of the CEO and senior management have to be approved by the shareholders' meeting. Furthermore, GRN 385, trying to prevent bad practices, asks if the company has implemented a formal procedure to annually review salary structures, total compensations granted to the CEO and other senior

Update and trends

On 23 February 2017, Law No. 21,000 was published in the Official Gazette, creating the new Financial Market Commission (FMC), a collegial and technical institution, which will replace the currently existing SVS. The FMC will come into force in a term of up to 18 months.

Some of the more important changes introduced by Law No. 21,000 include:

- shifting from a single superintendent to a collegiate five-member council;
- greater regulatory powers, which will permit faster regulatory adjustments to cope with the challenges of financial market regulation, including, among others, a regulatory impact integrated evaluation system and public consultation;
- improvements to the sanctioning procedure to strengthen its effectivity and the due process guarantees, making it possible to have a timely judicial review of the FMC's decisions; and
- the splitting of the investigative and prosecuting functions from the sanctioning functions, which are both currently exercised by the superintendent, to be now distributed between a prosecutor and the new council.

In recent years, Chilean corporations have started issuing voluntarily corporate governance handbooks and codes, with the purpose of compiling in a single document, organised and easy to access, all the information related to the company's corporate governance matters, including in certain cases the GRN 385 answers sent to the SVS and the policies and procedures related to them.

These types of initiatives are voluntary. They are the result of companies' own efforts and do not respond to any kind of legal requirement or actions from authorities or other organisations, as is the case in other Latin American countries.

executives, with the assessment of a third-party, and if they are published on the company's website.

30 D&O liability insurance

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

D&O liability insurance is a common practice for directors. Corporations can pay the director's premiums. However, as the director is not an employee of the company, it is highly likely that the Chilean Internal Revenue Service will consider the premium a rejected expense. This means that the company shall pay a penalty tax of 40 per cent of the expenses amount. It will be necessary to prove before a tax court that the premium expense was needed to generate the company's income.

31 Indemnification of directors and officers

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

There is no constraint on the company indemnifying directors and officers in relation to liabilities incurred in their professional capacity, but this is an uncommon practice. Liabilities that arise from gross negligence or fraud cannot be indemnified, in accordance with civil law.

32 Exculpation of directors and officers

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

Any by-laws disposition or shareholders' agreement that precludes or limits directors' or officers' liability will be null and void. Moreover, the approval of the annual report, financial statements and other documents by the shareholders' meeting does not preclude or limit the director's liability for determined acts or business, nor does the specific approval of them preclude liabilities when they have been executed fraudulently or negligently.

33 Employees

What role do employees play in corporate governance?

According to the law and regulations, employees do not play any specific role in corporate governance. They are stakeholders without attributions or rights. If a person is an employee but also a shareholder, he or she will play his or her role as any other shareholder.

34 Board and director evaluations

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

No, there is no legal requirement in this regard. However, GRN 385 asks if the company has established a formal procedure to annually review the board's organisation and functioning to detect areas of improvement, with the help of an expert third party. Additionally, GRN 385 asks about board evaluation process regarding the inclusion of practices mentioned in such rule.

Disclosure and transparency

35 Corporate charter and by-laws

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

Corporations shall have, available for shareholders, at their main office, branches and on its website (for listed corporations) updated versions of its by-laws duly signed by the CEO, indicating the date and notary public, in which their articles of incorporations, by-laws and any amendments have been granted and the information about their legalisations.

Additionally, GRN 385 asks if corporations have an updated website, where shareholders may easily access the company's public information.

36 Company information

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

The board shall disclose to shareholders and the general public certain of the company's legal, economical and financial information required by law or by the SVS. The specific obligations will depend on whether it is a listed or closed corporation. In listed corporations, the board has to take measures needed to avoid the information being disclosed to certain persons before the general release.

The board of directors has the authority to qualify certain information as confidential, when it refers to pending negotiations that, if they are known, may affect the social interest. This shall be agreed by at least three-quarters of the directors in the exercise.

Examples of disclosure obligations are:

- Information to be disclosed for the ordinary shareholders' meeting: annual reports, balance sheet, minutes, external auditors reports, etc, which shall be available for shareholders' review during the 15 days prior to the date of the ordinary shareholders' meeting in the company's offices. During that term, information from the company's affiliates shall also be available. In listed corporations the annual report, financial statements and auditors' report have to be made available for shareholders and some of those documents have to be published in the company's website.
- Ongoing information to be disclosed by listed corporations to the SVS, brokers and all stock exchanges (when the company is listed in one of them) contained in the GRN 30 includes:
  - quarterly and annually financial statements and reports;
  - capital variations;
  - annual report;
  - essential facts, about the company, its business and securities, as soon as the company knows about it or it happens. The information is essential when it would be considered relevant for investment decisions by a prudent person. The GRN includes a list of essential facts examples and the instruction to inform

them. Confidential information has to be provided to the SVS in accordance with special instructions; and
- information of interest means information that cannot be qualified as essential, but is useful for a proper financial understanding of a company, its securities or their offer.

There are several other norms that contain obligations to disclose information about several matters.

Finally, GRN 385 asks if the company has implemented a formal and ongoing improvement procedure to detect and implement eventual improvements in the production and diffusion of information to the public and if such procedure is audited by a third party, on an annual basis.

Hot topics

37 Say-on-pay

Do shareholders have an advisory or other vote regarding executive remuneration? How frequently may they vote?

Shareholders do not have an advisory or any other vote regarding executive remuneration; it is determined by the board of directors or by the senior management.

38 Shareholder-nominated directors

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

Yes, they do. The CEO shall inform shareholders, at least two days prior to the meeting, about the list of nominated directors that have accepted the nomination and have declared whether they have any unsuitability for the position. If this is not possible, the list shall be available at the beginning of the meeting. Candidates may be added to the list even during the meeting, provided they comply with certain requirements.

39 Shareholder engagement

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

Yes, usually Chilean companies engage with shareholders through the investor relation units.

GRN 385 asks whether companies have a unit in charge of the relationship with shareholders, investors and the media.

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Sources of corporate governance rules and practices

1 Primary sources of law, regulation and practice

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

The main sources of law relating to corporate governance in France are:
- the Commercial Code;
- concerning listed companies, the general regulations, which are binding, and recommendations of the French stock exchange authority (the Autorité des marchés financiers (AMF)), which may be binding on a case-by-case basis; and
- specific laws that organise the governance of corporate vehicles designed for certain business sectors (financial institutions) or professions (such as auditors or pharmaceutical businesses).

The relevant European regulations have been incorporated into these sources.

The Commercial Code encourages companies listed on a regulated market to refer to a corporate governance code, and requires those companies that do not intentionally refer to these codes to explain their reasons for not doing so and to clarify their own corporate governance rules.

Two established corporate governance codes are currently available: the Afep-Medef Code, designed for large listed companies, and the MiddleNext Code, which was initially dedicated to small and medium-sized listed companies and now also addresses the case of large listed firms controlled by one shareholder or a group of shareholders. They are non-binding, based on the 'comply or explain' principle. A corporate governance code for (non-listed) medium-sized and start-up companies was also published by a professional organisation of managers and directors (ADAE) several years ago.

2 Responsible entities

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

There is no specific agency with exclusive competence in the elaboration and enforcement of corporate governance rules.

However, the AMF, as guarantor of sound market information, closely reviews and monitors corporate governance practices of listed companies and publishes an annual report on this matter.

The Afep and Medef associations have set up a high committee on corporate governance in order to review the practices of the listed companies applying the Afep-Medef Code and to ensure the effective implementation of the 'comply or explain' principle. This committee works closely with the AMF.

Several shareholders' associations are active in order to promote and defend shareholders' rights. They are often consulted by authorities in the development of new regulations and are sometimes involved in legal actions to defend their position.

The rights and equitable treatment of shareholders

3 Shareholder powers

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

In France, the 'limited liability company' concept covers different corporate forms of vehicles:
- Public limited company (*société anonyme* (SA)): most functioning rules are provided for by the Commercial Code and are compulsory; the SA is the only type of vehicle (apart from the SCA) that may be listed.
- Joint-stock company (*société par actions simplifiée* (SAS)): functioning rules are predominantly decided by the shareholders in the articles of association.
- Limited company (*société à responsabilité limitée* (SARL)): functioning rules are provided for by the Commercial Code and are compulsory; an SARL is generally reserved to small businesses.
- Limited partnership (*société en commandite par actions* (SCA)), organised by the Commercial Code and to a certain extent by the articles of association – a sort of limited partnership with a share capital, where two types of members coexist: general partners (*commandités*), who are liable on their personal assets for the SCA's debts, and limited partners (*commanditaires*) who basically are shareholders. The SCA form is chosen by listed companies as a poison pill against hostile takeover bids.

In an SA, either with a one-tier structure (a board of directors) or with a two-tier structure (an executive board and a supervisory board), the shareholders always have the power to remove members of the (supervisory) board at a simple majority vote in a meeting, even if this matter has not been included in the agenda.

SCAs are managed either by a general partner, or a third person whose rules of appointment and removal are freely set in the articles of association. SCAs also have a supervisory board whose role is to control management and that may exercise a veto right on the appointment of managers. The power of shareholders in such companies is limited: every decision has to be confirmed by the general partners, with the exception of the appointment of the members of the supervisory board.

Shareholders of an SAS benefit from a large flexibility to draft the articles of association, especially as regards governance rules, which is the reason why investors who need to address specific governance issues and tailor peculiar corporate functioning rules generally choose this legal form. Appointment and removal rules of executives and directors are provided for in the articles of association.

SARLs do not have a board of directors per se, as management and executive functions are combined in a single type of duty (*gérance*). The appointment and removal of managers are decided by the shareholders at a simple majority unless the articles of association provide for a qualified majority. Shareholders may also request removal of the managers with cause to the courts.

When consulted on a specific question, a shareholders' vote is binding (with a few exceptions). But apart from their removal right regarding the board or legal action, shareholders have no direct way to require the board to pursue a particular course of action.

4 Shareholder decisions

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

Shareholders' approval is required for the following decisions:
- approval of the company's (and consolidated) annual accounts;
- dividends allocation;
- appointment of the (supervisory) board members and allocation of the global amount of their attendance fees, the (supervisory) board having the exclusive power to split the fees between members;
- appointment of the statutory auditors;
- approval of the report of the statutory auditors on transactions between the company and its related parties;
- amendment of the articles of association (eg, increase or reduction of the share capital, mergers, change of corporate form or nationality, etc); and
- dissolution.

The articles of association may also provide that certain other decisions require the shareholders' prior approval, but such restrictions cannot be opposed to third parties and agreements concluded without such a prior approval remain binding. The company's representatives can, however, be held liable for the loss suffered by the company as a result of such agreements. The same solution applies regarding transactions with related parties when the shareholders have refused to approve the statutory auditor's report.

5 Disproportionate voting rights

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

French law provides for the 'one share one vote' principle in non-listed companies (but exceptions are permitted) while in companies listed on a regulated market, a double voting right is automatically granted to registered shares after a two-year period of uninterrupted holding (unless otherwise provided for by the articles of association).

Companies may also issue preference shares deprived of voting rights, usually in consideration of entitlement to preferred dividends. Such preference shares are limited to a quarter of the total amount of shares in listed companies (half in non-listed). On the contrary, some preference shares benefit from double voting rights, or a veto right for certain decisions.

A cap on the votes may also be implemented for each shareholder, it being specified that the articles of association of listed companies may suspend such a limit in the event of a takeover bid.

In an SAS, disproportionate voting rights are allowed with no restriction.

6 Shareholders' meetings and voting

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

Shareholders must justify ownership of their shares two business days prior to the meeting in listed companies (record date) and either this date or the meeting date for non-listed companies.

Shareholders who cannot attend the meeting can vote by mail or proxy. This proxy is either given to a specific person, who may be a shareholder, or sent to the company with no specific proxy holder's name, which corresponds to a vote in the way recommended by the board. In companies that have adapted their articles of association accordingly, shareholders may also vote electronically.

Although French law allows shareholders to participate virtually in the meetings if the articles of association so provide, professional associations and law professionals do not, at present, recommend using such an option.

7 Shareholders and the board

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

Shareholders' meetings are generally convened by the board.

Shareholders may ask the board to convene a meeting. In case of refusal, shareholders holding at least 5 per cent of the share capital may request to the courts the appointment of an agent who will convene the meeting. Such shareholders do not need to evidence urgency, but the judge will assess whether the request is consistent with the company's interests.

After a public takeover or a change of control of a company, majority shareholders may also convene a shareholders' meeting.

Before a meeting, minority shareholders (holding at least 5 per cent of the voting rights in companies with a share capital not exceeding €750,000, less if it does) may force the board to put a matter on the agenda, including director nomination, which will be discussed during the shareholders' meeting. They may justify their action in a statement which will be transmitted to the shareholders. Otherwise, shareholders cannot force the board to circulate any statement.

8 Controlling shareholders' duties

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

French law does not provide for any duties owed by controlling shareholders to the benefit of the company or to minority shareholders. However, case law prevents majority shareholders from voting in favour of resolutions taken against the company's interests with the sole purpose of favouring their own interests to the detriment of other shareholders. When this is characterised by the judge, the disputed vote may be declared null and void and the majority shareholders may be sentenced to pay damages.

9 Shareholder responsibility

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

The responsibility of shareholders is normally limited to the price paid for their shares.

However, the corporate veil may be pierced when a shareholder has de facto replaced the CEO and committed mismanagement acts, for example if it has commingled its assets and those of the company or caused the insolvency of the company by obvious misconduct.

In addition, parent companies may be held liable for damage caused by their subsidiaries: as regards environmental losses, if a mismanagement action can be assessed against the parent company; and if they belong to a large group (employing 5,000 persons in France or 10,000 worldwide), as regards human rights abuses, physical injuries or environmental losses, if the parent company has failed in the setting-up of a specific prevention plan and if a loss directly arises out of such failure.

Corporate control

10 Anti-takeover devices

Are anti-takeover devices permitted?

Anti-takeover devices are allowed under French law insofar as they abide by the corporate interest. Although France has implemented the Takeover Directive, it has often chosen not to adopt some options of the Directive.

Before a takeover bid is public, various measures may be implemented to thwart any offer, including:
- double voting right, which increases the number of shares that a bidder must acquire to gain the target's control;
- prior disclosure of shareholders' agreements provisions relating to share transfer (see question 12);

- share repurchase programmes (up to 10 per cent of the share capital); and
- delegations to the board to issue new shares or specific 'bid warrants'. Such warrants are designed to be attributed, if a takeover bid takes place, to existing shareholders for no consideration, in order to maintain the share ownership, being specified that if the bid fails, the company can finally decide not to issue the shares.

During the takeover bid, unless the articles of association provide otherwise, the board is no longer (as it formerly was) required to remain neutral and to submit any anti-takeover action to shareholders' approval. The board may also sell (or buy) a strategic asset, seek an alternative and friendly bid ('the white knight'), use delegation previously granted by the shareholders, etc. However, an approval is still necessary to perform a repurchase programme if it may harm the success of the bid.

11 Issuance of new shares

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

Shareholders' approval is necessary for the issuance of new shares but can be delegated to the board (which may then sub-delegate such power to the executive officers). Rights of issuance can be granted to the board with or without a preferential subscription right to shareholders. In such latter case, a priority right may be implemented in listed companies by the board, depending on the shareholder delegation's terms.

12 Restrictions on the transfer of fully paid shares

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

Restrictions on share transfers are compulsory in SARLs (prior approval of any transfer to a third party) and optional in other non-listed limited liability companies. If some or all shareholders agree to be bound by such restrictions, they are provided for in the articles of association or in shareholders' agreements (in which case they may remain confidential).

Shareholders of listed companies may include share transfer restrictions in shareholders' agreements only and such restrictions must be disclosed to the public when they relate to at least 0.5 per cent of the shares or voting rights, failing which the undisclosed agreement will have no effect during a takeover bid (see question 10).

Common restrictions include pre-emption rights, prior approval (by the shareholders' meeting, the board or a specific corporate body), tag-along and drag-along rights, standstill. But apart from the latter clause whose effect has to be limited in time, such restrictions may not harm the ability of a shareholder to exit the company if it has found a buyer (the transfer being made to this buyer or to the company or the other shareholders).

13 Compulsory repurchase rules

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

The shareholder of a non-listed company may force the company or other shareholders to buy its shares if the implementation of a prior approval clause contained in the company's articles of association has given rise to the refusal of the contemplated share transfer (see question 12).

Articles of association of an SAS and non-listed SA may contain drag-along rights or exclusion clauses (with objective exclusion causes and price determination rules) whereby a shareholder may be forced to sell its shares.

In listed companies, compulsory repurchase may only occur when 95 per cent of the shares and voting rights are held by a shareholder or shareholders acting in concert. Such bid may be triggered either by minority shareholders or by majority shareholders, or may follow a takeover bid at the successful bidder's initiative.

14 Dissenters' rights

Do shareholders have appraisal rights?

Minority shareholders do not have the right to sell their shares if they disagree with a decision of the company unless it is so provided in the articles of association or in a shareholders' agreement.

Certain restructuring transactions (such as a merger, a disposal of all or most of the company's assets, reorientation of the company's purpose, substantial changes to the articles of association) involving listed companies may lead to the AMF imposing on the majority shareholders to launch a takeover bid at fair market value (this is compulsory in the event of the conversion of an SA into an SCA).

The responsibilities of the board (supervisory)

15 Board structure

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

One-tier structured SAs are largely predominant, representing about 80 per cent of large issuers. About two-thirds of them are led by a CEO who is also the chairman of the board. Two-tier structured SAs represent about 15 per cent and SCAs about 5 per cent.

16 Board's legal responsibilities

What are the board's primary legal responsibilities?

The board of directors is the corporate body in charge of setting the main lines of the company's business activity and strategy and of ensuring their implementation, in accordance with the powers reserved by law to the shareholders and the company's executives. If the board is legally entitled to deal with any issue it considers relevant, it has by law exclusive competence in the following matters:
- drawing up of the annual (consolidated) accounts and management report;
- suggestion of dividends allocation;
- convening of shareholders' meetings and fixing their agenda;
- appointment and removal of the company's executives;
- authorisation of guarantees granted by the company and of transactions with related parties; and
- bonds' issuance (unless reserved to the shareholders' meeting by the articles of association).

In two-tier structures, the supervisory board's role is mainly to appoint (remove if permitted by the articles of association), control and supervise the executive board (eg, review of the accounts, management reports and strategy, prior approval of transactions with related parties) and refer to the shareholders' meeting. The executive board and the supervisory board may each convene shareholders' meetings.

17 Board obligees

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

The board has no legal personality and is only a corporate body that promotes and defends the company's interests.

Ultimately, the board is responsible to the shareholders, who can decide, at each meeting, to remove any of its members (including all of them). However, civil and criminal liability of directors may be sought where applicable either by the company itself or by shareholders (see question 18) (or third parties in limited cases and public prosecutor as regards criminal liability).

18 Enforcement action against directors

Can an enforcement action against directors be brought by, or on behalf of, those to whom duties are owed?

Legal actions may be brought against directors individually or collectively. The 'corporate' derivative action aims at indemnifying against losses suffered by the company itself as a result of faults of its directors. It can be initiated for the account of the company either by the company's legal representative or by a shareholder acting on behalf of the company. Shareholders may also bring an action in order to be indemnified for losses that they have directly suffered.

Such actions may only be brought in the event that directors have committed a breach of law or of the company's articles of association, or mismanagement acts. When the fault is committed collectively, the enforcement action is led against all directors taken individually, but each member of the board may elude its liability if it can prove that it opposed the disputed decision.

Criminal liability may be sought in specific cases, mainly in the event of misuse of corporate assets, abuse of powers, distribution of fictitious dividend and publications of untrue accounts. It may be initiated by any purported victim, but the legal action is controlled by criminal judges.

19 Care and prudence

Do the board's duties include a care or prudence element?

Directors owe a duty of care to the company at all times. Case law has promoted a specific duty of loyalty by board members in the event that such directors hold sensitive information and are involved in share transactions with other shareholders.

Internal rules of the board often describe more precisely the scope of such duty (eg, attendance of members, conflict of interests).

20 Board member duties

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

The duties of the various board members are the same and considered on an equal basis.

Directors may be members of specific board committees (audit (which is compulsory in listed companies), appointment, compensation, strategic, ethical, etc) and their work (and exposure) may so differ in practice. Usually, members of specific committees are chosen among directors with skills and experience corresponding to their field of expertise.

21 Delegation of board responsibilities

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

The board may delegate to the management some of its specific powers such as the authorisation of guarantees (by law), or the issuance of new shares (upon shareholders' approval).

The board may create committees in charge of monitoring specific questions. It can also appoint any person in order to perform specific tasks. But the aim of such committees or such appointments is only to facilitate or improve the work of the board and its decision-making process. Directors cannot ignore any of the matters discussed in board meetings: committees or individuals that the board has appointed always act under its authority.

22 Non-executive and independent directors

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

Companies listed on a regulated market must appoint at least one independent director at their audit committee. The Afep-Medef and Middlenext Codes require that at least half of the directors are independent or one-third in case of a company controlled by a majority shareholder or a group of shareholders. The Afep-Medef Code also provides that independent directors should represent two-thirds of the audit committee and the majority of the appointment and compensation committee if applicable.

The definition of independence is left by law to the board (or supervisory board). Governance codes propose criteria in order to assess independence, which may be adapted by companies to the extent that they explain their approach. For companies referring to the Afep-Medef Code, independent directors are defined as having no particular relationship (majority shareholder, employee, family, others) with the company's executives. According to these criteria, an independent director is someone who:

- has not been an employee or an executive officer for the last five years in the company or a related company;
- is not a significant supplier, a client or a financing institution; and
- has not been an independent director for longer than 12 years (renewal included). This last provision is specific to the Afep-Medef Code.

While they are expected to be particularly cautious of the company's interests, their liability does not differ by law from that of the other directors.

23 Board size and composition

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

The board size of between three and 18 members is ultimately determined by the shareholders. If they do not provide otherwise, no more than one-third of the directors may be over 70 years old. The same threshold applies for employees of the company.

Listed companies must appoint women in a proportion of at least 20 per cent of the members in large companies since 2014, this ratio rising up to 40 per cent in 2017. They must include at least one independent director (see question 22).

Before their appointment, shareholders may request information on the candidates' curricula vitae during the last five years, and in listed companies a brief summary of their expertise is always available. Apart from the specific requirement regarding the independent member of the audit committee, expertise is not required by law.

Criminal records are only provided to the AMF for listed companies during IPOs, but directors or supervisory board members in all companies must demonstrate that they have not been restricted from running a business owing to criminal proceedings.

The (supervisory) board may appoint temporary new members in the event of a vacancy, subject to confirmation by the next shareholders' meeting, while only the shareholders may create new directorships.

24 Board leadership

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

Laws and governance codes do not require the separation or joining of these functions but organise decision-making processes (including in terms of transparency) in this respect.

Historically, such functions were joint and such structure still prevails today (about two-thirds of SAs with a one-tier structure are managed by a CEO who is also the chairman of the board).

25 Board committees

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

The audit committee is mandatory in companies listed on a regulated market but the board of directors may decide to take over its functions directly. In such cases, when the agenda of the board meeting handles relevant matters of the audit committee, executive members of the board must temporarily leave. Only board members may be part of the audit committee, of which at least one independent director must have a specific financial expertise (see question 22).

Otherwise, the board may set up whatever committees it considers appropriate and has complete flexibility to organise them.

26 Board meetings

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

Legally, in one-tier structures, the board must meet at least once in order to draw up annual accounts and convene the annual shareholders' meeting (twice in listed companies, which have to publish half-year accounts).

In two-tier structures, the supervisory board has to meet at least four times a year in order to review the executive board's report.

However, in listed companies, corporate governance codes require more frequent meetings: the MiddleNext Code recommends a minimum of four meetings a year, whereas the Afep-Medef Code does not set a minimum requirement but provides that the number of meetings must be sufficient so as to enable the board to perform an in-depth review of all topics that are put on its agenda and that one meeting per year must be held without the presence of the executive officers.

27 Board practices

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

A listed company is required to disclose in a report established by the chairman of the board specific information on its operations and on the company's governance in general. Such information includes the structure of the board, the numbers and the overall attendance of the meetings during the last year, which governance code it applies and a review of the company's compliance with such code. Explanations on the items it has chosen not to enforce have to be disclosed under the 'comply or explain' principle.

28 Remuneration of directors

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

In consideration of their duties in such capacity, directors can only receive attendance fees, the global amount of which is decided by the shareholders' meeting. The split of such amount is, however, reserved to the (supervisory) board itself, being specified that governance codes recommend to allocate the fees in consideration of the attendance of each relevant member to the meetings, a criteria that should be predominant for the Afep-Medef Code. Directors are also reimbursed for the expenses incurred while carrying out their duties but no other compensation is allowed.

Directors' appointment term is legally capped at six years (renewable) but the shareholders may retain a shorter term of duties.

Loans to directors are prohibited and transactions between the company and directors (or relatives) are submitted to a prior approval by the board and subsequent review by the auditors and vote by the shareholders. Transactions that exceed one year must now be reviewed by the board.

29 Remuneration of senior management

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

The remuneration of senior management is determined by the (supervisory) board, and has, in listed companies, to be disclosed to shareholders and to the public and is submitted to a compulsory 'say on pay' vote (see question 37).

Governance codes intend to set effective criteria in order to give a general and consistent frame to the executive officers' compensation. Such criteria include benchmark, balance, intelligibility and consistency.

When variable compensation is provided, the AMF requires that it is calculated with respect to objective criteria fixed in advance.

Executive officers are in the same position as directors regarding loans or transactions with the company (see question 28).

30 D&O liability insurance

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

Directors' and officers' liability insurance is permitted and very common in companies having significant business exposure. Usually, companies pay the corresponding premiums.

31 Indemnification of directors and officers

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

As opposed to market practice in other jurisdictions, a French company never indemnifies managers acting in their professional capacity as any fault committed by them would likely give rise to a claim by the company itself against such managers or the purpose of the D&O liability insurance scheme, which is authorised by French law, would cover the relevant situation where the managers would incur personal liability (unless the acts having given rise to liability cannot legally be covered by an insurance policy).

32 Exculpation of directors and officers

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

Executive officers may delegate to employees part of their powers in specific matters and consequently preclude their personal, including criminal, liability (eg, in labour law or tax matters). To be effective, such delegation must be precisely determined and the assignee must be granted all resources and powers needed to perform the relevant tasks (including in the articles of association or otherwise).

There is no other way to preclude or limit the liability of directors and officers.

33 Employees

What role do employees play in corporate governance?

All companies employing at least 50 individuals have to set up a works council, which has to be periodically consulted and informed on various matters that include in some instances contemplated corporate governance changes. Representatives of the works council may attend all meetings of the corporate bodies and must be provided with the same level of information.

Two non-cumulative schemes exist in order to appoint one or several genuine directors representing the employees in companies listed on a regulated market according to a process provided for in the articles of association: when they have employees owning more than 3 per cent of the share capital; or when they employ, with their subsidiaries, more than 5,000 individuals (10,000 worldwide) and must set up a works council.

34 Board and director evaluations

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

French law requires the chairman of the (supervisory) board of each listed company to issue an annual report on the corporate governance in place within the company. The (supervisory) board has to approve the terms of this report. The statutory auditors must also give their views thereon.

The content of this report addresses most of the corporate governance issues: the frequency of the (supervisory) board meetings, options chosen when the 'comply or explain' principle applies, description of the (supervisory) board's and the committees' work, description of the compensation policies for executives and directors, review of the independence criteria applicable to the directors, etc.

Every year, the AMF reviews a sample of these reports and delivers a study, which is a major source of sound practices in corporate governance (see question 2).

Disclosure and transparency

35 Corporate charter and by-laws

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

All companies' articles of association are available at the companies registry and can be sent electronically. Corporate governance codes recommend that listed companies publish on their website their board and committee internal rules.

36 Company information

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

All companies must file specific corporate documents with the companies registry, such documents being publicly available (eg, articles of association, and shareholder resolutions amending the articles of association or appointing corporate bodies, merger agreements, statutory auditors and specific auditors' reports).

Listed companies have periodic disclosure obligations. In particular they must make publicly available their annual financial report (containing the annual accounts and notes thereto, management report, statutory auditors' report), half-year information (half-year accounts, interim management report, and statutory auditors' limited review report) and certain other information such as statutory auditors' fees and missions, data regarding repurchase programme, etc. Quarterly results are no longer subject to a disclosure obligation but listed companies usually continue to disclose them. The annual financial report is often presented in a document, filed with or controlled by the AMF, which contains all sections of a prospectus not related to a specific securities transaction (and which can be used, with a supplement containing all such sections, as a prospectus).

They also have an ongoing disclosure obligation, where they must disclose with no delay any non-public information that, if known to the public, would likely have a significant effect on the securities price (privileged information). The AMF regulations authorise the relevant issuer to postpone such disclosure in order to protect its legitimate interests, provided that the public is unlikely to be misled and the issuer ensures confidentiality of such information.

Hot topics

37 Say-on-pay

Do shareholders have an advisory or other vote regarding executive remuneration? How frequently may they vote?

Following intense debates, a new law has established a binding 'say on pay' vote for companies listed on regulated markets as regards remuneration of the corporate officers (CEO, deputy CEO, chairman of the (supervisory) board but excluding directors). Two votes are compulsory:

- a first vote must be organised to approve the general terms and structure of the fixed and variable pay of the corporate officers, it being specified that in the event of a negative vote, the existing terms or structure would survive; and
- subsequently, votes on the individual remuneration (fixed, variable and exceptional) of corporate officers must be organised after the relevant financial year, it being specified that the variable and exceptional remuneration may not be paid until a positive vote occurs.

Golden parachutes have to be authorised as transactions with related parties (the vote not being purely advisory; see question 4).

38 Shareholder-nominated directors

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

Before a meeting, shareholders holding a certain number of shares (5 per cent if the share capital does not exceed €750,000, less if it does) may force the board to put the appointment of a director on the agenda. All meeting materials (including those at shareholders' request or initiative) are prepared and distributed at the company's expense.

During shareholders' meetings, in the event that a director nomination is on the agenda or upon dismissal and appointment of a director, every shareholder may apply for the board position.

Regarding proxy solicitation, shareholders may freely consult the list of registered shareholders in order to contact and convince them to vote in a certain way. However, they have no right of access to the list of bearer shares' holders. The cost of proxy solicitation is assumed by the initiator of such solicitation. Anyone can actively solicit proxies if it discloses its voting policy.

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39 Shareholder engagement

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

French listed companies are increasingly engaging with shareholders beyond the mandatory, legal interactions at the time of the annual shareholders' meeting (through written or oral questions, resolution proposals, etc). The engagement efforts mainly depend on the size of the company: the larger it is, the more specific and dedicated staff it involves. The types of initiatives are also diversified (shareholders' clubs, social events, periodical information meetings, newsletters, etc).

Germany

Eva Nase and Georg Greitemann

P+P Pöllath + Partners

Sources of corporate governance rules and practices

1 Primary sources of law, regulation and practice

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

The primary sources for capital companies in Germany (GmbH, AG, KGaA, SE) are the German Limited Liability Companies Act (GmbHG), the German Stock Corporation Act (AktG), the European and German acts on European stock corporations (Societas Europaea, SE), the German Commercial Code (HGB), the Reorganisation of Companies Act (UmwG), the Takeover Act (WpÜG), the Securities Trade Act (WpHG), the applicable listing rules and the German Corporate Governance Code (DCGK), which differentiates between recommendations, which must either be complied with or deviations from which must be explained (comply or explain), and proposals, from which deviations are allowed without disclosure.

2 Responsible entities

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

The primary government agencies are the federal parliament and, to a growing extent, the EU legislators. The German Corporate Governance Code and its annual amendments are prepared and issued by the Government Commission for the German Corporate Governance Code. The listing rules are usually set by the stock exchanges or other listing entities.

The rights and equitable treatment of shareholders

3 Shareholder powers

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

The two most popular legal company forms are the stock corporation (AG) and the company with limited liability (GmbH).

The members of the supervisory board (non-executive directors) are elected by the shareholders (general meeting). The members of the management board (executive directors) are elected by the supervisory board and not by the shareholders. This basic structure cannot be altered. Unless the articles of association provide otherwise, members of the supervisory board are elected by the simple majority of votes and can be removed with a 75 per cent majority of the votes. Unless the AG has entered into a control agreement with its parent company, the supervisory board and the management board act independently and cannot be required by the shareholders to pursue a particular course of action.

Unless the articles stipulate otherwise, the GmbH only has managing directors and no supervisory board. The managing directors are appointed and removed by the shareholders (shareholders' meeting) with a simple majority. The shareholders' meeting can require the managing directors to pursue a particular course of action.

The legal forms of a European stock corporation (SE) and a partnership limited by shares (KGaA) are, to a great extent, comparable to a German stock corporation (AG).

4 Shareholder decisions

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

The following selected decisions are reserved by law for the shareholders of a stock corporation (AG):

- election and removal of the supervisory board members;
- appointment of the auditor;
- appropriation of profits;
- formal approval of action for members of both the management board and supervisory board; and
- fundamental decisions, in particular amendments to the articles of association, liquidation of the corporation, merger, demerger, change of legal form, sale of substantially all of the corporation's assets, and conclusion of corporate agreements (control agreements, profit and loss pooling agreements).

The following decisions are reserved by law for the shareholders of a company with limited liability (GmbH):

- election and removal of the managing directors and conclusion of their service agreements;
- approval of the annual accounts;
- appointment of the auditor;
- appropriation of profits;
- formal approval of action for managing directors;
- fundamental decisions, in particular amendments to the articles of association, liquidation of the corporation, merger, demerger, change of legal form, sale of substantially all of the corporation's assets, and conclusion of corporate agreements (control agreements, profit and loss pooling agreements); and
- instructions to the managing directors.

Matters that are subject to a non-binding shareholder vote are rather uncommon in German law.

5 Disproportionate voting rights

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

In a stock corporation (AG), one share cannot carry more than one vote per share (in case of shares without nominal value) or one vote per euro of nominal value (in case of shares with a nominal value). The articles of association of a non-listed AG can provide for limits on the exercise of voting rights.

In a company with limited liability (GmbH), disproportionate voting rights or limits on the exercise of voting rights are allowed.

6 Shareholders' meetings and voting

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

In a stock corporation (AG), a European stock corporation (SE) and a partnership limited by shares (KGaA), shareholders cannot act by way of written consent without a meeting. Semi-virtual meetings of shareholders are permitted. The articles of association can provide for the requirement to register within a time frame of at least six days prior to the general meeting. In case of listed companies, such registration must be made by way of a specific depositary statement referring to the shareholding on the 21st day prior to the general meeting.

In a company with limited liability (GmbH), shareholders can act by way of written consent without a meeting. Virtual meetings of shareholders are permitted.

7 Shareholders and the board

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

In a stock corporation (AG), a European stock corporation (SE) and a partnership limited by shares (KGaA):

- shareholders holding at least 5 per cent of the registered share capital can require meetings of shareholders to be convened; and
- shareholders holding at least 5 per cent of the registered share capital or shares with a nominal amount of at least €500,000 can require resolutions to be put to a shareholder vote against the wishes of the supervisory board or management board, if such request is received by the company 24 days prior to the general meeting and, in case of a listed company, 30 days prior to the meeting.

Shareholders' requests to add to the meeting agenda must be published, potentially together with a statement from the management and supervisory board.

Counterproposals made by shareholders to the resolution proposals made by the management and supervisory board must be submitted to the shareholders, also potentially together with a statement of the management and supervisory board. In the case of listed companies, counterproposals and the company's statements thereto must be published on the company website.

In a company with limited liability (GmbH), shareholders holding at least 10 per cent of the registered share capital can require meetings of shareholders to be convened or require resolutions to be put to a shareholder vote against the wishes of the managing directors.

8 Controlling shareholders' duties

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

All shareholders have a fiduciary duty towards the company and towards the other shareholders. The fiduciary duty of controlling shareholders is more intense than the fiduciary duty of non-controlling shareholders. In a stock corporation (AG) with a controlling shareholder, the controlling shareholder and its boards are subject to certain additional statutory duties. Enforcement actions can be brought against controlling shareholders and, under certain circumstances, their representatives for breach of these duties.

9 Shareholder responsibility

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

Based on corporate law, shareholders can be held responsible for the acts or omissions of the company only under exceptional circumstances. This may happen where the company acts through its shareholders. For example, if the company with limited liability (GmbH) has no managing directors, the shareholders are obliged to file for insolvency if the company is insolvent. Failure to do so will result in liability of the shareholder.

There are certain other areas of the law, which provide for responsibility of shareholders for acts or omissions of the company, including without limitation antitrust law, data protection law and criminal law.

Corporate control

10 Anti-takeover devices

Are anti-takeover devices permitted?

In public takeover bids, the management board is allowed to take pre-bid and certain post-bid defensive measures in accordance with the Takeover Act.

Pre-bid defences

The target's shareholders' meeting can authorise the management board to take action to prevent the success of any takeover bid, subject to approval of a defensive action (if and when taken) by the supervisory board. This authorisation is valid for 18 months and requires a qualified majority (75 per cent of the share capital represented at the general meeting). Furthermore, the shareholders' meeting can decide on capital measures or it can authorise the management board to acquire the company's own shares or to issue convertible bonds.

Post-bid defences

After the takeover announcement, the management board must refrain from any frustrating action. However, the management board can seek alternative bids (white knight defence) or take actions, which a prudent and conscientious director of a company not subject to a public takeover bid would have taken. Moreover, it can take defensive actions approved by the target's supervisory board, respectively approved by the shareholders' meeting (see above), or call a shareholders' meeting following the takeover announcement to vote on the defensive action. The notice periods are significantly shorter than with regard to ordinary shareholders' meetings. If this meeting is convened, the offer period is extended to 10 weeks to allow the shareholders' meeting to take place before the offer expires. Finally, the boards can influence the shareholders to refuse a hostile takeover bid when giving their reasoned opinion. In this respect, the management board and the supervisory board must consider the transparency principle and avoid misleading statements.

European opt-in

A German listed company can opt out of the German rules for defensive action and opt in to the rules set out in the Takeover Directive (Directive 2004/25/EC) and implemented in the Takeover Act by amending the company's articles. By disapplying the opt-in, the target is automatically subject to the rules of the Takeover Act on defensive actions.

Breakthrough

Also, the articles of a German listed company may apply the 'breakthrough clause' of the Takeover Directive as implemented in the Takeover Act, under which certain transfer restrictions and restrictions on exercising voting rights in certain contracts do not apply under certain circumstances.

Publication of defence measures

All listed German companies must give detailed information on all existing defence mechanics in the management report that forms part of the company's annual financial statements. The supervisory board must comment on this information in its own statement for the annual general meeting.

11 Issuance of new shares

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

The general meeting of a stock corporation (AG), a European stock corporation (SE) and a partnership limited by shares (KGaA) can authorise the management board, subject to the approval of the supervisory board, to issue new shares ('authorised capital'). Authorised capital may not exceed 50 per cent of the registered share capital. Statutorily, shareholders do have pre-emptive rights. With a 75 per cent majority pre-emptive rights can be excluded, even in management board's authorisations to issue new shares. Yet, proxy voters only approve such authorisations for exclusions of pre-emptive rights under certain requirements and to a certain percentage of the authorised capital (often 20 per cent).

Similarly, the shareholders' meeting of a GmbH can authorise the managing directors to issue new shares ('authorised capital'). Authorised capital may not exceed 50 per cent of the registered share capital. Under applicable case law, shareholders of a GmbH have pre-emptive rights to acquire newly issued shares, subject to certain exceptions and exclusion mechanisms.

12 Restrictions on the transfer of fully paid shares

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

Restrictions on the transfer of fully paid shares in listed stock corporations (AG, SE or KGaA) are not permitted. Restrictions on the transfer of fully paid shares in non-listed companies are permitted and customary. In closed companies, the transfer of shares is usually subject to the prior approval of the supervisory board, shareholders' meeting or general meeting. Other customary restrictions include a right of first refusal or a tag-along right.

13 Compulsory repurchase rules

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

Compulsory share repurchases are not common in German law and practice. They may be allowed in certain exceptional cases.

14 Dissenters' rights

Do shareholders have appraisal rights?

Shareholders have the right to sell their shares to the company at a fair value in case of certain types of mergers or similar transactions (eg, entering into a domination and/or profit and loss pooling agreement, change of legal form, squeeze-out, delisting, etc).

The responsibilities of the board (supervisory)

15 Board structure

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

The predominant board structure of a stock corporation (AG), a European stock corporation (SE) and a partnership limited by shares (KGaA) follows the two-tier system with a management board, managing and representing the company, and a supervisory board supervising the management board. A one-tier system with one board consisting of executive and non-executive board members is only allowed in Germany within an SE.

Most companies with limited liability (GmbH) only have managing directors, which are all executive directors. They can have a supervisory board or advisory board, resulting in a two-tier structure. In cases of co-determination, a supervisory board is compulsory in a GmbH. A GmbH cannot have a one-tier board that includes the executive and non-executive directors.

16 Board's legal responsibilities

What are the board's primary legal responsibilities?

The supervisory board has the power to appoint and dismiss members of the management board, as well as the responsibility to supervise the management board's activities. So far, the supervisory board is entitled to request – regularly and irregularly – reports from the management board and to define certain transactions and measures in the articles of association of the company, the rules of procedure of the management board or in individual cases that are subject to the supervisory board's approval. However, such approval does not have any effect on the transactions or measures vis-à-vis third parties, but only on the internal relationship between the two bodies.

17 Board obligees

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

The supervisory board does not represent anybody in fulfilling its own legal duties. The supervisory board shall rather be independent to a great extent. Supervisory board members, who may be delegated or elected from a certain shareholder majority, are not allowed to pass on any information received in their function as members of the supervisory board to the respective shareholder. Consequently, supervisory board members must always act in the best interest of the company, which itself is defined by the 'stakeholder model' (opposite to the Anglo-Saxon shareholder model with a respective acting in the best interest of a shareholder).

18 Enforcement action against directors

Can an enforcement action against directors be brought by, or on behalf of, those to whom duties are owed?

Managing directors of a GmbH may be instructed to take or to refrain from taking certain measures by way of a shareholder resolution (see question 3). Management board members of a stock corporation (AG) and a European stock corporation (SE) are, vice versa, entitled to manage the company in their own discretion. Consequently, neither the general meeting nor the supervisory board is allowed to adopt management decisions and to bring forward enforcement action against members of the management board. However, the supervisory board is entitled and, according to case law, obliged to assert liability claims against the management board, if the company suffered damages due to breach of tasks and duties by the management board.

19 Care and prudence

Do the board's duties include a care or prudence element?

Managing directors of a company with limited liability (GmbH) and management board members of a stock corporation (AG), a European stock corporation (SE) and a partnership limited by shares (KGaA) do have to apply the care of a prudent and diligent businessperson. Also, in supervising the management board of an AG or SE, the supervisory board has to follow this principle.

20 Board member duties

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

Generally, supervisory board members have the same rights and duties. However, applicable law and the DCGK provide for the requirement of appointing individual members with certain skills, for example financing, reporting and auditing expertise. Thus, these members' duties differ from the other members' duties. Hence, the differences in duties do not reflect a higher liability exposure.

21 Delegation of board responsibilities

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

The supervisory board is not allowed to adopt management responsibilities and, vice versa, is not allowed to delegate supervising functions to the management board or to other persons. The supervisory board is, however, entitled to implement committees from its midst. In some instances, such as with respect to the management board members' service agreements, the committees are statutorily not entitled to resolve on such matters instead of the supervisory board, but only to prepare the respective resolutions of the supervisory board and to supervise their execution. Also, the board may ask a board member to prepare a certain topic. Yet, the responsibility to decide upon such topic remains in any instance with the supervisory board.

22 Non-executive and independent directors

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

In the case of a one-tier system within a European stock corporation (SE) (see question 15), applicable law requires that the majority of the members of the board must be non-executive. Members are non-executive if they are not registered as managing directors of the SE with the commercial register. If they are registered as managing directors, they have the power to manage and represent the company. Non-executive members are not allowed to do so, but are only entitled to supervise the executive directors (ie, the managing directors) within the internal relationship.

23 Board size and composition

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

The supervisory board of a stock corporation (AG), a European stock corporation (SE) and a partnership limited by shares (KGaA) must have at least three members. Unless the stock corporation is co-determined (meaning that one-third or half of the board members are elected by the employees), the supervisory board may also consist of any higher number of members, up to 9, 15 or 21 members, depending on the registered share capital of the corporation. In case of statutory co-determination, the number of members must be divisible by three. In case of equal co-determination, the total number of supervisory board members is dependent on the total number of German employees.

Shareholder representatives on the supervisory board are generally appointed by the general meeting; employee representatives in cases of co-determination generally by employee elections. In case of vacancies, under certain circumstances, members can, upon filing, also be appointed by a court.

24 Board leadership

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

In the German two-tier-system, the CEO (and other members of the management board), managing and representing the company, is strictly separated from the supervising function of the supervisory board. Both bodies are not allowed to adopt functions of the respective other body (see questions 21 and 22). In case of a one-tier-system, within a European stock corporation (SE) the CEO and chairman of the board may be the same person without any separation requirement.

25 Board committees

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

The supervisory board is entitled to establish committees from its midst. In some instances, the committees are statutorily not entitled to resolve on matters instead of the supervisory board, but only to prepare resolutions of the supervisory board and to supervise their execution. According to the DCGK, a listed stock corporation (AG), European stock corporation (SE) and partnership limited by shares (KGaA) need to implement an audit committee and a nomination committee for nominating the supervisory candidates.

26 Board meetings

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

Supervisory boards of listed companies are statutorily requested to hold four meetings a year. Supervisory boards of non-listed companies are entitled to resolve on the holding of only two meetings per year. In any case, the supervisory board has to report on the number and main topics of its meetings in its annual report to the general meeting.

27 Board practices

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

As mentioned in the answer to question 26, the board is statutorily obliged to report on its constitution, its meetings, the attendance thereof and its supervising activities in its yearly report to the general meeting. The same applies to the work of its committees.

28 Remuneration of directors

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

The AktG as well as the DCGK provide for specific rules, to which the supervisory board has to adhere when resolving upon fixed and variable remuneration of the management board members – the latter is differentiated between short-term and long-term incentives – as well as on loans or other compensatory arrangements (eg, stock options). Also, the general meeting is legally entitled to resolve on the management boards' remuneration (say-on-pay). However, this resolution is of a declaratory nature only (ie, the supervisory board's responsibility to decide upon the remuneration remains unaffected thereby). Service contracts may be entered into for five years at the utmost with the right of renewal.

29 Remuneration of senior management

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

The responsibility to decide upon senior management's cash compensation is statutorily addressed to the management board. The supervisory board can, however, foresee approval requirements with respect to cash compensation and other advantages like granting of cars. According to applicable law, the granting of stock options to senior management requires a resolution of the general meeting, which has to fulfil certain statutory requirements, and the approval of the supervisory board.

30 D&O liability insurance

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

D&O liability insurances are permitted and common practice for management and supervisory board members in listed companies. Yet, they are also becoming more popular in non-listed companies. Premiums are generally paid by the company. However, members of the management board of a stock corporation are obliged to bear a deduction between 10 per cent of the damage and one and a half times his or her fixed salary. With respect to supervisory board members, a respective deduction is recommended by the DCGK.

31 Indemnification of directors and officers

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

Besides the granting of D&O insurance coverage, indemnifications by a stock corporation (AG), a European stock corporation (SE) and a partnership limited by shares (KGaA) are not permitted, as the company is only allowed to waive or settle on liability claims against management board members three years following their accrual and only subject to a general meeting's approval without an objection of a shareholder minority jointly representing 10 per cent of the registered share capital.

In a German company with limited liability (GmbH), as German law follows the stakeholder model, according to which managing directors have to act in the best interest of the company (and not the shareholder or the majority of shareholders), indemnification agreements are subject to fiduciary duties' constraints. Also, indemnifications by a GmbH are not allowed, if and to the extent that the managing directors have breached capital protection rules.

32 Exculpation of directors and officers

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

A preclusion is not allowed within a stock corporation (AG), a European stock corporation (SE) and a partnership limited by shares (KGaA). The supervisory board is responsible and, according to case law, obliged to assert liability claims against management board members (see question 31).

33 Employees

What role do employees play in corporate governance?

The management board is obliged to implement proper corporate governance and to continuously supervise its functionality. Therefore, the management board is allowed to deploy employees by way of vertical instruction and is thus dependent on the fulfilment of the employees' tasks and duties. This fulfilment is itself subject to supervision by the management board.

34 Board and director evaluations

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

No such evaluations are provided for, either statutorily or according to regulation or listing requirements. This applies to both management and supervisory board.

Disclosure and transparency

35 Corporate charter and by-laws

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

The deed of incorporation and the articles of association of German companies are publicly available. They are available through the commercial register, which is administered and managed by the local courts. The online commercial register (www.handelsregister.de) includes and allows downloading of all commercial register documents submitted since 2007. The articles of association of listed companies are generally also available through their websites.

The by-laws of companies (meaning rules of procedure for the supervisory board, supervisory board committees, the management board or the managing directors) are generally not publicly available. Some listed companies publish their by-laws on their websites.

Update and trends

Shareholder interest and activism focuses on the election of a certain number of supervisory board seats, in order to be informed and able to have at least factual control over the management board. Also, shareholders use the public to address their concerns and wishes with respect to business operations and management board activities. In parallel, such shareholders more often take short-selling positions in the shares of the listed companies. Wirecard AG, Stada AG and Ströer SE are the most recent examples of shareholder activism in Germany.

36 Company information

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

Companies must publicly disclose their annual accounts. Listed companies may be required to disclose more financial documents, such as half-year or quarterly reports.

Companies must publicly disclose certain information regarding changes to their shareholder structure and certain other information (eg, capital increases).

Companies must file certain information and documents with the commercial register, which can be accessed by the public.

In addition, companies whose shares are listed in an organised market must disclose:

- insider information through ad hoc notifications;
- subject to receiving such information from shareholders, the increase and decrease of their shareholdings (3, 5, 10, 15, 20, 25, 30, 50 and 75 per cent), as well as the increase and decrease of positions in financial instruments with the same percentage rates except for the 3 per cent threshold;
- subject to receiving director's dealings notifications, information thereupon; and
- an annual statement on compliance with the German Corporate Governance Code (comply or explain, see question 1).

Hot topics

37 Say-on-pay

Do shareholders have an advisory or other vote regarding executive remuneration? How frequently may they vote?

The general meeting of a stock corporation (AG), a European stock corporation (SE) and a partnership limited by shares (KGaA) has an advisory vote on the remuneration of the members of the management board (see question 28). It cannot be objected to by voidance claim.

38 Shareholder-nominated directors

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

As the members of the management board of a stock corporation (AG), a European stock corporation (SE) and a partnership limited by shares (KGaA) are not elected by the shareholders' meeting, shareholders of a stock corporation do not have the ability to nominate members of the management board. As regards members of the supervisory board, candidates are to be proposed to the general meeting by the supervisory board. However, shareholders are entitled to make counterproposals to the resolution proposals made by the supervisory board (see question 7). Apart from this, the model of a shareholder-nominated director is not foreseen in German law and regulations.

Shareholders of a company with limited liability (GmbH) have the ability to nominate managing directors and have them included in shareholder meeting materials that are prepared and distributed at the company's expense.

39 Shareholder engagement

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

Listed companies generally do not engage with their shareholders, in particular not outside the ordinary or extraordinary general meetings. In preparing such meetings, the CEO has calls with shareholder representatives and potential proxy voters. However, the CEO does abstain from providing them with any information that the CEO has not already disclosed in the invitation to or does not intend to disclose in general meeting to all other shareholders.

However, the Government Commission for the DCGK has stated that dialogue between the supervisory board and investors is the best practice of German good corporate governance. It has therefore proposed to add a respective proposal to the DCGK that the chairman of the supervisory board should, to an appropriate extent, be in regular conversation with investors on supervisory board issues. The DCGK's inclusion of such proposal became effective on 27 April 2017. Yet, if a listed company denies following such proposal, it must neither explain such denial nor its reasons (see question 1).

Closed companies typically engage with their shareholders, as is the case in the majority of jurisdictions.

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Sources of corporate governance rules and practices

1 Primary sources of law, regulation and practice

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

The Companies Act 2013 (the Companies Act), which replaced the former Companies Act 1956 (the 1956 Act) on 1 April 2014, and the regulations issued by the Securities and Exchange Board of India (SEBI) are the primary sources of Indian corporate governance regulation.

The SEBI (Listing Obligations and Disclosure Requirements) Regulations 2015 (the Listing Regulations) specify the obligations of 'listed entities', a term that includes not only those entities that have listed their equity shares, but also those that have listed other instruments, including non-convertible debt securities, non-convertible redeemable preference shares, perpetual debt instruments, perpetual non-cumulative preference shares, Indian depository receipts, securitised debt instruments and units issued by mutual funds. The Listing Regulations make it mandatory for companies that have listed their equity shares and convertible securities to comply with certain requirements to ensure transparency in the management of such companies, such as the inclusion of independent directors, regulation of the remuneration of non-executive directors, constitution of various committees, disclosures on related-party transactions, accounting treatment, maintenance of a minimum frequency of meetings of the board of directors and limitation on the number of committees a director can be a chairman or member of. The Listing Regulations also require the adoption of a written code of conduct for all members of the board and senior management of every listed company. It is mandatory for listed companies to comply with the Listing Regulations. Any failure on the part of a listed company to comply with the Listing Regulations may lead, inter alia, to one or more of the following consequences: imposition of fines, suspension of trading; freezing of promoter or promoter group holding of equity shares and other actions being initiated by SEBI. Unlisted and closely held Indian companies are subject to the corporate governance norms contained in the Companies Act.

Additionally, the Securities Contracts (Regulation) Act 1956, the Securities and Exchange Board of India Act 1992, and the rules and regulations framed thereunder (particularly, the Securities and Exchange Board of India (Substantial Acquisition of Shares and Takeovers) Regulations 2011 (the Takeover Code), the Securities and Exchange Board of India (Prohibition of Insider Trading) Regulations 2015 (the Insider Trading Code) and the Securities and Exchange Board of India (Issue of Capital and Disclosure Requirements) Regulations 2009), and the Depositories Act 1996, also deal with corporate governance initiatives.

2 Responsible entities

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

The primary Indian implementation entities of corporate governance initiatives are SEBI (the primary regulator of the Indian securities market and listed companies) and the Ministry of Corporate Affairs (MCA), government of India.

Other entities responsible for the enforcement of corporate governance issues include:

- the National Company Law Tribunal (the Tribunal) under the Companies Act, having quasi-judicial powers to decide certain matters under the Companies Act, including the protection of minority shareholders from oppression by majority shareholders and mismanagement, and its appellate authority, the National Company Law Appellate Tribunal;
- the Registrar of Companies (RoC), which generally has its presence in every Indian state, and primarily ensures compliance by a company in relation to filings and disclosures under the Companies Act;
- the Regional Director (RD), to which certain powers of the Central Government have been delegated. There are seven RDs in India, each with their own territorial jurisdiction, in which they, inter alia supervise the working of the relevant RoCs; and
- the Competition Commission of India (CCI), created under the aegis of the Competition Act 2002, which regulates antitrust issues where a company's action may have an adverse effect on competition in the relevant Indian market.

The concept of shareholder activist groups or proxy advisory firms is emerging in India. The SEBI (Research Analysts) Regulations, 2014 (the Analyst Regulations) define a 'proxy adviser' as any person who provides advice, through any means, to an institutional investor or shareholder of a company, in relation to exercise of their rights in the company including recommendations on public offer or voting recommendation on agenda items. Institutional Investor Advisory Services India Limited (IiAS) and InGovern, both established in 2010, are prominent proxy advisory firms operating in India. Stakeholders Empowerment Services, a corporate governance research and advisory firm, claims to be the first company to have registered as a 'proxy adviser' under the Analyst Regulations, however these firms are not formally consulted by the authorities prior to promulgation of corporate governance initiatives. Usually, committee recommendations and proposed regulatory norms are put up for public comment by concerned authorities in order to ensure large-scale participation. The National Foundation for Corporate Governance, set up by the MCA as a not-for-profit trust, in association with the Confederation of Indian Industry, the Institute of Chartered Accountants of India and the Institute of Company Secretaries of India (ICSI) also provide a platform for spreading awareness regarding corporate governance issues.

The rights and equitable treatment of shareholders

3 Shareholder powers

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

An Indian public company is required to have at least two-thirds of its directors liable to vacate their position by rotation. Such directors are appointed by the shareholders in general meetings by an ordinary resolution of the company, and they are required to retire within a maximum period of three years from their appointment date. Any reappointment of such directors requires fresh shareholders' approval. Unless the articles of association (AoA) provide otherwise, the remaining directors of a public company and the directors of a private company (a company that restricts the number of its shareholders to 50), are also required to be appointed with shareholders' approval. Thus, in India, shareholders generally have a say in the appointment and reappointment of directors. In the absence of a higher requirement adopted by a company in its AoA, directors are appointed by a simple majority vote. The Companies Act also provides companies with an option to adopt a proportional representation mechanism for director appointments, so as to enable the representation of minority shareholders on the board.

To ensure wider shareholder participation in listed companies, the Companies Act provides for the appointment of one director by small shareholders of the listed company, where 'small shareholder' means a shareholder holding shares whose nominal value does not exceed 20,000 rupees. The Rules notified under the Companies Act specify that a listed company may either opt to have a small shareholders' director suo moto, or appoint one upon receiving notice from at least 1,000 small shareholders of the company or one-tenth of the total number of small shareholders of the company, whichever is lower. A small shareholders' director is an 'independent director' under the Companies Act and is not liable to retire by rotation; however, his or her tenure cannot exceed three years, and at the end of the tenure he or she is not eligible for reappointment.

The shareholders have inherent powers to remove directors (including non-retiring directors) by a simple majority vote, provided a special notice to this effect has been served on the company by shareholders holding at least 1 per cent of the paid-up share capital of the company or holding shares on which at least 500,000 rupees have been paid up on the date of the notice, at least 14 clear days prior to the ensuing general meeting (excluding the day when the notice is served and the day of the meeting); a copy of such special notice has been forthwith provided by the company to the directors proposed to be removed, and the directors are given an opportunity to present their case before the shareholders either in writing or at the general meeting convened to consider their removal. The company is required to give special notice to the members of a general meeting convened for such a resolution at least seven days before the meeting. Directors appointed by the Tribunal under the provisions of the Companies Act and directors appointed by the proportional representation mechanism cannot be removed by the shareholders.

Generally, the board is vested with the company's management powers and the shareholders are only entitled to exercise control over those matters that are specifically reserved under the Companies Act or the company's AoA, for shareholders' approval. Thus, generally, the shareholders cannot interfere in the board's decision-making process or usurp any authority available to them. However, shareholders, by virtue of their authority to appoint or remove directors, can control the overall board composition and can sometimes transact businesses, which for any reason cannot be transacted by the board, including resolving matters, in the event of there being a deadlock between directors or there being an inadequate quorum at the board level. The Companies Act specifically empowers shareholders holding at least 10 per cent of the paid-up share capital of the company to cause the company to notify its shareholders of any resolution proposed to be moved at a meeting of the shareholders, provided such a requisition is deposited with the company at least six weeks before the meeting in case the requisition would trigger the requirement of circulating a notice of the proposed resolution, and at least two weeks before the meetings for all other requisitions. Further, judicial pronouncements also suggest that when the directors act mala fide or act extraneously to their powers and are the wrongdoers, the shareholders are entitled to take steps for redressal.

4 Shareholder decisions

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

The Companies Act mandatorily requires shareholder approval for certain decisions including, among others, those relating to:

- change in name, registered office or authorised share capital;
- modification of the memorandum of association and AoA of the company;
- issuance of shares on a preferential basis;
- approval of audited accounts;
- declaration of dividends;
- appointment and removal of auditors;
- appointment and removal of directors and determining their remuneration;
- appointment of more than 15 directors to the board;
- reappointment of independent directors after the expiry of their term;
- approving loans to directors;
- disposal of a company's undertaking;
- borrowing and investing a company's funds beyond certain limits;
- approving any scheme of arrangement or compromise;
- a reduction in capital;
- buyback of securities;
- liquidation of a company;
- specified related-party transactions;
- application to change the status of the company to 'dormant';
- variation in the rights of shareholders; and
- approving the directors' holding of an office of profit (other than that as managing directors or managers) with the company or its subsidiaries.

The Companies Act does not provide a mechanism for a non-binding shareholders' vote. Though the primary authority to call general meetings and decide the agenda lies with the board, the shareholders are permitted to requisition general meetings to carry out proposed business or demand the circulation of resolutions proposed by them for consideration at the ensuing board-initiated general meeting. Any decisions on resolutions so initiated by shareholders, if approved by the requisite majority as prescribed under the Companies Act and the company's AoA, bind the board. For further information, see questions 3 and 7.

5 Disproportionate voting rights

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

Indian listed entities are prohibited from issuing shares in any manner that may confer on any person superior rights as to voting or dividend vis-à-vis the rights on equity shares that are already listed as per regulation 41 of the Listing Regulations. However, private limited companies and unlisted public companies are permitted to issue equity shares with a disproportionate right as to voting, dividends or otherwise, subject, inter alia, to the existence of a specific authority in this regard in their AoA and shareholders' approval. The preconditions to be met by a company for such an issuance are prescribed in the Companies (Share Capital and Debentures) Rules, 2014, including having a consistent track record of distributable profit for the last three years, and at any time, shares with differential rights cannot exceed 26 per cent of the total paid-up equity share capital of the company (including equity shares with differential rights). Companies are not under any limitation while determining disproportionate rights. Though equity shares with zero voting rights are generally considered extraneous to the Companies Act, through an amendment to the Companies Act in June 2015, the restriction in the Companies Act in regard to non-voting equity shares has been made inapplicable to private companies, subject to appropriate authorisation in the AoA, and therefore, private companies, which are not subsidiaries of public companies, are able to issue equity shares with zero voting rights. This flexibility will benefit private companies that want to obtain equity funding without dilution of control.

Preference shareholders do not have voting rights at general meetings, except on resolutions that directly affect their rights. However, voting rights on a par with the equity shareholders accrue to them in the event of the company defaulting in the payment of dividends to preference shareholders for a period of two years or more.

6 Shareholders' meetings and voting

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

Shareholders who are recorded in the register of members or in the records of the depository (for paperless shares) are entitled to attend and vote at general meetings. In the case of bearer securities (such as share stocks), when the shareholders present proof of ownership of the company's shares, as per the AoA, they become entitled to attend and vote at general meetings.

Shareholders who are natural persons can either attend general meetings themselves or appoint a proxy to attend and vote at the meeting. Shareholders who are legal entities are required to appoint natural persons as their authorised representatives to attend and vote at general meetings. These representatives can exercise all powers of the original shareholders including appointing a proxy. Proxies are prohibited from speaking at the meetings and unless the AoA provide otherwise, they can vote only by poll (and not by show of hands). The Companies Act prohibits a person from acting as proxy on behalf of more than 50 members, and members whose aggregate holding in the company exceeds 10 per cent of the total share capital of the company. When there is a show of hands, every shareholder has one vote irrespective of his or her shareholding in the company and on poll (if requisitioned) every shareholder has voting rights in proportion to his or her share in the company's paid-up equity capital.

If there are partly paid-up shares, voting rights are conferred based on the amount paid up on such shares and such rights would be unavailable on partly paid-up shares on which calls remain unpaid. For listed companies, and companies with more than 200 shareholders, approval on certain items requires the adoption of a postal ballot mechanism, in which votes are cast through postal ballots dispatched by the company to each of its shareholders individually. The Rules mandatorily require certain business to be transacted only by voting through postal ballot, including the following:

- alteration of the objects clause of the memorandum of association;
- change in the location of the registered office outside specified limits;
- issue of shares with differential rights;
- buyback of shares; and
- the disposal of a company's undertaking.

For voting rights available to preference shareholders, see question 5.

Shareholders may also participate in meetings through video conferencing and vote electronically through secure electronic platforms, since the Rules notified under the Companies Act make it mandatory for listed companies and companies with more than 1,000 shareholders to provide an electronic voting facility to its members for all general meetings. A 'virtual meeting' of the shareholders of a company, that is, a meeting without any physical venue, is not permissible under the Companies Act, as minimum quorum requirements, which are applicable shareholders' meetings of public companies and private companies, require the requisite number of members to be personally present at the venue of such meeting.

7 Shareholders and the board

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

Typically, the board convenes a company's general meetings. However, shareholders holding 10 per cent of the company's paid-up share capital, by a written notice, may requisition the board to convene an extraordinary general meeting. If the board fails to call a meeting within 21 days from the date of deposit of a valid requisition on a day not later than 45 days from the original requisition date, the shareholders may themselves proceed to convene an extraordinary general meeting within a period of three months from the date of the requisition.

Shareholders holding 10 per cent or more of the company's total voting power may requisition the company to circulate, along with the notice of a general meeting, any resolution that they intend to move at such meeting, along with a statement of the proposed matter to be dealt with in the resolution. However, the Companies Act does not provide for the circulation of statements by the board as received from dissident shareholders, who only have a right to discuss their views in a meeting and challenge the unfavourable decisions against them before the Tribunal in certain circumstances.

8 Controlling shareholders' duties

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

Controlling shareholders are expected not to oppress or act against the interests of the minority. Minority actions are allowed in cases of majority shareholders of a company proposing to benefit themselves at the expense of the minority, expropriating minority rights by carrying out modifications in charter documents or taking actions to oust the minority by the improper issuance of shares or otherwise.

Under the Companies Act, 100 shareholders in number or one-tenth of the total number of shareholders of a company, or shareholders holding not less than 10 per cent of the issued share capital of a company can bring actions against the controlling majority or the board, where the affairs of the company are being conducted in a manner oppressive to any shareholder; or in cases of mismanagement prejudicing the interests of the company or the public at large. Recently, in the ongoing dispute between Mr Cyrus Mistry and Tata Sons Limited, the Tribunal held that the term 'issued share capital' in the context of determining the qualification of shareholders to initiate an action for oppression and management before the Tribunal, includes preference capital as well, and therefore the complainants must, in aggregate, hold at least 10 per cent of the issued share capital of the company, which includes its preference capital, unless this requirement is waived by the Tribunal. On the issue of waiver of this requirement, the Tribunal held that such waiver is to be granted only in rare and compelling situations and further that the Tribunal shall only interfere if the actions of the board or majority are unconscionable, unjust and fraudulent, so as to cause oppression to the complaining party.

To protect the interests of minority shareholders, the Companies Act also provides for class action by members of a company seeking restraining orders against certain actions of the company and for claiming damages or compensation from the company, its directors, auditors or any expert, adviser or consultant for any wrongful act or for any incorrect or misleading statement made to the company. The Rules under the Companies Act provide that a class action may be initiated through an application to the Tribunal by at least 100 members of the company, or not less than 10 per cent of the total number of its members, whichever is lesser, or members holding 10 per cent of the issued share capital of the company. For companies that do not have a share capital, an application initiating a class action must be made by at least one-fifth of the total number of its members.

9 Shareholder responsibility

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

Generally, shareholders are not liable for the acts or omissions of a company. Shareholders' liability, in any event, only extends to their contribution towards the company's assets at the time of its winding up (without any limitation in cases of unlimited liability companies and to the extent of the amount unpaid on their shares or the amount guaranteed by them, in cases of limited liability companies).

Corporate control

10 Anti-takeover devices

Are anti-takeover devices permitted?

The Takeover Code provides for a compulsory offer of a minimum of 26 per cent of the paid-up capital by an acquirer.

Certain provisions of the Takeover Code make hostile acquisitions relatively difficult by favouring existing controlling shareholders and management. Particularly, the requirement to disclose shareholdings upon crossing certain thresholds allows the controlling shareholders to keep an eye on 'predators'. The Takeover Code also necessitates the target company's management to cooperate by requiring the letter of offer to include certain information of the target company, the authenticity of which is underwritten by the acquirer. Further, it also requires the target company's board to constitute a committee of independent directors to provide the shareholders their unbiased recommendations on whether the offer should be subscribed to and such recommendations are published at least two working days before the tendering period. Availability of the option to persons other than the acquirer to make competing offers also makes the takeover process difficult.

Indian takeovers are also subject to the CCI's scrutiny in cases where such a takeover can have an adverse effect on competition in a relevant Indian market.

Further, commercial contracts often have stringent 'change of control' clauses and may include the 'brand pill' provision, which prevents a hostile bidder from using the promoter's brand where the promoter loses control over the target.

11 Issuance of new shares

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

Companies need shareholders' approval through a special resolution (the number of votes cast in favour of the resolution by shareholders must be at least three times the number of votes cast against the resolution by shareholders) for the issuance of new shares and securities convertible into shares, except when such issuance is being effected through a rights issue, providing shareholders with a pre-emptive right to acquire newly issued shares in proportion to their existing contribution to the paid-up share capital of such company. Any offer to the public through prospectus by a listed company or a company intending to list its securities on any recognised stock exchanges in India must comply with the regulations issued by SEBI for such issuances.

12 Restrictions on the transfer of fully paid shares

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

Fully paid-up shares of public companies are freely transferable. Under the Companies Act, agreements between persons that restrict the transfer of such shares have been made enforceable as contracts. However, it is advisable to make the company a party to such an agreement restricting transferability to ensure that there is privity of contract, and the agreement is enforceable against the company.

It is mandatory for private companies to restrict transfer of their shares (including fully paid-up shares) by having specific provisions in their AoA and a private company may refuse to register a transfer of its shares pursuant to such a restriction. The affected transferee has the power to approach the Tribunal against the company's refusal to register such transfer.

13 Compulsory repurchase rules

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

Companies have to mandatorily redeem preference shares issued by them within a maximum period of 20 years from the issuance date. Such redemption is not a reduction in capital and companies are permitted to reissue the redeemed preference shares.

Equity shares have no such requirement; however, companies have the option to buy back equity shares under the voluntary route (up to 25 per cent of the aggregate paid-up capital and free reserves of the company by inviting shareholders to tender their shares) or via a reduction of capital approved by the Tribunal. Under the voluntary route, shareholders have an option not to tender their shares, unlike the Tribunal approved route, where once a reduction of capital is approved by the Tribunal and effected, it binds all the shareholders (including dissenting shareholders). Equity shares bought back or reduced in this way are necessarily extinguished, as Indian companies cannot hold their own shares.

Various authorities under the Companies Act are also entitled to direct a compulsory share repurchase, by a company or other shareholders, as a means of protecting minority interests, when there is oppression or mismanagement by majority shareholders. Further, the Companies Act allows an acquirer to squeeze out minority shareholdings, pursuant to a scheme approved by the shareholders holding nine-tenths of the value of the proposed transferable shares and, if not objected to by the Tribunal.

14 Dissenters' rights

Do shareholders have appraisal rights?

The Companies Act requires the promoters and shareholders in control of a company to give dissenting shareholders an opportunity to exit the company if it intends to utilise money raised from the public through the prospectus for any object other than the object stated in the prospectus; and vary the terms of any contracts referred to in the prospectus, at the exit price, and in the manner prescribed by SEBI.

SEBI amended the SEBI (Issue of Capital and Disclosure Requirements) (Second Amendment) Regulations 2016 on 17 February 2016 to include a chapter on 'Conditions and Manner of Providing Exit Opportunity to Dissenting Shareholders' (Exit Regulations). The Exit Regulations clearly specify that they are applicable only if:

- there are identifiable promoters or shareholders in control of the company;
- the public issue was opened after 1 April 2014;
- at least 10 per cent of the shareholders who voted in the general meeting disagree with the proposal for amendment of the objects or contract; and
- the amount to be utilised for the objects specified in the prospectus is less than 75 per cent of the total amount raised by the public issue.

The Exit Regulations prescribe a market-linked mechanism for the determination of the 'exit price' at which the dissenting shareholders will be provided an exit by the promoter or shareholders in control. The Takeover Code has been amended to ensure that the requirement of making a public offer is not triggered by an acquisition by promoters or shareholders in compliance with the requirements of the Exit Regulations.

Dissenting shareholders have ample exit opportunities in cases of takeover and delisting. In such cases, the acquirer or the promoters, as applicable, are required to provide an opportunity for the shareholders to tender their shares at a fair value. The Takeover Code provides for a compulsory offer of a minimum of 26 per cent of the paid-up capital. For the delisting of its shares from stock exchanges, it is mandatory for the promoters to offer to purchase shares of all the non-promoter shareholders who wish to tender their shares, and to acquire at least 90 per cent of total issued shares of that class.

The Tribunal may also order a company to make an exit offer to dissenting shareholders of a company proposing a compromise or arrangement with its members or creditors, if, in the opinion of the Tribunal, such an exit offer is necessary to effectively implement the terms of the compromise or arrangement. Further, in the case of a shareholders' right variation (by way of a resolution passed with a three-quarters majority of the particular class), the holders of at least 10 per cent of the shares of that class, being dissentient shareholders, can apply to the court for the cancellation of the variation.

The responsibilities of the board (supervisory)

15 Board structure

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

The predominant board structure for Indian-listed companies remains one-tier. The Companies Act and the Listing Regulations provide for the formation of an audit committee, a nomination and remuneration committee and a stakeholders' relationship committee. However, the recommendations of these committees are not binding on the board as they are only advisory in nature. For instance, the board is not bound by the recommendations of the audit committee as long as it discloses its non-acceptance of the recommendation along with the reason for such non-acceptance in the board report.

All related-party transactions proposed to be undertaken by a company require the approval of the audit committee. An omnibus approval may be granted by the audit committee for one financial year subject to the transactions meeting specified criteria such as the maximum value of the transactions in aggregate and individually, the extent and manner of disclosure required and periodic review of the transaction undertaken pursuant to such an omnibus approval.

16 Board's legal responsibilities

What are the board's primary legal responsibilities?

The board's primary responsibilities include managing the company's affairs and assets and ensuring the company's compliance with applicable laws. Apart from the powers specifically reserved for shareholders, the board is entitled to exercise all powers and to do all acts and things, as the company is authorised to do, subject to compliance with applicable laws, the provisions of the company's charter and the regulations, if any, made by the shareholders in a general meeting.

Besides, directors owe a fiduciary duty to the company and are expected to show the utmost care, diligence and skill in the exercise of their power and, where the company has violated any applicable laws, they are generally deemed to be 'officer who is in default'. They are also expected to execute their duties in a manner that does not conflict with their personal interests.

Regarding the shareholders, the primary responsibilities of the board include finalising the company's accounts and presenting them for shareholders' approval, recommending dividends and convening shareholders' meetings. The Companies Act and the Listing Regulations specifically provide that directors are generally liable to members of the company while carrying out the company's business and are expected to act in good faith and promote the object of the company for the benefit of its members as a whole.

The Companies Act prescribes a binding 'Code for Independent Directors' which provides the standard for professional conduct for independent directors.

17 Board obligees

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

The board represents the company and all actions taken by the board in good faith and intra vires bind the company. The board owes legal duties to the company and the directors are per se not agents or trustees of the shareholders. However, the board is expected to exercise its duties with the utmost care, diligence and skill while exercising its powers and any breach thereof may make it liable to the shareholders and to affected third parties, such as creditors, debenture holders, trustees or other persons dealing with the company.

18 Enforcement action against directors

Can an enforcement action against directors be brought by, or on behalf of, those to whom duties are owed?

Directors can be held personally liable for, among others, illegal acts, fraud, negligence, conspiracy, breach of trust and duties, false representation, wilful contribution to tortious action, misappropriation of the company's funds and assets, making improper payments including dividend payments and entering into contracts ultra vires. In such cases, the company or its shareholders (by means of derivative actions), along with the affected third parties, can sue the directors for such breaches, through class action (see question 8) or otherwise.

19 Care and prudence

Do the board's duties include a care or prudence element?

Directors owe a fiduciary duty to the company and are expected to show the utmost care, diligence and skill in the exercise of their power and decision-making. They are expected to execute their duties in a manner that does not conflict with their personal interests and are required to disclose to the board their direct and indirect interests in any business dealing concerning the company. If there is a conflicting personal interest, they are mandated to refrain from participating in such a decision-making process. The Code for Independent Directors requires independent directors to inter alia satisfy themselves on the integrity of the financial information of the company, and the robustness of its financial controls and systems of risk management, safeguard the interests of all stakeholders, particularly the minority shareholders, and seek clarification or amplification of the information provided to the board, and where necessary, obtain and follow professional advice and the opinion of external experts at the expense of the company.

Judicial pronouncements suggest that the directors must use their skill reasonably and in sync with their knowledge and experience. They are expected to adopt the standard of care that an ordinary person might be expected to take in the circumstances and therefore they cannot be held responsible for mere judgement errors if they have acted in good faith.

20 Board member duties

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

Directors can be executive or non-executive.

Executive directors, such as managing and full-time directors, perform day-to-day management duties for the company in addition to being board members.

A managing director is entrusted with substantial management powers under the company's AoA, other agreements, or resolutions passed by the shareholders or the board. Full-time directors in the employment of the company are responsible for discharging duties as per their terms of employment and are usually assigned duties related to finance, human resources and legal compliance.

Non-executive directors are directors simpliciter who participate in the board decision-making process and discharge other duties that may be entrusted upon them by the board or the shareholders.

Independent directors take part in the decision-making process at the board, audit and remuneration committee meetings (where their presence is mandatory). They bring about 'independence' to the decision-making process and generally ensure the company's compliance with the corporate governance norms, as well as acting as a whistle-blower in the shareholders' interest and in the larger public interest.

Owing to the varied roles of the directors, the Companies Act follows the concept of 'officer who is in default' as persons responsible for the breach of the Companies Act's provisions. The managing director, whole-time director and key managerial personnel (a role akin to that of managing director, but who need not necessarily be a board member) are the persons primarily responsible as 'officer who is in default' and in their absence and in the absence of any other director who has been entrusted with that specific duty, all of the company's directors become liable.

The Companies Act mandates that a majority of the directors comprising the audit committee must be persons having the ability to read and understand financial statements, and as stated in question 25, the Listing Regulations further require listed companies to ensure that all members of its audit committee are able to read and understand financial statements; and at least one member has accounting or related financial management expertise.

21 Delegation of board responsibilities

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

Among others, decisions that cannot be delegated include:
- making calls to shareholders with regard to unpaid share monies;
- approving the buyback of securities;
- issuance of securities, including debentures;
- approving financial statements and the board's report;
- diversification of the business of the company;
- amalgamation, merger or reconstruction of the company;
- takeover or acquisition of a controlling or substantial stake in another company;
- filling in casual vacancies of directors;
- making political contributions;
- appointment or removal of key managerial personnel;
- appointment of internal and secretarial auditors;
- sanctioning contracts in which directors are interested;
- receiving notice of directors' interests or shareholdings;
- appointment of a managing director who is already a managing director in another company;
- making loans and investments in certain cases;
- approving a declaration of solvency in a voluntary winding up; and
- approving the advertising text for attracting deposits.

The board, as it is under a fiduciary duty, cannot delegate functions that require judgement or discretion on its part. Further items reserved under the company's AoA or by the shareholders in a general meeting for the board cannot be delegated.

Apart from the above decisions, the board has the authority to delegate its powers by means of a board resolution to a committee or the company's executive or non-executive directors, employees, etc.

Further, the powers of a company's managing director, who is entrusted with substantial management powers (including the power exercisable by the board, which the shareholders intend to delegate to the managing director), are often prescribed in the company's AoA.

22 Non-executive and independent directors

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

'Non-executive directors' are not per se defined in the Companies Act or otherwise. The term is commonly used to refer to directors who are directors simpliciter and do not hold any managerial positions, apart from being a board member.

The Companies Act requires listed companies and public companies with paid-up share capital exceeding 100 million rupees or turnover exceeding 1 billion rupees or loans, debentures and deposits exceeding 500 million rupees to have at least one-third of their board made up of 'independent directors'.

The Listing Regulations makes it mandatory for listed companies to have at least half of their board made up of 'independent directors' if the board chairman is an executive director, or a non-executive director who is a promoter or is related to the promoters or holds a managerial position at board level or a level below that. In other cases, where the board chairman is a non-executive director not falling into the category discussed above, listed companies are required to have at least one-third of their board made up of independent directors. The Listing Regulations further provide that independent directors must be provided suitable training to familiarise them, inter alia, with the company, the nature of the industry in which the company operates, their role, rights and responsibilities in the company and the business model of the company; the details of such training imparted are to be disclosed by the company in its annual report.

The Companies Act defines 'independent director' as a non-executive director who, among other factors:
- apart from receiving director's remuneration, does not have any material pecuniary relationships or transactions with the company, its promoters, its directors, its senior management or its holding company, its subsidiaries and associates during the two immediately preceding financial years, which may affect the independence of the director;
- is not related to promoters or directors of the company or its holding subsidiary or associate company;
- has not been an executive of the company in the immediately preceding three financial years;
- is not a partner or executive or was not a partner or executive, during the preceding three years, of:
  - the statutory audit firm or the internal audit firm that is associated with the company; or
  - legal firms and consulting firms that have a material association with the company; and
- is not a substantial shareholder of the company, owning 2 per cent or more of the voting shares along with his or her relatives.

Unlike executive directors, independent directors are not responsible for day-to-day company management. They actively participate in the board, audit and remuneration committee decision-making process (where their presence is mandatory). They instil external and wider perspective, bring independence to the decision-making process and generally ensure compliance by the company with corporate governance norms. Independent directors are also expected to act as whistleblowers and act in the shareholders' and the public interest for the implementation of corporate governance norms. Independent directors of a company are required to hold and attend at least one meeting in a year without the attendance of non-independent directors and members of the management to review the performance of non-independent directors and the board as a whole and the chairperson, and assess the quality, quantity and timeliness of flow of information between the company's management and the board.

The Companies Act provides stringent qualifications for an independent director and provides for detailed guidelines for appointment, roles and responsibilities of independent directors with a view to ensure that they work in an objective manner in the Code for Independent Directors. While there is no minimum age requirement for independent directors under the Companies Act, in view of the nature of their responsibilities, it is essential that a person sought to be appointed as an independent director must have legal competence and therefore must not be less than 18 years of age.

23 Board size and composition

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

Board composition

Public and private companies are required to have a minimum of three and two directors, respectively, and a maximum of 15 directors. The Companies Act has also introduced the concept of a 'one person company', which is required to appoint only one director. A company's AoA may specify a higher minimum number of directors on the board, and a company can appoint more than 15 directors by passing a special resolution.

Listed companies and public companies with paid-up share capital of 1 billion rupees or turnover exceeding 3 billion rupees are required to appoint at least one female director. Further, listed companies have to ensure that at least one-third of their board comprises independent directors, and public companies with paid-up share capital exceeding 100 million rupees, or turnover exceeding 1 billion rupees or aggregate outstanding loans, debentures and deposits exceeding 500 million rupees are required to have at least two independent directors on their board.

Further, a person cannot be appointed as director in more than 20 companies at a time, out of which not more than 10 can be public companies. As regards listed companies, a director cannot be a member of more than 10 committees or a chairman of more than five committees across all companies in which he or she is a director.

The Listing Regulations requires the board of a listed company to have an optimum combination of executive and non-executive directors with at least one female director and not less than 50 per cent of the board comprised of non-executive directors. Further, if it has a non-executive chairman, one-third of its directors are required to be independent directors; this is 50 per cent if it has an executive chairman.

Banking companies are subject to additional requirements as prescribed under the Banking Regulation Act 1949 (the BR Act) and the guidelines issued by the Reserve Bank of India (RBI) for directors' qualifications and composition of board.

The AoA of a company may confer on the board the power to appoint any person, other than a person who fails to get appointed as a director in a general meeting, as an additional director. Further, the board if authorised by the AoA of the company or a shareholders' resolution, may appoint a person as an alternate director for a director of the company, in his or her absence from India for a minimum period of three months, provided such person is not already an alternate director for another director of the company. The board of public companies are empowered to fill any casual vacancy on the board that may arise upon the office of a director getting vacated during his or her term in the normal course, subject to regulations in the AoA.

Directors' qualification

The Companies Act only permits natural persons to be directors, and every company is required to have at least one director who has stayed in India for at least 182 days in the previous calendar year. The Companies Act prohibits the following from being appointed as directors:

- any person of unsound mind;
- an undischarged insolvent;
- any person who has applied to be registered as an insolvent, or has been convicted by a court of an offence involving 'moral turpitude' and has been sentenced to imprisonment for at least six months in respect thereof;
- any person who has failed to pay calls on his or her shares for more than six months, or is subject to a court order disqualifying him or her, or is already a director in a public company that has failed to comply with certain filing requirements or has failed to repay a deposit, debentures or the payment of dividends and such failure has not been remedied within one year of being appointed as a director; or
- any person who has been convicted for an offence dealing with a related-party transaction under the Companies Act in the preceding five years.

Private companies, through their AoA, may provide for more director disqualification grounds. Further, there are additional qualifications applicable to 'independent directors' (see question 22), managers, managing and full-time directors, in relation to, inter alia, age and criminal record.

Board composition disclosure

Every company is required to keep a register of its directors and key managerial personnel at its registered office, and it must report any changes in directorship to the RoC within 30 days. Information on composition of the board also forms a part of the company's annual return that is filed with the RoC. Every director is required to make disclosures of his or her directorship in all companies or any changes therein to companies in which he or she is a director. Also, a listed company must disclose its board composition in its corporate governance report as part of its annual report under the Listing Regulations.

24 Board leadership

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

The Companies Act prohibits the appointment of the same person as the chairperson of the company as well as the managing director or CEO of the company, unless the AoA provides otherwise or the company does not carry on multiple businesses. The Listing Regulations provide that a listed company may appoint separate persons to the post of chairperson and managing director or CEO; however, this is specified as a discretionary requirement, and listed companies may decide their own policy in this regard, subject to compliance with the Companies Act.

In the Indian context, a managing director, who is a person entrusted with substantial management powers of a company, is equivalent to the CEO. The CEO or manager (and managing director) are recognised as 'key managerial personnel' by the Companies Act, who need not necessarily be directors of the company. While the board chairman is primarily responsible for regulating the conduct of the board meetings, the managing director is responsible for managing the day-to-day affairs of the company and exercising powers as may be entrusted to him or her by the board, shareholders or under the AoA.

The Listing Regulations require certification by the CEO (or the chief financial officer of the company) on certain operational matters and on adherence to the code of conduct adopted by the company for its board members and senior management.

Generally, closely held Indian companies have a 'chairman and managing director' who acts both as a CEO and board chairman. For best practices, reference may be made to the Kumar Mangalam Birla Committee Report (1999), which recommended that the chairman's role, being, in principle, different from that of the CEO, should necessitate companies to appoint a non-executive director over an executive director as chairman.

25 Board committees

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

Under the Companies Act, listed companies and public companies with paid-up capital exceeding 100 million rupees, or turnover exceeding 1 billion rupees, or aggregate outstanding loans or borrowings or debentures or deposits exceeding 500 million rupees have to constitute an audit committee and a nomination and remuneration committee. Further, any company which consists of more than 1,000 security holders is required to constitute a stakeholders' relationship committee to consider and resolve the grievances of security holders of the company. Additionally, every company with net worth exceeding 5 billion rupees or turnover exceeding 10 billion rupees or net profit exceeding 50 million rupees is required to constitute a corporate social responsibility committee. In addition, the board may constitute directors' committees or other expert committees to assist them and to discharge their functions. As per the Companies Act, the audit committee has to consist of at least three directors with independent directors forming a majority, and a majority of its members must have the ability to read and understand financial statements.

The Listing Regulations require every listed company to constitute an audit committee with a minimum of three directors, of which two-thirds and the chairman should be independent directors; all members should be able to read and understand financial statements; and at least one member should have accounting or related financial management expertise. The prior approval of the audit committee is necessary in case of related-party transactions.

Further, the Listing Regulations require listed companies to constitute a nomination and remuneration committee with at least three non-executive directors and at least 50 per cent of the directors should be independent. The nomination and remuneration committee is to be chaired by an independent director. Listed companies are also required to constitute a 'stakeholders relation committee' whose chairperson must be a non-executive director. The top 100 listed companies, determined on the basis of market capitalisation, also have to constitute a 'risk management committee', consisting of a director as the chairperson, and senior executives of the company as members.

26 Board meetings

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

A company must have at least four board meetings in a year, such that not more than 120 days intervene between two consecutive board meetings. The Listing Regulations impose a similar condition of there not being a gap of more than 120 days between two board meetings.

27 Board practices

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

As per the Listing Regulations, listed companies are required to submit quarterly and annual compliance reports to the stock exchanges containing specified information regarding the board, including the composition of the board and board committees, remuneration of directors and related-party transactions approved by the board, among other things. Furthermore, listed companies are required to have a separate section in the annual report of the company containing a detailed compliance report on corporate governance aspects.

As per the Companies Act, all companies are also required to provide details with regard to the board and committees in the board report (which is mandatory under the Companies Act and is to be presented by the board at the annual general meeting). The Companies Act additionally requires companies to submit in general meetings a directors' responsibility statement and a declaration by the independent directors verifying their independence based on the prescribed criteria. Companies that are required to constitute a nomination and remuneration committee have to also submit the company's policy on directors' appointment and remuneration including criteria for determining qualification and independence of directors.

28 Remuneration of directors

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

Remuneration

Private companies have full flexibility as regards determining directors' remuneration and the process to be followed in this regard.

Public companies are required to determine remuneration payable to directors though their AoA or a shareholders' resolution passed in a general meeting. As per the Companies Act, the total remuneration payable by a public company to its directors, including the managing director and full-time director in a financial year cannot exceed 11 per cent of the net profits of the company in that financial year. Further, the remuneration payable to any one managing director, full-time director or manager cannot exceed 5 per cent of the net profits of the company in that financial year without obtaining the approval of the shareholders of the company in respect of such remuneration in a general meeting. Non-executive directors' remuneration is subject to an overall cap of 1 per cent of net profit, if the company has a managing director, full-time director or manager; and 3 per cent of the net profit in other cases. As per the Companies Act, a loss-making public company can only pay fixed remuneration to a managerial person and any payment exceeding such limits requires the approval of central government. No such prior approval is required to determine the remuneration that may be paid to a managerial person who is functioning in a professional capacity and possesses at least graduate level qualification with expertise and specialised knowledge in the field in which the company operates; provided such person does not hold any shares or interest in the company, its holding and subsidiary companies and is not related to any director of such company, its holding or subsidiary companies including for a minimum period of two years preceding his or her appointment.

Listed companies are required to disclose in their board's report the ratio of the remuneration of each director to the median employee's remuneration and as per the Listing Regulations, all fees or compensation of the non-executive directors, including independent directors, shall be fixed by the board and require shareholders' approval (except for sitting fees), and remuneration details of all directors are required to be disclosed in the annual report of such listed entity.

Length of director's service contract or appointment

As per the Companies Act, two-thirds of a public company's directors are liable to vacate their position by rotation within a maximum period of three years from their appointment date. Managing directors, full-time directors or managers can be appointed for a maximum period of five years at a time and in certain events the remuneration payable to managing or full-time directors or managers can be determined by the shareholders for a period of three years at a time.

Loans

As per the Companies Act, a public company is prohibited from advancing any loan to directors or providing guarantees or any other security in relation to a loan taken by its directors or any person in whom the directors may be interested, either directly or indirectly, except as a part of the conditions of service extended by the company to all its employees, or pursuant to a scheme approved by the members of the company by a special resolution. Finance companies may extend loans to their directors provided the interest charged by them is not below the RBI-prescribed threshold.

Additionally a company requires board approval, and in certain situations even shareholders' approval, through a special resolution when it is entering into any contract or arrangement with a director of the company, since a director is a 'related party' to the company under the Companies Act.

Banking companies are subject to further requirements in relation to the aforementioned, as have been prescribed under the BR Act and the guidelines issued by the RBI. The grant of loan by a banking company to its directors is restricted and the determination of terms of directors' appointment and payment of remuneration to directors is subject to the approval of the RBI. The RBI has clarified that the approval process will involve an assessment of whether the compensation policies and practices followed by the concerned banking company are in accordance with the principles and implementation standards on sound compensation practices issued by the Financial Stability Board, an international body based in Basel, Switzerland monitoring the global financial system.

29 Remuneration of senior management

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

The Companies Act and the Listing Regulations define 'senior management' as officers of the listed company who are members of the core management team of a company (excluding the board) and are one level below the executive directors, including all functional heads.

Chief executive officers, chief financial officers, and company secretaries (who are employees and need not necessarily be directors), form the senior management. These appointments are also included within the definition of 'key managerial personnel' in the Companies Act. While the Act regulates the remuneration payable by public companies to its directors and manager, it does not similarly restrict remuneration payable to other 'key managerial personnel'. The nomination and remuneration committee of a company is required to formulate and recommend to the board a policy regarding remuneration of directors, key managerial personnel and other employees and ensure that remuneration to key managerial personnel and senior management involves a balance between fixed and incentive which reflects the short and long-term performance objectives appropriate to the working of the company and its goals. In terms of the Code for Independent Directors, independent directors should weigh in on appropriate levels of remuneration for key managerial personnel and senior management.

Unlike directors, the appointment and remuneration of senior management is governed by the terms of their appointment and employment. There are no formal guidelines on matters pertaining to the advancement of loans to senior managers or other transactions between the company and senior managers. Therefore, companies are free to determine their policies in this regard. The terms of appointment and payment of remuneration to its senior officials by banking companies, however, remain subject to the approval of the RBI, as detailed in question 28.

30 D&O liability insurance

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

The Companies Act permits a company to obtain insurance on behalf of its key managerial personnel to indemnify them against any liability in respect of any negligence, default, misfeasance, breach of duty or breach of trust. The company can pay the premium and it would not be considered as a part of the remuneration of the director or officer, however, in the event that the director or officer is found guilty, the premium paid on any such insurance is to be treated as a part of their remuneration under the Companies Act.

31 Indemnification of directors and officers

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

As discussed in question 30, Indian companies can indemnify directors for liabilities related to negligence, default, misfeasance, breach of duty or breach of trust as regards the company. Further, as provided under the model AoA to the Companies Act, the company is required to, at its own cost, indemnify every officer of the company against any liability incurred by him or her in defending any proceeding (civil or criminal) in which judgment is given in his or her favour or in which he or she is acquitted or discharged.

These liabilities are different from those incurred by directors in the ordinary course of managing the company's affairs, in good faith and within their authority. While dealing on behalf of a company in good faith, directors have been treated as the company's agents and have accordingly been provided with safeguards as available to agents generally under the Indian Contract Act 1872, including a right to seek indemnity from the principal (the company).

Companies ordinarily insert specific provisions in the AoA providing for directors' indemnities, to the extent not prohibited under the Companies Act.

32 Exculpation of directors and officers

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

The Companies Act does not permit the preclusion or limitation of directors' liability. However, as discussed in questions 30 and 31, directors can be suitably insured and indemnified by companies against liabilities, to the extent not prohibited under the Companies Act.

33 Employees

What role do employees play in corporate governance?

The Companies Act requires listed companies, companies which accept public deposits and companies which have borrowings exceeding 500 million rupees from banks and public financial institutions to establish a 'vigil mechanism' for directors and employees to report genuine concerns from a corporate governance perspective. The vigil mechanism is required to provide adequate safeguards against victimisation of persons who report concerns, and where necessary must provide direct access to the chairperson of the audit committee.

The Listing Regulations incorporate the whistle-blower concept and provide that a listed company should have a vigil mechanism for directors and employees to report to the management concerns about unethical behaviour, actual or suspected fraud or violation of the company's code of conduct. The vigil mechanism should provide for adequate safeguards against victimisation of any person who acts as a whistle-blower, including direct access to the chairman of the audit committee, in appropriate and exceptional matters.

Sometimes, individuals go out of the organisational hierarchy and make information available to the public or other external authorities, in order to effectively carry out the whistle-blowing function.

34 Board and director evaluations

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

The Companies Act requires listed companies, and public companies with paid-up share capital exceeding 250 million rupees, to disclose the manner in which formal annual evaluation has been undertaken by the board of its own performance and the performance of the committees constituted by the board and individual directors in the board's report. The nomination and remuneration committee of each such company and the independent directors have been made responsible for carrying out the evaluation of each director's performance, however the Companies Act does not provide for the mode, manner and process to be followed for such evaluation. Directors on the board of government companies are exempt from the evaluation requirement, provided that they are required to be evaluated by the ministry or governmental department that is administratively in charge of such a company as per its own methodology.

The Listing Regulations additionally require the board of directors of listed companies to undertake an evaluation of the performance of the independent directors on the board. The entire board is required to participate in the evaluation of each independent director, except for the individual independent director being evaluated. The nomination and remuneration committee of listed companies has been tasked with formulating the criteria for evaluation of performance of independent directors, as well as the board as a whole, which evaluation criteria is to be disclosed by the company in its annual report. The board of listed companies is required to monitor and review the evaluation framework for the board of directors.

The ICSI published a 'Guide to Board Evaluation' in April 2015 (before the Listing Regulations came into effect) to provide guidance to companies on how to evaluate the performance of its board with suggested parameters and sample models for evaluation. ICSI recommends that the evaluation process should include an analysis of the time spent by the board in considering matters, and whether the terms of reference of various committees set up by the board have been met, in addition to verifying compliance with the Companies Act, and also recommends involving an external expert for such evaluation, to add a level of independence to the exercise.

Disclosure and transparency

35 Corporate charter and by-laws

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

The company is required to file its charter documents and any amendments thereto with the RoC, and they can be inspected and copies obtained online by any person registered with the MCA portal at http://mca.gov.in/mcafoportal/viewPublicDocumentsFilter.do upon payment of a nominal fee of 100 rupees.

36 Company information

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

Companies must make periodic filings of the company's audited accounts, the board's report, auditor's report and annual return with the RoC.

Additionally, inter alia, when the company passes certain resolutions, there are changes in directorships, the creation or satisfaction of charges on the assets, changes in authorised or paid-up share capital or changes in the registered office address, the company must file such information with the RoC.

Further, companies are also required to file with the RoC, inter alia, certain notices or advertisements issued by the company, the orders

Update and trends

The MCA, on 1 June 2016 constituted the Tribunal and its appellate authority, the National Company Law Appellate Tribunal (NCLAT). Pursuant to the constitution of the Tribunal and NCLAT, the CLB has been dissolved and the jurisdiction of the CLB has been subsumed by the Tribunal, with all pending matters before the CLB being transferred to the Tribunal, including matters pertaining to oppression and management. The Tribunal has also replaced and subsumed the jurisdiction of the Board for Industrial and Financial Reconstruction (BIFR), the Appellate Authority for Industrial and Financial Reconstruction (AAIFR), and the jurisdiction of the High Courts for company matters pertaining to mergers, compromises and other corporate restructurings and will resolve insolvency cases of companies and limited liability partnerships. This has led to consolidation of corporate jurisdiction in India, and is expected to have significant advantages, including avoiding multiplicity of proceedings in various fora, and reducing the time taken for adjudication because of the focused jurisdiction and specialised knowledge of the adjudicators; the Tribunal and the NCLAT are mandatorily required to have a prescribed proportion of 'technical members' who have expertise and experience inter alia as chartered accountants, company secretaries or cost accountants for a minimum period of 15 years, or otherwise have proven ability and experience of not less than 15 years in law, industrial finance, labour matters or other disciplines related to management of companies. The Tribunal has its principal bench in New Delhi, and 10 benches in Ahmedabad, Allahabad, Bengaluru, Chandigarh, Chennai, Guwahati, Hyderabad, Kolkata, Mumbai and New Delhi, having prescribed territorial jurisdiction. The principal bench has jurisdiction over all matters involving a company whose paid-up share capital is in excess of 50 million rupees. All matters pertaining to 'class actions', application of the Companies Act to foreign companies and annual reports of government companies are within the exclusive jurisdiction of the principal bench, notwithstanding the location of the registered office of the company in question, or its share capital.

The Insolvency and Bankruptcy Code 2016 (the Code) has been reviewed by the Ministry of Law and Justice with a view to consolidating and amending the laws relating to reorganisation and insolvency resolution of inter alia corporate persons in a time-bound manner, while maximising the value of assets of such persons. The Code is applicable to all companies registered under the Companies Act and the erstwhile Companies Act, 1956, and the adjudicating authority for any proceeding for their insolvency, liquidation, or voluntary liquidation is the Tribunal. In terms of the Code, the corporate insolvency resolution process in regard to any company is to be completed within a period of 180 days from the date on which the application to initiate such process is admitted by the Tribunal.

On 1 June 2016 MCA amended the provisions in the Companies Act empowering shareholders to collectively initiate a 'class action' against a company before the Tribunal if they believe that the management or conduct of the affairs of the company are being conducted in a manner prejudicial to the interests of the company, its members or its depositors (also see question 8).

On 9 September 2016 the MCA updated the Companies (Mediation and Conciliation) Rules, 2016 pursuant to which, any party to a proceedings before the Tribunal, the NCLAT or the central government may request for the matter underlying such proceeding to be referred to mediation or conciliation by an expert empanelled with the central government. The Tribunal, the NCLAT or the central government also the have the power to suo moto refer matters to mediation or conciliation by an empanelled expert. Any mediation or conciliation of such proceedings is required to be completed within three months of the reference, and the expert is required to forward its recommendations to the Tribunal, the NCLAT or the central government, as applicable. If the parties to the proceeding are able to reach an agreement or settlement, such agreement is to be reduced in writing to submitted to the Tribunal, the NCLAT or the central government, as applicable, for taking it on record.

The Listing Regulations have been amended to require the top 500 listed companies, based on market capitalisation, to formulate and disclose their dividend distribution policies in their annual reports and on their websites, which should include the circumstances in which the shareholders can or cannot expect dividend, the financial parameters and the internal and external factors to be considered, utilisation of retained earnings and parameters for various classes of shares.

The central government has been empowered to establish or designate 'special courts' for the express purpose of providing expedited trial of offences punishable under the Companies Act with imprisonment of two years or more. Special courts have been set up in various states and union territories of India, including Delhi, Chandigarh, Haryana and Rajasthan.

of the Tribunal, charter documents and amendments thereto. Indian RoC filings are electronically effected through the MCA portal at http://mca.gov.in/mcafoportal/showEformUpload.do and can be inspected by any person registered with the portal upon the payment of a nominal fee of 100 rupees. Certified copies of filings can also be obtained.

The Companies Act also requires companies to make disclosures to its shareholders, by incorporating information into the general meeting notices, the board's report and auditors' report. For certain corporate actions, the stakeholders' and other authorities' disclosure is required to be made by way of notices and advertisements.

Listed companies are subject to additional disclosure requirements under the Listing Regulations, the Takeover Code and Insider Trading Code, for better implementation of corporate governance initiatives.

Hot topics

37 Say-on-pay

Do shareholders have an advisory or other vote regarding executive remuneration? How frequently may they vote?

See questions 28 and 29. For public companies, the remuneration payable to managing or full-time directors or managers can be determined by the shareholders for a period of three years at a time.

38 Shareholder-nominated directors

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

Under the Companies Act each shareholder can nominate him or herself or another person as a director appointee for consideration of the shareholders at a general meeting by providing the company with at least 14 days' notice and depositing a fee of 100,000 rupees with the company. The rules framed under the Companies Act provide that the company shall inform its shareholders of every nomination notice at least seven days before the general meeting, either individually through email or written notice to the shareholders, along with a notification on the website of the company, or through newspaper advertisements of such nominations, at the company's expense. Upon a resolution passed by simple majority (unless otherwise provided in the AoA) in the general meeting, the nominee stands elected as a director. The company is required to refund the deposit to the nominating shareholder if the proposed person gets elected as a director, or gets more than 25 per cent of the total votes validly cast on the resolution at the general meeting.

Commonly, significant investors or joint venture partners have the right to nominate board members via 'pooling arrangements' and other provisions inserted to that effect into the AoA.

39 Shareholder engagement

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

Companies typically engage with their shareholders at their annual general meeting. The introduction of electronic voting and postal ballot facilities for a large number of matters requiring shareholder approval have enabled greater participation of small shareholders in decision making, including by eliminating the considerable time and cost expended by shareholders to attend general meetings.

The directors of a company are expected to attend all general meetings of a company, and if any director is unable to attend a general meeting, the chairman of the meeting is required to explain the reason for such absence at the meeting. Specifically, the chairman of the nomination and remuneration committee, audit committee and the stakeholders committee, if constituted by a company, are required to attend general meetings of the company, and in their absence, another member of the above committees duly authorised by the relevant chairman, must attend the general meeting. This standard has been introduced by the Companies Act and ICSI to ensure that at least one member of each of these committees is present at every general meeting to address shareholders' queries, if any, concerning their respective committees.

On 7 November 2016 the India-UK Financial Partnership, which was formed in July 2014 to provide policy inputs to both governments in the financial sector, presented a paper titled 'Responsible Shareholder Engagement – An Indian Stewardship Code' to Mr Arun Jaitley, the Finance Minister of India. The report states that good corporate governance and effective investor stewardship are essential for corporate success and that institutional investors, in particular, have a fiduciary duty to actively and appropriately represent the interests of their investors, who are typically small investors, to the companies in which they hold investments. Specifically in regard to listed companies, the paper recommends the development of an 'Indian Stewardship Code' to be adopted by public and private mutual funds, insurance companies and foreign investors which will introduce a 'voting plus' and 'comply or explain' framework to create responsible shareholder engagement in India and a constructive and mutually beneficial two-way dialogue between shareholders and the boards of listed Indian companies.

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Sources of corporate governance rules and practices

1 Primary sources of law, regulation and practice

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

Public companies in Israel are governed by the Companies Law 1999 (the Companies Law), the Securities Law 1968 (the Securities Law) and the rules and regulations promulgated thereunder. Public companies that are traded on the Tel Aviv Stock Exchange (TASE) are also subject to the regulations of the TASE. Additional, more specific rules and regulations (which are not discussed in the following answers) may apply to companies in certain industries, such as financial institutions (pension funds, mutual funds, insurance companies and provident funds), banking corporations and government companies. All of the above-mentioned laws, rules and regulations are binding; the 'comply or explain' approach is not customary in Israel.

2 Responsible entities

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

The primary government agency responsible for enacting and enforcing rules of corporate governance in Israel is the Israeli Securities Authority (ISA). Public companies that are traded on the TASE are also subject to the supervision of the TASE. There are a few advisory firms in Israel who provide guidance to institutional investors in respect of voting on corporate governance-related matters, the leading one being Entropy Risk Management Solutions Ltd. In February 2014 the ISA published a new arrangement for the activity of advisory firms, within whose framework there has been defined the extent of verification that is required from the advisory firms and the manner in which institutional bodies can transact with them. This arrangement is intended to deal with developments that have arisen in the capital market over the past few years and furthers institutional activism in Israel.

The rights and equitable treatment of shareholders

3 Shareholder powers

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

Pursuant to the Companies Law, and unless provided otherwise in the articles of association, shareholders have the power to appoint and remove directors by a resolution that must be adopted by an ordinary majority. With respect to the removal or appointment of external directors in a public company, the Companies Law sets out a special voting mechanism for doing so. Shareholders may influence the course of action taken by the board of directors (the board) in two principal ways: the general meeting may use its authority to amend the articles of association, including by assuming powers conferred on the board, and shareholders holding over a certain amount of issued share capital and voting rights may require the board to convene a general meeting on any matters that are appropriate to be brought before the shareholders for the decision of the general meeting.

4 Shareholder decisions

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

Pursuant to the Companies Law, the following decisions are reserved to the shareholders' general meeting:

- alterations in the articles of association;
- exercise of the powers of the board in the event of its incapacitation;
- appointment of the auditor and termination of its employment;
- appointment of external directors;
- confirmation of certain acts and transactions involving conflicts of interest, interested parties or controlling shareholders;
- confirmation of the compensation policy of the company;
- changes in the registered share capital of the company; and
- mergers (subject to certain exceptions).

In a recent amendment to the Companies Law, a unique mechanism was established for approving the compensation policy of the company and the terms of service of office holders (who are neither directors nor controlling shareholders of the company), pursuant to which, in the event of specific circumstances as prescribed in the Companies Law, the board may adopt a decision on the aforesaid issues that stands contrary to the position of the general meeting (see question 37).

5 Disproportionate voting rights

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

There are generally no limits under law with respect to the exercise of voting rights by shareholders. The Securities Law provides that the TASE may not permit the registration for trade of shares or convertible securities unless the company's share capital consists of only one class of securities granting equal voting rights in proportion to their par value. It should be noted that companies that first issued shares before the adoption of this rule in 1990 are allowed to maintain disproportionate voting rights, provided that in any new issuance they only issue shares bearing the best voting rights from among the existing classes of shares. As a result of this rule, the vast majority of listed companies in Israel follow the one share, one vote principle. It should be noted that a public company may issue shares with dividend preference and no voting rights.

6 Shareholders' meetings and voting

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

Pursuant to the Companies Law, resolutions in the general meeting of shareholders of a public company cannot be adopted without an actual meeting. Each shareholder generally has the right to participate in general meetings and to vote therein. Shareholders can participate and vote in the meeting in four primary ways: in person, via electronic voting platforms, by proxy and, in certain decisions, by written ballot. A shareholder has the right to receive confirmation of share ownership from the stock exchange member through which his or her share is held. Proxies and written ballots need to be delivered to the company in advance of the meeting and follow certain formal requirements. Generally, shareholders are not obliged to participate or vote in general meetings. However, managers of mutual funds that hold shares issued by a public company (excluding foreign securities) are required to participate and vote (that is, not abstain) at a general meeting of the company, if in their opinion a proposed resolution submitted for the approval of the general meeting may potentially harm the interest of the holders of the units of the mutual fund. The fund manager must provide a detailed report to the ISA and the TASE regarding their vote at the general meeting. While private companies are allowed to hold a general meeting using any means of communication, provided that all shareholders participating can hear each other simultaneously, public companies are not allowed to hold virtual meetings.

7 Shareholders and the board

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

The right to demand a general meeting is granted to shareholders who hold at least 5 per cent of the share capital and 1 per cent of the voting rights, or 5 per cent of the voting rights. One or more shareholders who hold at least 1 per cent of the voting rights may ask the board to include any appropriate subject, including director nominations, on the agenda of a future general meeting.

Where a general meeting has been convened, any shareholder may request the company to send a statement of position on behalf of the shareholder to the other shareholders in the company on matters that are subject to voting by written ballot.

8 Controlling shareholders' duties

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

According to the Companies Law, the shareholders have the following duties towards the company and towards the other shareholders: a shareholder will, in exercising his or her rights and in carrying out his or her duties to the company and to the other shareholders, act in good faith and in a customary manner, and will refrain from exploiting his or her power within the company, specifically when voting on certain key issues; and a shareholder will refrain from discriminating against other shareholders.

The following have a duty to act fairly towards the company: controlling shareholders; a shareholder who knows that its vote will be determinative with respect to a resolution at a company general meeting or a class general meeting; and a shareholder who, according to the articles of association, has the power to appoint or prevent the appointment of a company officer.

A breach of any of the duties listed above shall be treated as a breach of contract by the above-mentioned shareholders, mutatis mutandis. In addition, in the case of discrimination against shareholders, the court may issue directives it sees fit to remove or prevent such discrimination.

9 Shareholder responsibility

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

Lifting the corporate veil

The Companies Law provides that the court is entitled to assess corporate debt to a shareholder of the company, if it finds that the circumstances warrant this, in extraordinary cases in which the separate legal entity doctrine was employed in a manner designed to defraud or discriminate against a creditor, or in a manner deemed detrimental to the company's objectives in which an unreasonable risk was taken that affected the ability of the company to service its debts.

A controlling shareholder shall be liable towards other security holders for any damage caused by virtue of the company's violation of the provisions of the Securities Law or the regulations enacted thereunder, subject to certain defences included in the Securities Law.

A controlling shareholder shall be further liable to anyone who purchased securities in an issuance under a prospectus, and to anyone who sold or acquired securities in the course of trading on a stock exchange or over the counter, for damage caused to them by the inclusion of a misleading item in the prospectus, subject to certain defences included in the Securities Law.

Corporate control

10 Anti-takeover devices

Are anti-takeover devices permitted?

Anti-takeover devices are generally permitted in Israel, subject to the board and shareholders' duties under the Companies Law (see questions 8 and 16). However, such devices, including 'poison pills', are less common because most companies are held by controlling shareholders, and therefore hostile takeovers are rare. The use of classified boards is more frequently practised in Israel; the leading proxy advisory firm in Israel was against such practice in its recently published guidelines.

11 Issuance of new shares

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

A company's registered share capital is set out in the company's articles of association. Only the general meeting has the power to increase or reduce registered share capital, subject to the provisions of the law. The company may not stipulate alternative provisions regarding this matter. The board has the power to issue shares and convertible securities up to the limit of the registered share capital of the company. Pre-emptive rights are permitted pursuant to the Companies Law, but are uncommon in public companies, however, the company may decide to publish rights offering to its shareholders.

12 Restrictions on the transfer of fully paid shares

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

The Companies Law establishes a presumption that shares are transferable, but allows companies to include, in their articles of association, provisions that limit the transfer of shares pursuant to conditions prescribed in such articles. However, the TASE regulations provide that one of the conditions for registering shares or other securities for trade is that the company's articles of association do not limit the transfer of the shares listed for trading. Exceptions do exist to this rule. In IPOs, the TASE requires that the transferability of the shares held by pre-existing shareholders be 'locked up' for designated periods of time following the IPO (with certain exceptions as specified in the TASE regulations). Similarly, the Securities Law restricts the resale on the TASE of publicly traded shares placed in private placements for certain periods of time.

13 Compulsory repurchase rules

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

A company may include in its articles of association a provision permitting it to issue redeemable securities. Such redemption may be compulsory (call option of the company) or voluntary (put option of the security holder), as provided in the articles of association.

As for compulsory purchases and squeeze-out of minority shareholders, the Companies Law provides that a shareholder acquiring shares that bring its holdings to over 90 per cent must issue a 'full' tender offer for the remaining shares of the company. If the tender is accepted, and less than 5 per cent remain in the hands of the minority shareholders, the Companies Law mandates compulsory sale of these remaining shares. In addition, if a merger proposal is approved in a general meeting, shareholders that voted against the merger will be compelled to sell their shares in the merger.

14 Dissenters' rights

Do shareholders have appraisal rights?

Pursuant to the Companies Law, shareholders have appraisal rights in 'full' tender offers (whether they oppose or agree to the offer), but not in mergers. If a fair stock price is determined by the court, the offeror (not the company) shall have to pay such price to shareholders who exercised their rights (or to all shareholders, if a class action was filed). An offeror may provide in the tender offer documents that the appraisal rights will be available only to those shareholders who opposed the offer (though such conditions may discourage acceptance of the offer).

The responsibilities of the board (supervisory)

15 Board structure

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

The board structure for listed companies is best categorised as a one-tier structure; external directors, however, are elected for a mandatory three-year term.

16 Board's legal responsibilities

What are the board's primary legal responsibilities?

The board is responsible for determining the policy of the company and supervising the performance of the functions and acts of the general manager within that framework. In addition, the board is responsible for the following matters:

- determining the company's plans of action, the principles for funding them and the priorities between them;
- examining the company's financial status, and setting the credit limits of the company;
- determining the organisational structure of the company and its wage and compensation policies;
- issuance of debentures;
- preparation of financial reports and certification thereof;
- reporting to the annual general meeting on the position of the company's affairs and on the outcome of its business activities;
- appointing and removing the general manager;
- deciding on acts and transactions requiring its approval pursuant to the articles of association or the Companies Law (primarily, related-party transactions or transactions involving conflicts of interest);
- issuance of shares and convertible securities;
- distributions and dividends; and
- providing its opinion to the shareholders on 'special' tender offers (within the meaning of the Companies Law).

17 Board obligees

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

Pursuant to the Companies Law, the board's fiduciary duties (duty of loyalty and duty of care) are to the company and the directors must represent and protect the company's best interests. However, this does not preclude a director from owing fiduciary duties towards another person. Therefore, although the Companies Law includes no general duty of the directors to the shareholders, it has been determined by case law that such duties may arise in special circumstances.

Pursuant to the Securities Law, directors shall be liable towards security holders for any damage caused by virtue of the company's violation of the provisions of the Securities Law or the regulations enacted thereunder and for damage caused by the inclusion of a misleading item in the prospectus, subject to certain defences included in the Securities Law.

18 Enforcement action against directors

Can an enforcement action against directors be brought by, or on behalf of, those to whom duties are owed?

Pursuant to the Companies Law, the company is eligible to directly file suit against a director who breached his or her duties (subject to any exemption granted by the company (see question 32)). Shareholders and directors are entitled to initiate a derivative action on behalf of the company, should the company fail to take the necessary action against directors in breach of their fiduciary duties. A derivative action requires the approval of the court, which shall give approval if it is convinced that the action and the conduct thereof are prima facie in the best interests of the company and that the plaintiff is not acting with lack of good faith. In a decision dated 27 August 2014, the Israeli Supreme Court acknowledged, for the first time, a shareholder's right to file a multiple derivative action.

19 Care and prudence

Do the board's duties include a care or prudence element?

Pursuant to the Companies Law, a director owes the company a duty of care. In order to act with the level of care prescribed under the law, a director shall act with the standard of care with which a reasonable director, in the same position and in the same circumstances, would act, which shall include taking reasonable steps, in view of the circumstances of the case, to obtain information regarding the business expedience of an act submitted for his or her approval or of an act done by him or her by virtue of his or her position, and to obtain all other pertinent information regarding such acts.

20 Board member duties

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

Under the Companies Law, the duties of individual members of the board do not differ, regardless of their skills or experience. For example, clause 253a of the Companies Law states that nominating a director with accounting and finance expertise or professional qualifications does not change the responsibilities assigned to him or her and the other directors in the company. However, as set forth above, the law does require all directors to act with the level of care that a reasonable director would have taken. A court may consider the skill and experience of different directors in setting the level of care expected from such directors and determining liability for breaches of the duty of care.

21 Delegation of board responsibilities

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

Generally, pursuant to the Companies Law, the board may not delegate its responsibilities to management or other persons. The board may, however, delegate some of its responsibilities to a directors' committee, subject to certain exceptions set out in the Companies Law.

22 Non-executive and independent directors

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

The Companies Law includes a requirement that a public company appoint two 'external directors' (ie, directors who do not have a connection to the company or to a controlling shareholder). In order to minimise the dependence between the external director and the company or a controlling shareholder, the law provides that dismissal of an external director before the end of his or her term (which is statutorily set to three years) can be affected only in special circumstances and requires a special majority of the shareholders. Moreover, there are restrictions regarding the remuneration and appointment of external directors and, particularly, the appointment of external directors for additional terms. External directors must have either professional skills or accounting and financial expertise.

Pursuant to the Companies Law, a public company may also appoint to the board 'disinterested directors'; a disinterested director must fulfil all the requirements of an external director (except for residency requirements, which apply to external directors of companies that are listed on the TASE only), as well as not having held a position of a director in the company for the past nine years.

As mentioned in question 20, the board members' responsibilities do not differ.

23 Board size and composition

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

Pursuant to the Companies Law, the annual general meeting appoints the directors (both serving directors and new appointments), unless otherwise provided in the articles of association. A company may prescribe in its articles of association the maximum and minimum number of seats on the board. Notwithstanding this, the Companies Law contains general provisions with regard to the number of directors that may be appointed to the board of public companies. In this regard, reference is made in the Companies Law to the appointment of at least four directors to serve as members of the board of public companies. This fact stems from the provisions of the Companies Law, in terms of which the Audit Committee of the company will comprise at least three directors, with the chairman of the board being unable to serve as a member of the Audit Committee. The provisions of the law define particular rules with regard to specific companies, so that, for example, directives of the Supervisor of Banks provide that the board of directors of a banking corporation will consist of between seven and 15 directors. Further, a person who is a candidate to hold office as a director must state that he or she possesses the required skills and time to fulfil his or her responsibilities, considering the size and needs of the company. The Companies Law also lists the following criteria board members must fulfil:

- a person may not serve as a director if he or she has been convicted of one of the offences listed in that section, until five years have passed since the conviction (the listed offences are those that relate mainly to bribery and fraud, or are offences committed by directors, violations of securities laws and offences, which because of their nature, severity or circumstances the court has determined that the convicted person may not serve as a director of a public company);
- minors, legal incompetents, and those who have been declared bankrupt and have not yet been released from that status may not be appointed as directors as well; and
- there are no residency restrictions for a director who is not an external director.

The following information regarding company directors must be made available to investors in the annual report: personal details, membership of board committees, status as external or disinterested director, status as an employee of the company or affiliated companies, tenure on the board, educational background, occupation during the previous five years, list of companies in which he or she serves as director, whether he or she is a relative of another principal shareholder, directors or key executives and expertise in accounting or finance.

24 Board leadership

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

Pursuant to the Companies Law, a public company's CEO or his or her relative or subordinate may not serve as chairman of the board, and the CEO's powers will not be conferred upon the chairman of the board. A special majority in the general meeting may authorise the chairman of the board to fulfil the role of CEO for periods of up to three years (pursuant to an amendment on 3 April 2016 to the Companies Law Regulations, for companies that offer securities to the public for the first time, such authorisation is required only after five years from the date the company became a public company).

25 Board committees

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

The board of a public company must appoint from its members an audit committee, which shall be responsible for locating defects in the company's business administration and making proposals to the board regarding ways for correcting such defects. The audit committee must also approve related-party transactions or other transactions involving conflicts of interest (except for compensation-related transactions, which are generally approved by the compensation committee). The audit committee must include at least three board members and all of the external directors. The majority of members must be disinterested or external directors.

The Companies Law regulations also require the board to establish a financial statements committee to examine the financial statements of the company, which must include at least three members, all of whom must be board members and a majority of whom must be disinterested or external directors. All members must be able to read and understand financial statements and at least one member must have accounting and financial expertise. An audit committee that meets these criteria may also serve as the financial statements committee.

Pursuant to a recent amendment to the Companies Law, the board of a public company must also appoint from its members a compensation committee. As part of its functions, the compensation committee will be responsible for making recommendations to the board regarding the company's compensation policy for directors and officers (collectively referred to in the Companies Law as 'office holders') and to update the same from time to time. The compensation committee will also have responsibility for deciding whether to approve transactions regarding the terms of office and service of office holders and controlling shareholders that require its approval under the law (see questions 28 and 29). The members of the compensation committee shall include at least three board members and all the external directors. The external directors shall constitute the majority of members.

In all three committees, no controlling shareholder, his or her relative, executive director or director who regularly provides services to the company or to a controlling shareholder may serve as a member.

Under the Companies Law, the board may establish additional directors' committees, unless the articles of association provide otherwise. The law stipulates that if a certain responsibility is delegated to a committee, all members of that committee must be board members and at least one member in each such committee must be an external director. A directors' committee whose function is to advise the board, or to make recommendations only, may comprise of members who are not directors, unless the articles of association provide otherwise.

26 Board meetings

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

The Companies Law provides that the board shall be convened for meetings 'according to the needs of the company', but the board of a public company must be convened at least once every three months. The chairman of the board, or a number of directors as required by the Companies Law, may convene the board at any time.

27 Board practices

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

Pursuant to the Companies Law, a company must prepare minutes of the proceedings at meetings of the board and of board committees and to keep them at its registered office for a period of seven years from the date of the meeting. Board procedures are generally not publicly available; however, in certain cases in which shareholders are entitled to receive information regarding transactions that require shareholder approval, the related board procedures may also be subject to disclosure.

28 Remuneration of directors

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

A transaction between a public company and a director regarding his or her terms of office and service, requires the approval of each of the compensation committee, the board and the general meeting. Such approval of the compensation committee and the board will be given in accordance with the company's compensation policy (except in exceptional circumstances), which will be determined, inter alia, based on considerations such as the size of the company and the nature of its activities, the furtherance of its objects, the creation of appropriate incentives for office holders as well as the contribution of office holders to realising the company's objectives.

The remuneration terms of external directors are set out in regulations enacted under the Companies Law. If their remuneration is set in accordance with the regulations, the approval thereof will not require the consent of the general meeting.

Directors are usually appointed for a one-year service period, unless provided otherwise in the articles of association, except for external directors, who are elected for service terms of three years.

Pursuant to the Companies Law, any other transaction (including a loan) between a company and a director as well as a transaction between a company and another person in which a director has a personal interest will require the consent of the board, unless some other manner of approval is prescribed in the articles of association. An extraordinary transaction, as defined by the Companies Law, will also require the approval of the audit committee. Where the director is also a controlling shareholder or relative thereof, the transaction will also require the approval of the general meeting with a special majority.

29 Remuneration of senior management

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

Generally, a transaction between a company and an officer (who is not a director) regarding his or her terms of office and service, except in exceptional circumstances, will be consummated in accordance with the company's compensation policy. Such a transaction will require the approval of the compensation committee and thereafter the approval of the board. A transaction between the company and the general manager or controlling shareholder (or his or her relative) regarding his or her terms of office and service will also require the approval of the general meeting with a special majority (although, recent amendments to the Companies Law Regulations provides certain exemptions to this provision, especially with regard to companies that offer securities to the public for the first time). Where the candidate for the office of general manager is not related in any way to the company, the compensation committee may exempt the general meeting from approving a transaction that accords with the compensation policy if its finds that referral of the transaction for the approval of the general meeting will frustrate the transaction. A new amendment to the Companies Law regulations provides that dual-listed companies and foreign companies shall include in their notice of the annual general meeting for a given financial year, a full and personal description of the respective terms of service of the five office holders who, during that year, received the highest remuneration in the company.

Changes to existing terms of remuneration will only require the approval of the compensation committee, subject to confirmation by the compensation committee that the changes are not material.

Pursuant to the Companies Law, any other transaction (including a loan) between a company and a senior manager as well as a transaction between a company and another person in which a senior manager has a personal interest, will require the consent of the board, unless some other manner of approval is prescribed in the articles of association. An extraordinary transaction, as defined by the Companies Law, will also require the approval of the audit committee. Where the senior manager is also a controlling shareholder or relative thereof, the transaction will also require the approval of the general meeting with a special majority.

30 D&O liability insurance

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

Pursuant to the Companies Law, a company may, if the articles of association so permit and subject to receiving the necessary approvals, as set out in question 28 (with respect to remuneration of directors) and question 29 (with respect to remuneration of senior managers), take out a liability insurance policy for its office holders with respect to any liability imposed on them due to an act performed by them in their capacity as such, with respect to each of the following:

- a breach of the duty of care towards the company or to another person;
- a breach of the duty of loyalty towards the company, provided that the office holder acted in good faith and had a reasonable basis for believing that the act would not harm the company interests; and
- a financial liability imposed on the office holder in favour of another person.

Notwithstanding the foregoing, a provision in the articles of association permitting the company to purchase directors' and officers' liability insurance with respect to any of the following will not be valid:

- a breach of duty of loyalty, except if such breach is committed by an office holder acting in good faith and with reasonable basis for believing that the act would not harm the company's interests;
- a breach of duty of care committed intentionally or recklessly, except if committed only in a negligent manner;
- an act performed with intent to make unlawful personal profit; or
- a fine imposed upon such office holder.

D&O liability insurance is common in public companies in Israel and the company often pays the premium.

31 Indemnification of directors and officers

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

Pursuant to the Companies Law, a company may, if the articles of association so permit and subject to receiving the necessary approvals, as set out in question 28 (with respect to remuneration of directors) and question 29 (with respect to remuneration of senior managers), indemnify office holders with respect to any liability imposed on them or

Update and trends

The business judgement rule
For the first time, the Supreme Court in Israel adopted the 'business judgement rule' into Israeli law. This precedential ruling dealt with the request to approve a derivative action filed on behalf of Bezeq (The Israel Telecommunication Corp) against the controlling shareholder of the company and other officers regarding the capital reductions and dividend distributions that were made after the controlling shareholder acquired Bezeq through a leveraged buyout. The claim alleged, inter alia, that the distribution of the dividends was intended to enable the controlling shareholder to repay the loan he had taken to acquire control of Bezeq. The new court ruling is a comprehensive guide for the way in which judges review corporate executives' business decisions. The judges in this case made a great effort to render a decision that would create more certainty in the market regarding the issue of judicial intervention in corporate decisions. After many years of attempts, the Israeli Supreme Court adopted the 'business judgement rule' into Israeli law in a precedential manner.

Amendments to the Companies Law regulations
Certain amendments to the Companies Law regulations were published this past year, which deal with easing the restrictions in the area of corporate governance. The amendments are part of a general aim, inter alia, to remove barriers and to encourage companies' entry into the capital market. Among the variety of topics the amendments dealt with can be found terms and conditions of officers' employment, compensation of external directors, easing transactions with interested parties, etc. For instance, one of the amendments states that CEOs may update the compensation of their officers without the need for the compensation committee's approval, provided that the terms of office of the officer conform with the remuneration policy of the company and that the remuneration policy determines that an immaterial change in the terms of the office of an officer, within the limits stipulated in the remuneration policy, may be approved by the CEO of the company.

expenses incurred by them owing to an act performed by them in their capacity as such, with respect to each of the following:
- a financial liability imposed upon the office holder for the benefit of another person pursuant to a judgment, including a judgment given in settlement or an arbitral award approved by the court (financial liability);
- reasonable litigation expenses, including attorneys' fees, incurred by the office holder in an investigation or proceeding against him or her, in which no criminal indictment has been filed; and
- reasonable litigation expenses, including attorneys' fees, incurred by the office holder or charged to him or her by the court, in a proceeding filed against him or her by or on behalf of the company or by any other person, or for a criminal charge from which he or she was acquitted or for a criminal charge in which he or she was found guilty of an offence not requiring proof of criminal intent.

A provision in the articles of association regarding indemnity may be one of the following:
- a provision permitting the company to give an undertaking in advance to indemnify its office holders, provided that such undertaking, when related to 'financial liability', as aforementioned, be limited to types of events that in the opinion of the board can be foreseen at the time of granting the undertaking to indemnify and to a sum determined by the board as reasonable in the circumstances of the case; or
- a provision permitting the company to indemnify its office holder ex post facto.

Notwithstanding the foregoing, a provision in the articles of association permitting the company to indemnify office holders with respect to any of the following will not be valid:
- a breach of duty of loyalty, except if such breach is committed by an office holder acting in good faith and with reasonable basis for believing that the act would not harm the company interests;
- a breach of duty of care committed intentionally or recklessly, except if committed only in a negligent manner;
- an act performed with intent to make unlawful personal profit; or
- a fine imposed upon such office holder.

Indemnification provisions are common in public companies in Israel.

32 Exculpation of directors and officers

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

Pursuant to the Companies Law, a company may, if the articles of association so permit and subject to receiving the necessary approvals, as set out in question 28 (with respect to remuneration of directors) and question 29 (with respect to remuneration of senior managers), exempt office holders in advance in relation to their liability toward the company with respect to damages resulting from a breach of the duty of care, except for liability in respect of breach of the duty of care regarding distributions.

Notwithstanding the foregoing, a provision in the articles of association permitting the company to exempt office holders from their liability toward the company with respect to any of the following shall not be valid:
- a breach of duty of loyalty;
- a breach of duty of care committed intentionally or recklessly, except if committed only in a negligent manner;
- an act performed with intent to make unlawful personal profit; or
- a fine imposed upon such office holder.

33 Employees

What role do employees play in corporate governance?

The employees' role in the company's corporate governance is not mandated or prescribed by law, but companies may engage employees in various ways in this respect. For example, employees may take part in the internal audit process or in overseeing the implementation of internal corporate governance guidelines.

34 Board and director evaluations

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

The evaluation of the board, its committees or directors is not mandated or prescribed by law, regulation or listing requirements. As a matter of practice, some advisory firms may publish, from time to time, their evaluation regarding the corporate governance of public companies, including views regarding the board's structure and policies.

Disclosure and transparency

35 Corporate charter and by-laws

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

Public companies' articles of association are published on the ISA website (MAGNA) as well as on the TASE website (MAYA) and, thus, are available for inspection by the public.

36 Company information

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

Pursuant to the Securities Law, all reports filed by public companies are generally available for inspection by the public via the ISA and TASE websites (MAGNA and MAYA respectively). A public company must also report to the registrar of companies on issues relating to name change, change of address of the registered office, merger or change in the type of company (eg, a private company that has become a public company or a public company that has become a private company).

The Securities Law and Securities Regulations define the reporting requirements of a public company and determine that a public company is obliged to submit three types of reports to the ISA and the TASE: annual, quarterly and immediate. The annual report must include, inter alia, a description of the company's business, the board's report on the state of the company's affairs, financial statements and a report on the effectiveness of internal control over financial reporting and disclosure. The quarterly report must include, inter alia, interim financial statements, an interim directors' report and an interim report on the effectiveness of internal control over financial reporting and disclosure. An immediate report shall be submitted for each of the list of events that are defined by law as important to a reasonable investor contemplating the purchase or sale of securities of the company (eg, a change in the issued or registered capital, a decision regarding the amendment of the articles of association, changes in holdings of interested shareholders, etc).

Hot topics

37 Say-on-pay

Do shareholders have an advisory or other vote regarding executive remuneration? How frequently may they vote?

The Companies Law sets forth a unique mechanism for the voting by shareholders regarding the company's compensation policy as well as the approval of the terms of office and service of an office holder (who is neither a director nor controlling shareholder).

Pursuant to the law, the board of a public company shall set a compensation policy, after considering the recommendations of the compensation committee. The compensation policy requires the approval of the general meeting with a special majority. However, the board may also determine the compensation policy even if the general meeting opposes its approval (except where the matter concerns a second-tier subsidiary) and only where the compensation committee and, thereafter, the board have decided, based on detailed reasons and after discussing the matter anew, that approval of the compensation policy, despite the opposition of the general meeting thereto, is in the interests of the company.

Similarly, approval of the terms of office and service of an office holder (who is neither a director nor controlling shareholder) not determined in accordance with the compensation policy requires the approval of the general meeting (with special majority). Nonetheless, the compensation committee and the board may approve a transaction for determination of the terms of office and service of an office holder in special circumstances, and provided also that the matter does not concern a second-tier subsidiary, even if the general meeting opposes approving the same.

Approval of the terms of office and service of the general manager (who is neither a director nor controlling shareholder) requires the approval of the general meeting (with special majority) irrespective of whether such terms are in accordance with the compensation policy. Nonetheless, the compensation committee and the board may approve a transaction for determination of the terms of office and service of a general manager in special circumstances, and provided also that the matter does not concern a second-tier subsidiary, even if the general meeting opposes approving the same.

38 Shareholder-nominated directors

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

As described in question 7, pursuant to the Companies Law, shareholders may call general meetings and propose matters to be included on the agenda of general meetings, including those pertaining to the nomination and election of directors.

Companies must allow shareholders to vote on the appointment of directors by written ballot without requiring their presence at the general meeting, and to send shareholders the written ballots (which will set out all nominees to the board, including those made by shareholders) in advance of the meeting, at the company's expense. Companies are further required to distribute the written opinions on agenda items, of shareholders who requested them, to the other shareholders, and such distribution will be at the company's expense if so prescribed in the articles of association (otherwise, the company may charge the requesting shareholders for reimbursement of its reasonable distribution costs).

A new amendment to the Securities Law sets forth a mechanism for an electronic voting platform, which will allow shareholders and holders of warrants of public companies to vote by means of the electronic voting platform on diverse matters that require shareholder approval, including the appointment of directors.

39 Shareholder engagement

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

In public companies, a small number of shareholders do actually participate in the annual meetings and, in most cases, send proxies. However, due to institutional shareholders and their reliance on proxy advisory firms (such as Entropy Risk Management Solutions), there seems to be more engagement, especially in high-profile issues such as executive compensation. The participants on behalf of the company are usually the chairman of the board of directors or another authorised officer, depending on the issue in debate. The engagement typically occurs during annual meetings and periodic public reporting to the stock exchange and not on a continuous basis; nonetheless, companies occasionally publish presentations on the stock exchange website and invite discussion on the presented topic.

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Sources of corporate governance rules and practices

1 Primary sources of law, regulation and practice

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

The primary regulation is the Italian Civil Code (ICC). Further, Legislative Decree No. 58 of 24 February 1998 – the Italian Financial Act (TUF) – is applicable to listed companies. Listed companies may choose to comply (under the 'comply or explain' principle) with the provisions of the Corporate Governance Code issued by the Corporate Governance Committee of the Italian Stock Exchange in 2006, amended in 2010 and in July 2015 (the Code).

2 Responsible entities

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

The primary entity responsible for making rules and enforcing laws is Parliament, but, in some cases established by the Italian Constitution, laws may also be adopted by the government and the ministries. Further, regulations are issued by authorities, such as the Italian Stock Exchange (Borsa Italiana SpA), Consob (the Italian stock market regulatory authority) and the Bank of Italy.

Particular groups and associations whose views are taken into consideration on the enactment of new regulations and laws include the Italian Confederation of Industries (Confindustria), trade unions, Assonime (the listed companies' association), consumer associations and associations related to particular sectors.

The rights and equitable treatment of shareholders

3 Shareholder powers

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

In SpAs adopting the traditional system or the one-tier system, as well as in Srls, the shareholders' meeting shall appoint and remove directors, using the majority principle. However, in Srls, management is usually entrusted to the quotaholders, unless otherwise provided in the company's by-laws.

Under article 2351 of the ICC each share gives the right to vote. Other than as provided in special laws, the by-laws may provide for the creation of shares without voting rights, with voting rights limited to specific matters or with voting rights subordinated to the occurrence of certain conditions not merely dependent on the exercise of individual rights. The value of such shares cannot be higher in aggregate than one-half of the capital.

Under paragraph 4 of the above-mentioned article, shares carrying multiple voting rights can be issued, but each multiple voting share can have up to a maximum of three voting rights.

According to article 2380-bis of the ICC, board activity is characterised by autonomy and exclusivity. The shareholders cannot, therefore, interfere with the management of the business or take formal steps to require the board to pursue a particular course of action; they can only remove the directors at a shareholders' meeting or choose not to re-elect them when their tenure expires.

4 Shareholder decisions

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

In SpAs adopting either the traditional system or the one-tier system, the ordinary shareholders' meeting shall:

- approve the annual financial statements;
- appoint and remove directors and auditors and the subject to whom the audit of the statutory accounts is entrusted;
- establish the directors' and auditors' remuneration, if not established in the by-laws;
- resolve on the directors' and auditors' liability;
- resolve on other matters attributed to the meeting by law or the by-laws; and
- approve the procedural rules, if any, for the meeting.

In SpAs adopting the two-tier system, the ordinary shareholder shall:

- appoint and remove the members of the supervisory board;
- establish their remuneration;
- resolve on their liability;
- resolve on the distribution of profits; and
- appoint the subject to whom the audit of the statutory accounts is entrusted.

In SpAs the extraordinary shareholders' meeting shall resolve on amendments to the by-laws, the appointment, the replacement and the powers of the liquidators and on any other matter attributed to it by law.

In Srls, the quotaholders resolve on:

- the approval of the financial statements and the distribution of profits;
- the appointment of the directors, if provided by the by-laws;
- the appointment of the auditors and the subject to whom the audit of the statutory accounts is entrusted, if necessary;
- the amendments of the by-laws;
- the decision to enter into a transaction that may involve amendments to the company's purpose or to the quotaholders' rights; and
- other matters attributed to them through the by-laws and on every other matter the directors or the quotaholders representing at least one-third of the capital submit for their approval.

5 Disproportionate voting rights

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

In SpAs, the principle 'one share, one vote' normally applies. However, the by-laws may provide for the creation of classes of shares without voting rights, with voting rights limited to specific matters or subordinated to certain conditions. In any event, the value of such shares cannot be greater in aggregate than half the share capital. Further, in companies that do not have recourse to the risk capital market, the by-laws may provide that voting rights shall be limited to a maximum amount or that they must be staggered. The by-laws may provide also for shares with multiple voting rights (up to a maximum of three votes for each share).

In Srls, the vote of each quotaholder is valid in proportion to its quota.

6 Shareholders' meetings and voting

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

SpA

Shareholders' meetings are duly assembled with the presence of as many shareholders as represent at least half of the company's share capital, excluding shares without voting rights. The ordinary meeting passes resolutions by an absolute majority of the attendees unless a higher majority is required by the by-laws.

An extraordinary meeting passes resolutions with the vote in favour of as many shareholders as represent more than half the share capital of the company unless a higher majority is required by the by-laws. Extraordinary meetings of companies that have recourse to the risk capital market are duly assembled when as many shareholders as represent at least half of the capital or a higher percentage provided for in the by-laws are present and such a meeting passes resolutions with a vote in favour of at least two-thirds of the share capital present at the meeting.

If the shareholders present do not represent the proportion of capital required for a quorum, the meeting must be called again. At the second meeting, the ordinary shareholders' meeting passes resolutions on the matters that should have been dealt with at the first meeting, regardless of the part of capital represented by shareholders in attendance, while an extraordinary meeting is duly assembled with the presence of shareholders representing more than one-third of the share capital and passes resolutions with a vote in favour of at least two-thirds of the share capital present at the meeting.

To participate in the meeting, if the shares are in registered form, the company shall record in the shareholders' book those shareholders who have attended the meeting or who have deposited their shares. In any event, the by-laws may allow for attendance at the meeting through telecommunications or the expression of a vote by correspondence.

Srl

The by-laws may provide that quotaholders adopt decisions through written consultation or on the basis of consent expressed in writing: the documents must be signed by the quotaholders and the subject matter of the resolution, as well as the consent to it, must be made clear.

Otherwise, the quotaholders' meeting must be called, in the manner established in the by-laws, when required by the directors or by quotaholders representing at least one-third of the capital. The quotaholders' meeting must also be called in the event of decisions regarding amendments to the by-laws, decisions to enter into transactions that cause a substantial change in the corporate purpose or a significant change in the rights of the quotaholders, and decisions regarding the reduction of capital for losses.

Generally in Srls, decisions are validly adopted with the presence of as many quotaholders as represent at least half the capital and decisions are passed by an absolute majority of the attendees. However, decisions regarding amendments to the by-laws or decisions to enter into transactions that cause a substantial change in the corporate purpose or a considerable change in the rights of the quotaholders are adopted with the vote in favour of quotaholders representing at least half of the capital.

Further, if provided by the by-laws, quotaholders may attend the meeting through telephone or video conferencing.

7 Shareholders and the board

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

Once directors have been appointed, the shareholders' meeting can no longer give binding orders to the directors regarding the performance of management acts. In SpAs, the directors or the management board shall call a shareholders' meeting without delay when requested by as many shareholders as represent at least one-tenth of the company's share capital (or one-twentieth, if the company participates in the venture capital market) or a lower percentage provided for in the by-laws. If the directors, the management board, the auditors, the supervisory board or the control committee, in their stead, fail to proceed, the calling of the meeting is ordered by a decree of the president of the court, if the refusal to call the meeting is unjustified. However, the calling of a meeting at the request of the shareholders is not allowed on matters that the meeting resolves pursuant to law upon the proposal of the directors or on the basis of a project or of a report prepared by them.

In Srls, the quotaholders' meeting must be called if requested by a number of quotaholders representing at least one-third of the capital.

8 Controlling shareholders' duties

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

Under Italian law, general and specific duties are provided for directors and not for controlling shareholders. There are specific provisions concerning the challenge of shareholders' resolutions in which the controlling shareholders can decide the vote.

In SpAs, any adopted shareholders' resolution that is not in compliance with the law or the by-laws may be challenged by shareholders who were not present, or dissented or abstained from the vote (as well as by the directors, the supervisory board or the auditors). Apart from the not present, dissident or abstained shareholders, shareholders who own as many shares with voting rights with reference to the specific resolutions as represent on aggregate at least one per thousand of the capital in companies having recourse to the risk capital market and 5 per cent in other cases; the by-laws may reduce or exclude such a requirement. Shareholders who do not represent the required portion and those who are not entitled to challenge the resolution are entitled to damages caused to them by the non-compliance of the resolution with law or with the by-laws.

In Srls, management is usually entrusted to the quotaholders, unless otherwise provided in the by-laws. Quotaholders who do not participate in management of the entity have the right to receive news on the business from the directors and to consult, through professionals in their trust, the company's books and the documents relating to the management. Each quotaholder may promote an action for liability against the directors and may also request, in the event of serious irregularities in the management of the company, that a precautionary order of revocation of the directors be adopted.

9 Shareholder responsibility

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

In SpAs and Srls, only the company is liable for the company's obligations. However, in the event of insolvency, for obligations incurred during the period in which the shares or quotas are held by a sole shareholder or quotaholder, such a person has unlimited liability when payment-in on capital has not been made pursuant to law or until the notice formalities are complied with as required by law.

Further, members have unlimited liability in a general partnership, a limited partnership and a partnership limited by shares and, therefore, the company's bankruptcy entails the members' bankruptcy.

Corporate control

10 Anti-takeover devices

Are anti-takeover devices permitted?

Directors of listed companies must refrain from actions or transactions that could counteract the achievement or the aims of the offering for the period from the date of notice of the offering until closure of the offering or until the offering expires, unless approved by the shareholders' meeting.

11 Issuance of new shares

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

In SpAs, the by-laws can grant to directors the power to increase capital one or more times up to a specified amount and for a maximum period of five years. The minutes of the board of directors' resolution increasing the capital shall be drawn up by a notary and must be filed and registered at the registry of enterprises.

In the case of a capital increase, newly issued shares and debentures convertible into shares shall be offered under option to shareholders in proportion to the number of shares owned by them. However, no option right is given with regard to newly issued shares that must be paid by contributions in kind and, if it is in the interests of the company, the option right can be denied or limited.

12 Restrictions on the transfer of fully paid shares

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

The by-laws may subject the transfer of shares or quotas to special conditions, such as pre-emption rights in favour of the other shareholders or quotaholders or the consent of the corporate organs or of the other shareholders or quotaholders, and may prevent their transfer for a period of time. In an SpA, the prohibition on transferring shares is valid for no longer than five years from the date of incorporation of the company or from the time when the prohibition is introduced, while in an Srl, there are no time limits, but the quotaholder or his or her heirs are entitled to withdraw from the company at any time.

13 Compulsory repurchase rules

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

Repurchases are allowed and may be provided in share transfer agreements.

14 Dissenters' rights

Do shareholders have appraisal rights?

In an SpA, shareholders who did not participate in the following resolutions are entitled to withdraw from the company:
- amendments to the company's purpose that lead to a significant change in the company's activities;
- transformation of the company;
- transfer abroad of the company's registered office;
- revocation of liquidation;
- elimination of one or more of the reasons for withdrawal provided for in the by-laws;
- changes to the criteria for the determination of the value of shares in the event of withdrawal; and
- amendments to the by-laws concerning voting or participation rights.

Further, in companies established for an unlimited duration, which are not listed on regulated markets, the right of withdrawal is granted at any time.

Moreover, the by-laws may provide for the withdrawal right in the following cases:
- extension of the life of the company;
- introduction or removal of liens on circulation of the share certificates; or
- additional circumstances when the company does not have recourse to the risk capital market.

The by-laws of an Srl determine when the quotaholders are entitled to withdraw from the company and the related methods. In any event, quotaholders who have not consented to the change of the corporate purpose or to the type of company, to its merger or demerger, to the revocation of the status of liquidation, to the transfer of the legal address abroad, to the cancellation of one or more causes for withdrawal provided in the by-laws and the completion of transactions that cause a substantial change to the purpose of the company established in the by-laws or in a relevant change to the rights attributed to the quotaholders, are entitled to withdraw. Further, if it is a company without a term, the right of withdrawal may be exercised by quotaholders at any time.

The responsibilities of the board (supervisory)

15 Board structure

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

Most listed companies adopt the traditional system. One-tier and two-tier systems are rare in Italy.

16 Board's legal responsibilities

What are the board's primary legal responsibilities?

The management of the company is the exclusive responsibility of the directors and their primary duty and responsibility is achieving the corporate purpose.

17 Board obligees

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

The directors shall fulfil the duties imposed upon them by the law and by the by-laws with the diligence required by the nature of the appointment and by their specific competence. They are jointly liable towards the company for damages caused by the non-observance of such duties, except for functions vested solely in the executive committee or in one or more directors. Moreover, directors are liable towards company creditors for non-observance of their duties concerning the preservation of the company's assets.

18 Enforcement action against directors

Can an enforcement action against directors be brought by, or on behalf of, those to whom duties are owed?

SpA

An action for liability of the directors can be brought pursuant to a resolution of the shareholders' meeting and may be started within five years of the termination of a director's office.

Further, a company action may also be exercised by shareholders representing at least one-fifth of the capital or such different percentage indicated in the by-laws, which in any event cannot be greater than one-third and, in companies having recourse to the risk capital market, may be brought by shareholders representing one-twentieth of the capital.

An action for liability against directors may also be brought by creditors when the company's assets prove insufficient for the satisfaction of their claims.

Finally, individual shareholders and third parties are entitled to compensation for damages if they are directly damaged as a result of malice, fraud or negligence of the directors. In this case, the action may be brought within five years of the act that damaged the shareholder or the third party.

In companies adopting the two-tier system, an action for liability against directors may be brought by the shareholders, as explained above, or by the supervisory board.

Srl

An action for liability against directors may be brought by each quotaholder. Further, any quotaholder or third party who has been directly damaged by wilful or negligent acts of the directors is entitled to compensation for damages.

19 Care and prudence

Do the board's duties include a care or prudence element?

Under the ICC, directors shall fulfil the duties imposed upon them by law and by the by-laws with the diligence required by the nature of the appointment and by their specific competences.

The same rules apply to the members of the management board in companies adopting the two-tier system.

20 Board member duties

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

Different skills of the directors may be taken into consideration by the shareholders' meeting when appointing them and may also be indicated in the relevant resolution. Further, directors' specific competences are evaluated for determining their duties.

21 Delegation of board responsibilities

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

The board of directors fixes the content, the limits and the methods for the exercise of the delegated powers; it may always give directives to the delegated bodies and bring back to the board transactions falling within the delegation received. In any event, the following functions cannot be delegated:

- the issue of bonds, if delegated to the board;
- the drafting of financial statements;
- an increase in the share capital, if delegated to the board;
- a reduction of the share capital for losses or if it falls below the legal limit; and
- a drafting of merger or demerger projects.

The same rules apply to the members of the management board in companies adopting the two-tier system.

22 Non-executive and independent directors

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

For listed companies, the Code provides that the board of directors shall be made up of executive and non-executive directors with an adequate competence and expertise, establishing only that the number, competence, authority and time availability of non-executive directors shall be such as to ensure that their judgement may have a significant impact on the board's decisions.

Under the Code, the following are qualified as executive directors:

- the managing directors of a listed company or one of its subsidiaries having strategic relevance, including the relevant chairmen when they are granted individual management powers and when they play a specific role in the establishing of the business strategies;
- the directors vested with management duties within the listed company or in one of its subsidiaries having strategic relevance, or in a controlling company when the office also concerns the listed company; and
- the directors who are members of the executive committee of the listed company, when no managing director is appointed or when the participation on the executive committee, taking into account the frequency of the meetings and the scope of the relevant resolutions, effectively entails the systematic involvement of its members in the day-to-day management of the listed company.

23 Board size and composition

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

According to paragraph 4 of article 2380-bis of the ICC, if the by-laws make no provision for the number of directors, but indicate only the maximum and minimum number, the number is determined by the shareholders' meeting.

Both a sole director or a number of directors may be appointed in unlisted SpAs, but a board of directors must be appointed in listed companies.

The board of directors selects the chairman from among its members, unless he or she is appointed by the meeting.

The number of members of the board of directors is normally selected according to the requirements of the company concerned. In Italy, small and medium-sized companies normally have a board of directors composed of three or five members; in listed companies the average is 13 members. Companies in the financial sector have a higher number of directors.

Legally sanctioned persons, persons disabled from their rights, bankrupts and those who have been convicted with a sentence entailing legal sanction, even temporary, from public office or are unable to exercise managerial functions, cannot be appointed directors or management board members and, if appointed, shall forfeit their office. These are known as causes of ineligibility.

Special laws provide for numerous causes of incompatibility with the office of the director (eg, civil servants, holders of government positions, members of Parliament and lawyers cannot sit on a board of directors). The causes of incompatibility, separate from the causes of ineligibility cited above, mean only that the person concerned must choose between the positions; thus the resolution appointing them is not null and void.

In companies adopting one-tier systems, at least one-third of the members of the board must hold the requirements of independence, which are:

- not having been sanctioned, deprived of their rights, bankrupted or convicted with a sentence entailing interdiction, even temporary, from public office or being unable to exercise managerial functions;
- not being a spouse or related to the directors of the company, the company, the relatives and those who are related by blood or marriage within the fourth degree to the directors of companies controlled by it, of companies that control it and of companies under common control; and
- not being related to the company or to companies controlled by it or to companies that control it or companies under common control by an employment relationship or by a regular consultancy contract or by other economic relationship that may prejudice the independence, as well as, if provided by the by-laws, requirements provided for in codes of conduct drafted by trade associations or by companies managing regulated markets.

For listed companies, the Code provides that the board shall be made up of executive and non-executive directors, as well as that an adequate number of non-executive directors (in any case, not less than two) shall be independent, in the sense that they do not maintain, nor have recently maintained, directly or indirectly, any business relationships with the listed company, or persons linked to it, of such a significance as to influence their autonomous judgement.

For listed companies, the by-laws must always provide for mechanisms appointing the board of directors that assure a balance between men and women (the 'pink share'). The gender less represented must obtain at least one-third of the elected positions. The same criterion is also valid for the oversight committee in the two-tier system.

According to article 2386 of the ICC, if in the course of the fiscal year a vacancy for one or more directors occurs, the others provide for their replacement by resolution approved by the board of statutory auditors, provided that the majority is always constituted by directors appointed by the meeting. The directors so appointed remain in office until the next meeting.

If vacancies of a majority of the directors appointed by the meeting occur, those who remain in office shall call a meeting to provide for filling the vacancies.

24 Board leadership

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

There are no mandatory rules on this. However, since the chairman and the CEO exercise different functions, the best practice recognises the separation between them.

In fact, with regard to listed companies, the Code provides that it is appropriate to avoid the concentration of corporate offices in one single individual. However, in the event that the chairman of the board of directors is the CEO of the company, the Code suggests that the board designates a lead independent director, who represents a reference and coordination point for the requests and contributions of non-executive directors and, in particular, of those who are independent.

25 Board committees

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

In companies adopting the one-tier system, a management control committee must be established within the board of directors. Unless otherwise provided in the by-laws, the board of directors shall determine the number and the appointment of the members of the committee.

However, the members of the committee cannot be less than three in companies that have recourse to the risk capital market.

The committee is formed by directors having the requirements of good repute and professional experience provided for in the by-laws, and the requirement of independence, who are not members of the executive committee and to whom powers or specific appointments are not delegated and who in any event do not perform functions pertaining to the management of the company or of the companies that control it or are controlled by it. At least one member of the committee must be selected from subjects registered in the register of accounting auditors.

The Code provides that listed companies shall establish among its members one or more committees with proposing and consultative functions. In particular, the board of directors shall:

- evaluate whether to establish a nomination committee among its members made up, for the majority, of independent directors;
- establish a remuneration committee among its members, made up of non-executive directors, the majority of whom are independent; and
- establish an internal control committee, made up of non-executive directors, the majority of whom are independent. If the listed company is controlled by another listed company, the internal control committee shall be made up exclusively of independent directors. At least one member of the committee must have adequate experience in accounting and finance, to be evaluated by the board of directors at the time of his or her appointment. However, committees may be avoided and, therefore, their duties shall be performed by the board if certain conditions established by the Code are met.

26 Board meetings

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

The law requires at least one board of directors' resolution per year for the annual approval of financial statements.

27 Board practices

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

Directors shall draft minutes for each board of directors' meeting, which must evidence the attending directors, the resolutions adopted and the directors dissenting or abstaining. Further, when a director is appointed (or is removed), his or her appointment must be filed at the registry of enterprises, also indicating his or her powers to act on behalf of the company.

In listed companies, the corporate governance report to be published annually must indicate, inter alia:

- agreements between companies and directors, members of the control body or supervisory council that envisage indemnities in the event of resignation or dismissal without just cause or if their employment contract should terminate as the result of a takeover bid;
- rules applying to the appointment and replacement of directors and members of the control body or supervisory council, and to amendments to the by-laws if different from those applied as a supplementary measure; and
- the existence of delegated powers regarding share capital increases or powers of the directors or members of the control body to issue security-related financial instruments or to authorise the purchase of the company's own shares.

28 Remuneration of directors

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

Under article 2389 of the ICC, directors are entitled to receive a remuneration for their activities. The directors' fee is established under the by-laws and if it is not provided therein, it may be established at the time of their appointment by the shareholders' meeting (in the one-tier and traditional administration system under article 2364, paragraph 1, No. 3 and 2389 of the ICC respectively) or by the supervisory board (in the two-tier system unless otherwise indicated in the by-laws).

Should the compensation not have been established (and there is no evidence that the directors have waived it), the directors may ask the court to set an appropriate amount.

Generally speaking the compensation is composed of: a fixed amount; a variable amount relating to the achievement of specific goals; special treatments when the termination occurs; and benefits like the personal use of certain company assets or an insurance policy for civil liability.

Remuneration may also be represented in whole or in part by profit sharing or by the attribution of the rights to subscribe shares of the future issue at a predetermined price.

The remuneration of directors vested with special appointments (for example, chairman or managing directors) in compliance with the by-laws is decided by the board of directors, after having heard the board of statutory auditors.

As regards listed companies, the Code provides that the remuneration of directors and key management personnel shall be established in a sufficient amount to attract, retain and motivate people with the professional skills necessary to successfully manage the listed company, as well as that shall be defined in such a way as to align their interests with pursuing the priority objective of the creation of value for the shareholders in a medium to long-term time frame.

With regard to directors with managerial powers or performing functions related to business management, as well as with regard to key management personnel, a significant part of the remuneration shall be linked to achieving specific performance objectives, possibly including non-economic objectives, identified in advance and determined in line with the guidelines contained in the general policy. The remuneration of non-executive directors shall be proportional to the

Update and trends

In the past year the corporate governance of Italian listed companies has continued to undergo significant changes as a result of legislative innovations and market pressure. Data on control model and ownership structure of listed banks shows a reduction of the average weight of major shareholders and a rising presence of foreign institutional investors. Over the past few years, gender diversity in listed companies has been steadily advancing, with a larger role also in listed banks.

A recent issue is represented by the management of cybersecurity threats. Cyber criminals are growing increasingly sophisticated in their attacks. Internal auditors rank this issue among their top three challenges, and more than 80 per cent of senior executives, in recent studies, said cybersecurity is also a boardroom concern.

commitment required from each of them, also taking into account their possible participation in one or more committees.

29 Remuneration of senior management

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

The minimum amount of the managers' remuneration is determined by the applicable national collective bargaining agreement.

30 D&O liability insurance

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

There are no provisions of law on this point. However, it is common practice for a company to take out liability insurance coverage in order to limit the personal liability of directors and managers.

31 Indemnification of directors and officers

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

Under the ICC, in SpAs, the company can waive the exercise of its rights or of actions for liability against directors and settle them, provided that such waiver and settlement are approved by an express resolution of the shareholders' meeting and provided that there is not an opposing vote of the minority of the shareholders' representing at least one-fifth of the company's capital, or one-twentieth in companies having recourse to the risk capital market or the lower percentage provided by the by-laws. Shareholders who have started the action may also abandon it or settle it. Any compensation for the waiver or settlement must be for the benefit of the company.

In companies adopting the two-tier system, the supervisory board may waive or settle a liability action against the management board's members provided that such decisions are approved by the absolute majority of shareholders and that shareholders representing the abovementioned percentages do not oppose it.

In Srls, liability actions against directors may be the object of a waiver or a settlement by the company provided that the majority of the quotaholders representing at least two-thirds of the capital vote in favour and that quotaholders representing one-tenth of the capital do not oppose them.

32 Exculpation of directors and officers

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

Under article 2393, paragraph 6, of the ICC, SpAs may waive liability actions against the directors and settle the legal proceeding provided that the waiver and the settlement have been resolved by the shareholders' meeting and the waiver has not been opposed by shareholders who represent at least one-fifth of the share capital (one-twentieth for listed companies). There is also the possibility for shareholders (representing at least one-fifth of the share capital) to waive or settle the liability action promoted autonomously against directors (according to article 2393-bis, paragraph 6, of the ICC).

Srls may waive the liability action against the directors provided that the decision has been approved by quotaholders representing at least two-thirds of the share capital and the decision has not been opposed by quotaholders representing at least one-tenth of the share capital.

However, the abovementioned waivers are valid only regarding the company and the shareholders or quotaholders concerned without prejudice to third parties' rights (for example, the company's creditors).

In addition, it is common in practice that the shareholders' meeting grants the board members and executives a discharge for liability relating to the content of the financial accounts and grants the former board members and former executives a discharge for liability relating to their work.

33 Employees

What role do employees play in corporate governance?

There are no rules or provisions on an employee's role in corporate governance.

34 Board and director evaluations

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

There are no specific provisions or practices that require evaluation of the board, its committees or directors.

Disclosure and transparency

35 Corporate charter and by-laws

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

The deed of incorporation and the by-laws must be filed at the registry of enterprises. These documents are available to anyone at the registry of enterprises' office where the company has its registered office.

36 Company information

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

Listed companies and the persons that control them shall make the following available to the public and to Consob, without delay:

- any inside information of a precise nature relating to its financial instruments and that, if made public, would be likely to have a significant effect on the prices of those financial instruments and directly concerns the company and their subsidiaries;
- information on compensation plans based on financial instruments in favour of members of the board of directors or the management board, employees and collaborators not linked to the company by an employment contract and of members of the board of directors or the management board, employees and collaborators of parent companies or subsidiaries;
- information regarding major holdings that exceed the percentage provided by Consob; and
- information regarding shareholders' agreements.

Listed companies shall also publish the following information in the yearly corporate governance report:

- the capital structure;
- any restriction on the transfer of securities;
- significant direct and indirect holdings;
- if known, the holders of any securities with special control rights and a description of such rights;

- the mechanism for the exercise of voting rights in any employee share scheme where voting rights are not exercised directly by the employees;
- any restrictions on voting rights;
- shareholders' agreements;
- any significant agreement to which the company is party and which take effect, alter or terminate upon a change of control of the company, and the effects thereof;
- agreements between companies and directors, members of the control body or supervisory board that envisage indemnities in the event of resignation or dismissal without just cause, or if their employment contract should terminate as the result of a takeover bid;
- rules applying to the appointment and replacement of directors and members of the control body or supervisory board, and to amendments to the by-laws;
- the existence of delegated powers regarding share capital increases or powers of the directors or members of the control body to issue security-related financial instruments or to authorise the purchase of own shares;
- adoption of a corporate governance code of conduct issued by regulated stock exchange companies or trade associations, giving reasons for any decision not to adopt one or more provisions, together with the corporate governance practices actually applied by the company over and above any legal or regulatory obligations;
- the main characteristics of existing risk management and internal audit systems used in relation to the financial reporting process;
- the operating mechanisms of the shareholders' meeting, its main powers, shareholders' rights and their terms of exercise, if different from those envisaged by legal and regulatory provisions applicable as supplementary measures; and
- the composition and duties of the management and control bodies and their committees.

Hot topics

37 Say-on-pay

Do shareholders have an advisory or other vote regarding executive remuneration? How frequently may they vote?

See question 28.

38 Shareholder-nominated directors

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

Yes. However, if the proxy solicitation is promoted in listed companies under article 136 of Consob Regulation No. 11971/1199, its expenses shall be borne by the subject promoting such solicitation.

39 Shareholder engagement

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

Shareholders and quotaholders may be appointed as company directors (according to article 2380-bis and article 2475, paragraph 1, of the ICC respectively). As a consequence, these directors may be granted executive powers in order to perform specific activities.

In addition, note that it is forbidden (according to article 2342, paragraph 5, of the ICC) for shareholders to make contributions consisting of services and works while (under article 2464, paragraph 6, of the ICC) the quotaholders may undertake the obligation to perform works or services as contributions and for the company's benefit, provided that they take out an insurance policy or a bank guarantee by which the obligations undertaken are guaranteed.

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Sources of corporate governance rules and practices

1 Primary sources of law, regulation and practice

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

The Companies Act, its subordinate rules and rules of stock exchanges govern issues relating to incorporation, organisation, operation and administration of corporations. In addition, the Financial Instruments and Exchange Act and rules of stock exchanges regulate disclosure of information by listed corporations. Further, the Japan Corporate Auditors Association has published a Code of Kansayaku Auditing Standards as standards for corporate auditors in the conventional 'corporate auditor-type' governance structure. The Corporate Governance Code published jointly by the Financial Supervisory Agency and the Tokyo Stock Exchange became effective from 1 June 2015 through amendment of the rules of the stock exchanges. Most of the rules of stock exchanges are mandatory rules but the provisions in the rules relating to the Corporate Governance Code apply on a 'comply or explain' basis.

2 Responsible entities

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

There are no specific government agencies or other bodies responsible for enforcing the statutes except for the courts. Commentaries authored by officials of the Department of Justice are sometimes relied upon, however. The rules of stock exchanges are enforced by the exchanges through a listing agreement between the exchange and the listed company. There are no well-known shareholder rights protection groups whose views are considered.

The rights and equitable treatment of shareholders

3 Shareholder powers

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

Directors of a stock corporation are elected at the general meeting of shareholders by a simple majority of votes (where shareholders hold at least a majority (or lesser number set forth in its articles of incorporation but at least one-third) of voting rights present) unless otherwise provided for in its articles of incorporation. A director of a stock corporation can be removed at the general meeting of shareholders by a simple majority of votes unless also otherwise provided for. Shareholders of a stock corporation do not have the direct power to decide the course of action of the corporation except for certain material actions, such as mergers and corporate splits. They can do so only through the appointment of directors and proposals at general meetings of shareholders. A stock corporation can issue special shares that have voting rights only in respect of items specified in the articles of incorporation. Thus shareholders with limited voting rights cannot appoint or remove directors if the items listed in the articles of incorporation do not include such an appointment or removal. Further, the articles of incorporation can specify items that require the approval of a meeting of holders of a specific type of shares. Therefore if the articles of incorporation provide that the appointment or removal of directors requires the approval of a specific type of shareholder, such shareholders have the right of veto in respect of the appointment or removal of directors.

Non-public stock corporations can issue a class of shares that carries exclusive power to appoint a certain number of directors but this type of share is not permitted for public corporations.

4 Shareholder decisions

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

The scope of decisions reserved to the shareholders differs depending on the type of governance structure adopted by corporations. The following shows the scope for corporations that have adopted the corporate auditor-type governance structure:

- appointment and dismissal of directors, statutory accounting advisers, corporate auditors (corporate auditors do not exist in corporations that adopted the committee-type governance structure) and accounting auditors;
- payment of dividends and disposition of loss (with certain exceptions);
- payment of dividends in kind;
- determination of remuneration for directors, statutory accounting advisers and corporate auditors;
- discharge of liabilities of directors, statutory accounting advisers, corporate auditors, executive officers and accounting auditors (unless the articles of incorporation give such authority to the board of directors);
- amendment of the articles of incorporation;
- issuance of shares at specially favourable prices;
- issuance of stock options at specially favourable prices;
- change of types of corporations;
- mergers;
- corporate splits;
- statutory share transfers (a procedure to create a wholly owning parent above an existing corporation by operation of law);
- statutory share exchanges (a procedure under which one corporation becomes a wholly owned subsidiary of another corporation by operation of law);
- transfers of all or a material part of its business;
- leases of all the business;
- entrustment of all the business to another party;
- agreements to share all the profit with another party;
- acceptance of the entire business of another corporation;
- acquisition of material assets within two years of its incorporation;
- authorisations to purchase its own shares for counter value with certain exceptions;

- acquisition of special shares that are specified as shares that may be acquired by the issuing corporation in its entirety by a resolution of shareholders;
- consolidation of shares;
- capital reductions;
- reductions of legal reserves; and
- dissolution of the corporation.

While there is no requirement for a non-binding shareholder vote, the management of companies sometimes obtain shareholders' resolutions as support for their actions.

5 Disproportionate voting rights

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

Under the Companies Act, a stock corporation may adopt the unit system for its shares where one voting right is granted to one unit of shares. For example, if a corporation's articles of incorporation provide that 1,000 shares of common stock constitute one unit, a shareholder that owns 2,000 common shares has two votes for his or her shares. The number of shares constituting one unit for one class of shares can be different from that for another class of shares. So, if the corporation sets different numbers for different classes of shares, it can effectively give disproportionate voting rights. In addition, a corporation can issue shares with limited voting rights (namely, shares that do not have voting rights in respect of the items specified in the articles of incorporation of the corporation). Lastly, the articles of incorporation of the company may provide that certain matters that are subject to approval of a general meeting of shareholders or approval of the board of directors also require approval of the meeting of a certain class of shareholders.

6 Shareholders' meetings and voting

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

In order to attend and vote at a general meeting of shareholders, a shareholder must have his or her name registered in the register of shareholders of the corporation. Once his or her name is registered, it will remain on the register until the shareholder transfers the relevant shares to a third party and such transfer is logged in the register. A shareholder may delegate authority to another person to act as a proxy. However, under their articles of incorporation many corporations require that such other person also be a shareholder. A shareholders' resolution can be passed if all the shareholders agree in writing. As such written resolution requires unanimous agreement, practically speaking a listed corporation cannot pass a written resolution. A stock corporation can designate more than one place to have a shareholders' meeting, but audio and visual connection must be established in all places.

7 Shareholders and the board

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

A shareholder that has been holding 3 per cent or more of the entire voting rights for the previous six months has the right to require that directors of the corporation convene a general meeting of shareholders (the scope of qualified shareholders can be expanded by the articles of incorporation). If directors fail to convene a general meeting of shareholders without delay, the requesting shareholder may convene a meeting after obtaining the approval of the court. A shareholder who has been holding 1 per cent or more of the entire voting rights, or 300 or more voting rights for the previous six months, has the right to require the corporation to include its proposals (including a list of director candidates) in the agenda of the general meeting of shareholders by sending written notice to that effect to the corporation eight weeks prior to the date of the meeting (the scope of qualified shareholders can be expanded by the articles of incorporation). Shareholders do not have the right to require the board to circulate their dissenting statements.

8 Controlling shareholders' duties

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

There are no specific provisions in the Companies Act or established court precedents that establish the duties of controlling shareholders. However, a resolution of a general meeting of shareholders can be nullified through a resolution nullification suit if the resolution is unduly tainted as a result of the exercise of voting rights by one or more shareholders having special interest in the resolution. A resolution nullification suit must be filed with the court within three months of the date of the relevant shareholders' meeting.

9 Shareholder responsibility

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

Theoretically speaking, a shareholder could be held responsible for the acts or omissions of the company if a director representing the company commits a tort when he or she is an employee of the shareholder and acts under control of that shareholder, or a director representing the company and the relevant shareholder jointly commit a tort. However, a shareholder will not be held responsible solely for the exercise of (or failure to exercise) his or her voting rights even if the voting is a decisive factor in the general meeting of shareholders.

Corporate control

10 Anti-takeover devices

Are anti-takeover devices permitted?

Many listed Japanese corporations have adopted various types of anti-takeover devices recently. Most of them are structured to enable the board of directors to issue stock acquisition rights that cannot be exercised by a hostile acquirer. The validity of these devices has, however, not been fully tested by the courts.

11 Issuance of new shares

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

In the case of listed corporations, as long as the issue price is nearly equal to the market price, the board can issue new shares without shareholder approval under the Companies Act. However, the rules of the Tokyo Stock Exchange require:

- an independent party opinion confirming necessity and appropriateness of the issuance; or
- shareholder approval if:
- the number of the new shares is 25 per cent or more of the outstanding shares; or
- the issuance results in a change of controlling shareholder.

12 Restrictions on the transfer of fully paid shares

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

No share transfer restrictions enforceable by the corporation itself are allowed in the case of listed corporations. Agreements among large shareholders sometimes contain this type of provision. In the case of non-listed corporations, the Companies Act allows a corporation to have a provision in its articles of incorporation where the transfer of shares requires approval of the board of directors. If a shareholder of such a corporation wishes to sell his or her shares, but the board of directors does not approve such a transfer, the shareholder may require the board of directors to appoint a purchaser who is acceptable to them.

If a listed corporation amends its articles of incorporation to include such a provision, its shares are delisted in accordance with stock exchange listing rules.

13 Compulsory repurchase rules

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

A corporation may not directly force its shareholders to sell their shares to it unless such a compulsory repurchase is specifically provided for in its articles of incorporation as a characteristic of the relevant shares. But a corporation can effectively force its shareholders to sell their shares through attaching such repurchase provision by the resolution of a shareholders' meeting in which a large shareholder has a controlling stake. Further, a shareholder holding 90 per cent or more may force the other shareholders to sell their shares to itself under the special provisions in the Companies Act.

14 Dissenters' rights

Do shareholders have appraisal rights?

Yes. Shareholders have appraisal rights in cases of mergers, corporate splits, statutory share exchange, statutory share transfer and certain changes of the terms of shares.

The responsibilities of the board (supervisory)

15 Board structure

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

The conventional Japanese governance structure is one-tier. The board of directors consists of all the directors of the corporation including directors who can represent the company (namely, representative directors). In addition, a listed corporation has a board of corporate auditors consisting of at least three corporate auditors (in the case of a corporation with a stated capital of ¥500 million or more or with total debts of ¥20 billion) or at least one corporate auditor (in the case of other corporations) whose duty, in both cases, is to audit the directors' conduct. The Companies Act also allows two types of two-tier governance structures. One is a committee-type structure consisting of the board of directors (appointed by the shareholders), its three committees (audit, nomination and compensation) and executive officers appointed by the board. The other is an audit committee-type structure consisting of the board of directors and an audit committee. Members of the audit committee are directors separately elected as such at the shareholders' meeting.

16 Board's legal responsibilities

What are the board's primary legal responsibilities?

In the case of corporations that have adopted the conventional corporate auditor-type governance structure, the board of directors determines all management matters unless they are specifically reserved for a general meeting of shareholders under the Companies Act (such as a merger) or they are delegated by the board to a representative director (a director with power to represent and bind the corporation, who is also a member of the board). The Companies Act specifically requires a board resolution if a corporation wishes to conduct any material actions including, but not limited to, the following actions:

- disposition or acceptance of important assets;
- borrowing of substantial amounts of money;
- appointment and dismissal of managers and other important employees;
- establishment, change and abolition of branches and material organisations;
- determination of material items relating to issuance of bonds;
- determination of a corporate governance system; and
- discharge of liabilities of directors, statutory accounting advisers, corporate auditors, statutory executive officers and accounting auditors authorised by the articles of incorporation.

The board may not delegate these items to a director. In the case of corporations that adopt the committee-type governance structure, the board may, and normally does, commission most of the powers to executive officers appointed and supervised by the board. In the case of corporations that adopt the audit committee-type governance structure, the board may delegate most of the decision-making powers to individual directors if the majority of its directors are outside directors or the articles of incorporation contains provisions to allow such delegation.

17 Board obligees

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

The board of directors is the decision-making body of a corporation. Each director owes fiduciary duties to the corporation. Therefore, he or she may not act for the benefit of a major shareholder if such an action is against the interests of the shareholders as a whole. Further, directors are required by the Companies Act to exercise the duty of care of a prudent manager in performing their duties.

18 Enforcement action against directors

Can an enforcement action against directors be brought by, or on behalf of, those to whom duties are owed?

A corporate auditor (a person elected at the general meeting of shareholders) of a corporation that adopted the conventional corporate auditor-type governance structure may apply to the court seeking injunctive relief if the conduct of a director goes beyond the objectives of the corporation or violates the law or the articles of incorporation, or such conduct is threatening and such conduct would cause material damage to the corporation. Members of the audit committee of a corporation that adopted the committee-type governance structure and members of the audit committee of a corporation that adopted the audit committee-type governance structure also have the same power. A shareholder who has held shares in the corporation for the preceding six-month period may also apply for injunctive relief if there is a possibility that such conduct by a director would cause 'substantially material' damage to the corporation.

19 Care and prudence

Do the board's duties include a care or prudence element?

Each director owes fiduciary duties to the corporation. A director is also required to exercise the duty of care of a prudent manager in performing his or her duties. A director may not engage in business that competes with the business of the corporation unless that director first obtains the board's approval. Further, a director may not enter into a transaction with the corporation unless he or she first obtains board approval. Even if a director obtains board approval in connection with a transaction with the corporation, he or she is still liable for any damages incurred by the corporation as the result of such a transaction.

20 Board member duties

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

As a general rule, the duties of individual members of the board do not differ from each other irrespective of the difference of skills or experience. In the case of a corporation that has adopted a conventional corporate auditor-type governance structure, however, there is no separation of the functions of directors and those of officers in charge of the day-to-day management of the corporation. So, in most corporations, each director also serves as an officer in charge of a specific aspect of management of the corporation. In this sense, the duties of individual members of the board may differ. In the case of a corporation that has adopted a committee-type governance structure, the members of each committee perform additional duties. The same applies to members of the audit committee in a corporation that has adopted the audit committee-type governance structure.

21 Delegation of board responsibilities

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

In the case of a corporation that adopted the conventional corporate auditor-type governance structure, in principle, the board acts as a management body as well as a supervising body. But the board may delegate its responsibilities to each director except for material matters regarding the business of the corporation (including but not limited to those specifically identified in the Companies Act) and the following matters:
- disposition or acceptance of important assets;
- borrowing of a substantial amount of money;
- appointment and dismissal of managers and other important employees;
- establishment, change and abolition of branches and material organisations;
- determination of material items relating to the issuance of bonds;
- determination of corporate governance system; and
- discharge of liabilities of directors, statutory accounting advisers, corporate auditors, statutory executive officers and accounting auditors authorised by the articles of incorporations.

In the case of a corporation that adopted the committee-type governance structure, the board is expected to act mainly as supervising body and can delegate management decisions to statutory executive officers except for the limited number of items specified in the Companies Act. The board is also required to determine the following items:
- management policy;
- items necessary for operation of the audit committee;
- allocation of duties among statutory executive officers and matters relating to relationship among plural statutory executive officers;
- identification of the director to whom statutory executive officers should request convocation of a meeting of the board of directors; and
- determination of framework to assure appropriate management of the corporation.

In the case of a corporation that adopted the audit committee-type governance structure, the board can delegate management decisions to individual directors except for the limited number of items specified in the Companies Act if the majority of its directors are outside directors or the articles of incorporation contain provisions to allow such delegation. The board is also required to determine the following items: management policy; items necessary for operation of the audit committee; and determination of a framework to assure appropriate management of the corporation.

22 Non-executive and independent directors

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

If a listed corporation, which has adopted the conventional corporate auditor-type governance structure, does not have an outside director, it must explain, at the annual general meeting of shareholders, why it is appropriate not to have an outside director. In other words, the Companies Act strongly recommends that listed corporations have at least one outside director. An 'outside director' is defined as a director who:
- is not an executive director, statutory executive officer, manager or other employee of the corporation or any of its subsidiaries;
- has not served as executive director, statutory executive director, manager or other employee of the corporation or any of its subsidiaries for the last 10-year period immediately preceding the appointment as a director;
- is not a director, statutory executive officer, manager or other employee of its parent corporation;
- is not an executive director, statutory executive officer, manager or other employee of any of the subsidiaries of its parent corporation; and
- is not a related to any of the directors, statutory executive officers, mangers or other important employees of the corporation.

There are some additional rules relating to qualification of 'outside' directors. In the case of a corporation that has adopted the committee-type governance structure, it has to establish three committees (audit, nomination and compensation committees) and appoint one or more executive officers. Each committee must consist of at least three directors (a majority of whom must be outside directors). None of the members of the audit committee may hold the position of statutory executive officer, executive director, manager or employee of the corporation or any of its subsidiaries or statutory accounting adviser of any of the subsidiaries. In the case of a corporation that adopted the audit committee-type governance structure, it has to establish an audit committee. The audit committee must consist of at least three directors (a majority of whom must be outside directors). Each member of the audit committee of this type of corporation is a director elected as such member at the general meeting of shareholders. None of the members of the audit committee of this type of corporation may hold the position of executive director, manager or other employee of the corporation, or the position of statutory accounting adviser or statutory executive officer of any of the subsidiaries of the corporation. Legally, the responsibility of the outside directors is the same as that of those not classified as outside directors, provided, however, that a corporation can adopt articles of incorporation authorising the corporation to enter into an agreement with each of the outside directors and non-executive directors to limit the maximum amount of monetary liability of such directors. Stock exchange rules require a listed corporation to have at least two independent officers. An 'independent officer' is defined as an outside director or corporate auditor whose interest will not conflict with that of general shareholders.

23 Board size and composition

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

It is not possible for the following to be a director:
- a legal entity;
- a person subject to guardianship or curatorship;
- a person who was previously subject to any criminal sanction under the Companies Law or other certain types of laws if two years have not passed since the end of the criminal sanction or the probation period; or
- a person who was subject to imprisonment under the laws other than those covered by the item above if that period of imprisonment or probation has not ended.

If a corporation intends to have a board structure, it must have at least three directors based on the provisions in the Companies Act. Further, the articles of incorporation of most corporations have provisions regarding the minimum or maximum number of directors. The size of the board is determined by a shareholders' resolution through their power to appoint and remove directors in accordance with such restrictions. Board vacancies must be filled by the appointment of new directors through a resolution of the shareholders' meeting. A shareholders' meeting can appoint a candidate for such substitute director in advance. If there is such substitute director, then such substitute director becomes a director once an existing director resigns or dies.

Update and trends

After the introduction of the Japanese Corporate Governance Code in 2015 (the Code), listed companies in Japan have been very sensitive about the impression given by their corporate governance structures and the relevant disclosure to the market. While significant change has yet to come, the Code is slowly impacting listed companies' attitude towards the market and shareholders.

24 Board leadership

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

The Companies Act does not require the separation of the functions of board chairman and CEO or president. In a corporation that has adopted the corporate auditor-type governance structure or audit committee-type governance structure, the board of directors appoints one or more representative directors from among themselves. A representative director represents and may legally bind the corporation. Customarily, one of the representative directors is the president and another is the chairman. If there is a chairman, he or she customarily serves as chairman at board meetings. If there is no chairman, the president customarily serves as chairman at such meetings. The position of chairman at meetings is customarily provided for in the articles of incorporation or the regulations of the board of directors of the corporation. In a corporation that adopted the committee-type governance structure, the board appoints statutory executive officers, who run the day-to-day business of the corporation, and the representative statutory executive officer or officers, who represent the corporation and can legally bind it. Statutory executive officers may be elected from among the directors. One of the representative statutory executive officers customarily uses the title of CEO.

25 Board committees

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

In the case of a corporation that has adopted the corporate auditor-type governance structure, board committees are not mandatory. Although the corporation may have internal board committees, they are not legally recognised bodies under the Companies Act. In the case of a corporation that has adopted the committee-type governance structure, the corporation has to set up the nomination, audit and compensation committees and appoint one or more executive officers. Each committee has to consist of at least three directors (a majority of whom must be external directors not also serving as executive officers). None of the members of the audit committee may be a statutory executive officer, executive director, manager or employee of the corporation or any of its subsidiaries or statutory accounting adviser of any of the subsidiaries. The nomination committee has the power to determine proposals to be submitted to the general meeting of shareholders as to the appointment and removal of directors. The audit committee has the power to audit the performance of directors and statutory executive officers and to determine proposals to be submitted to the general meeting of shareholders as to appointment, removal or non-renewal of outside accounting auditors. The compensation committee has the power to determine the compensation payable to directors, statutory executive officers and statutory accounting advisers. In the case of a corporation that has adopted the audit committee-type governance structure, it has to establish an audit committee. The audit committee must consist of at least three directors (a majority of whom must be outside directors). Each member of the audit committee of this type of corporation is a director elected as such member at the general meeting of shareholders. None of the members of the audit committee of this type of corporation may hold the position of executive director, manager or other employee of the corporation or the position of statutory accounting adviser or statutory executive officer of any of the subsidiaries of the corporation.

26 Board meetings

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

The Companies Act requires that each representative director and each executive director of a corporation that adopted the corporate auditor-type governance structure or the audit committee-type governance structure reports on how he or she has been carrying out the business to the board of directors at least once every three months. Therefore, the meeting of the board of directors must be held at least once every three months. In the case of a corporation that has adopted the committee-type governance structure, similar obligations are imposed on executive officers. Therefore, the meeting of the board of directors must be held at least once every three months.

27 Board practices

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

The governance structure of the corporation is registered in the commercial register. The corporation's commercial register is a public record. If it is necessary for a shareholder of a corporation or a shareholder of the parent of a corporation to exercise his or her rights, he or she can access and make copies of the minutes of the board meetings after obtaining court permission. A creditor of a corporation can also apply for court permission if such access is necessary to claim compensation for damages incurred against a director, statutory accounting adviser, corporate auditor or statutory executive officer of the corporation.

28 Remuneration of directors

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

In a corporation that has adopted the corporate auditor-type governance structure, the remuneration of directors must be approved at a general meeting of shareholders unless there are relevant provisions in its articles of incorporation. Most stock corporations approve the maximum aggregate amount of remuneration payable to the entire group of directors and give the board of directors the power to decide how it is allocated among the directors. The board of directors generally delegates such power to the president and representative director. In a corporation that has adopted the audit committee-type governance structure, the remuneration of directors who are to serve as members of the audit committee must be approved at a general meeting of shareholders separately from that payable to directors who are not to serve as members of the audit committee. The directors who are also members of the audit committee have the right to express their opinion on the remuneration payable to audit committee members at the general meeting of shareholders. The audit committee member director elected by the audit committee may express opinion on the remuneration payable to directors who are not audit committee members. In a corporation that has adopted the committee-type governance structure, the remuneration of the directors must be approved by the compensation committee.

In a corporate auditor-type governance corporation, the length of directors' service shall be two years or less. In an audit committee-type governance corporation, it shall be two years for audit committee member directors while it shall be one year or less for other directors. It shall be one year in a committee-type governance corporation. Even if the service contract provides for a longer term, such provision will not limit the power of the general meeting of shareholders to replace the directors upon expiry of the two-year period. For the corporation to advance a loan to its director or to enter into a transaction with its director, the relevant director is required to obtain a board resolution in respect of such a loan or transaction.

29 Remuneration of senior management

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

No law, regulation, listing requirement or practice exists that affects the remuneration of directors. Loans to directors and other transactions between the company and directors must be approved by the board of directors (or general meeting of shareholders if the company has not adopted a board system). Board approval is also required for loans to, and transactions with, statutory executive officers in cases where corporations have adopted a committee-type governance system.

30 D&O liability insurance

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

D&O insurance is permitted and has recently become common practice. The company can pay the premiums.

31 Indemnification of directors and officers

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

There is no explicit provision prohibiting the company from indemnifying directors in respect of liabilities incurred against a third party in their capacity as directors. But such indemnities are not common. If the articles of incorporation of the company contain a specific provision, the board may discharge a certain portion of the directors' liabilities against the company itself, which exceeds the amount calculated based upon the formula specified in the Companies Act. The corporation can enter into a contract with its outside directors or non-executive directors, limiting their liabilities against the company to a certain amount if it is so authorised in its articles of incorporation.

32 Exculpation of directors and officers

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

A two-thirds vote at the shareholder meeting can limit the liability of directors and officers to certain statutorily calculated amounts (except in the case of certain types of liability) unless the relevant damages incurred by the company are caused by gross negligence of the relevant director or officer. This power can be delegated to the board of directors by amending the articles of incorporation of the company. Liabilities of outside directors, non-executive directors and auditors can be limited by a liability-limiting agreement if the articles of incorporation contain a provision permitting such an agreement.

33 Employees

What role do employees play in corporate governance?

Legally, employees do not play any role in corporate governance in Japan. As a minimum matter of course, in many instances, the management of a corporation consults the union or the representative of employees when they wish to conduct major corporate restructuring.

34 Board and director evaluations

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

Under the Corporate Governance Code, which is enforced only on a 'comply or explain' basis, the board of directors is required to analyse and valuate effectivity of the board management every year and disclose the outline of the result of such analysis and valuation to the public.

Disclosure and transparency

35 Corporate charter and by-laws

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

The articles of incorporation are the only constitutional document of a stock corporation. There are no by-laws or corporate charters. Under the Companies Act, the articles of incorporation are only available to shareholders and creditors. In the case of a listed corporation, its articles of incorporation are publicly available at the head office and major branches of the corporation and the office of the relevant stock exchange, because the articles of incorporation are one of the attachments to a securities registration statement and annual securities report, which a listed corporation must file every year.

36 Company information

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

A listed corporation is required to file an annual securities report setting forth the business results of the corporation with the appropriate local finance bureau within three months of the end of its fiscal year via the electronic corporate disclosure system, EDINET. It must also file a quarterly report within three months of the end of each quarter. Such reports are available to the public via EDINET. Further, stock exchange rules require timely disclosure by listed corporations of major events or decisions of the listed corporation.

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Hot topics

37 Say-on-pay

Do shareholders have an advisory or other vote regarding executive remuneration? How frequently may they vote?

In the case of the corporate auditor-type governance structure, a resolution of the general meeting of shareholders is required for a Japanese listed corporation to pay remuneration to its directors or corporate auditors unless it is already provided for in its articles of incorporation. Once the maximum amount of the aggregate amount of remuneration payable to directors and to corporate auditors are so approved, no further resolution is required unless such maximum amount needs to be amended. In the case of the audit committee-type governance structure, such amount payable to audit committee member directors and to other directors must be separately determined. In the case of the committee-type governance structure, remuneration of the directors and executive officers is determined by the remuneration committee. So, in this case, shareholders do not have any direct power to determine the remuneration of directors and executive officers.

38 Shareholder-nominated directors

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

A shareholder or a group of shareholders who have held 1 per cent or more of the outstanding voting rights for the previous six months can ask the directors to present a proposed agenda, including appointment of directors to the general meeting of shareholders, by giving eight weeks' notice.

39 Shareholder engagement

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

In Japan, listed companies' engagement with their shareholders is relatively limited. But when there is a proposed resolution that is not very popular among the shareholders, the company sometimes contacts shareholders to urge them to cast positive votes at its shareholders' meeting. Such actions are often conducted by persons within its general affairs bureau under the supervision of directors.

Lebanon

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Sources of corporate governance rules and practices

1 Primary sources of law, regulation and practice

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

The primary source of law, regulation and practice relating to corporate governance in Lebanon is the Lebanese Code of Commerce (LCC) issued on 24 December 1942 by virtue of Law Decree No. 304 (amended by several subsequent laws and law-decrees). Other sources of law are as follows.

Banking laws and regulations

- The Code of Money and Credit (CMC) executed by Decree No. 13,513 and issued on 1 August 1963 (amended by several subsequent laws and decrees). The main issues relate to approval by the general assembly of letter of credits granted to board members (article 152) and the possibility for a shareholder or group of shareholders owning 10 per cent of the shareholding of the company or the financial institution to file before the competent courts an opposition to the decision of appointment of an auditor by the general assembly.
- Decision of the Central Bank of Lebanon (BDL) No. 7,737 of 15 December 2000, as amended by Intermediary Decision No. 10,707 of 21 April 2011 and Intermediary Decision No. 11,322 of 12 January 2013, concerning internal control and internal audit in banks and financial institutions. This decision provides, inter alia, that the bank's senior management (as defined in the BDL's decisions) must establish, and update as required, a framework for the bank's internal control that should be adequate, taking into account the size of the bank or financial institution, the nature of the risks that the bank or the financial institution encounters or may encounter; the decision also sets the minimum requirements for which such framework must cater. It also provides that all banks and financial institutions must have an internal audit unit and it sets the requirements to be fulfilled by such unit, that it should be entirely independent from the operations side of the business, that it should not have any executive responsibilities at the bank or financial institution, and that it should be objective in the undertaking of its tasks. The unit's president is appointed by the board, and the bank or financial institution must inform the Banking Control Commission of his or her name, of any change and the reasons for the change, and provide the Banking Control Commission with his or her CV. The tasks of this unit include an evaluation of the efficiency of the rules of corporate governance and of the policies and procedures that complete it, at all levels of the bank, and of the compliance of all units, departments and branches therewith, and, by virtue of the last amendments brought to this decision, the verification of the effectiveness of the process and procedures of compliance with the laws and regulations that are followed by the Compliance Department.

  The unit must also, inter alia, prepare an internal audit charter that guarantees its independence and sets its prerogatives, undertake an audit of the bank's or financial institution's activities and operations within specific audit cycles, and prepare and execute annual audit plans.
- BDL Decision No. 9,382 of 26 July 2006, as amended by Intermediary Decision No. 10,708 of 21 April 2011, concerning corporate governance in banks. This decision provides that all banks operating in Lebanon must:
  - work hard to comply with the principles that were and will be issued by the Basel Committee, relating to enhancing corporate governance in banks;
  - prepare their own Code of Corporate Governance that must include at a minimum the information determined in the said decision;
  - publish a summary of such a Code on their website and in their annual report; and
  - provide the Banking Control Commission with a soft and a hard copy of such Code and of any amendments thereto.
- BDL Decision No. 9,725 of 27 September 2007, concerning corporate governance in Islamic banks. According to this decision, Islamic banks must deploy a framework and internal regulations relating to corporate governance, according to the rules that are internationally recognised and that do not contravene applicable Lebanese laws and regulations, notably the aforementioned BDL Decision No. 9,382 of 26 July 2006 on corporate governance in banks. By virtue of this decision, each Islamic bank must establish a special unit called a 'corporate governance unit' that is independent from the bank's operational management and has no executive power, with the purpose of overseeing the implementation and development of internal rules on corporate governance. This unit shall include at least:
  - one or more members from the bank's board who do not have executive functions;
  - one or more members of the shariah consultative body established at the Islamic bank, according to article 9 of Law 575 of 11 February 2004;
  - the chief of the internal audit unit; and
  - the chief of the shariah auditing unit, created by virtue of article 9 of the decision.

  Islamic banks must also abide by specific disclosure requirements enumerated in a form attached to the decision. By virtue of the decision, Islamic banks must adopt a sound investment strategy.

  Also, the general management of the Islamic bank is responsible for verifying that the bank is operating in accordance with the provisions and principles of Islamic law (shariah). Consequently, the shariah consultative body is only responsible for delivering independent opinions about compliance with shariah law.

  As mentioned before, by virtue of article 9 of the decision, Islamic banks must create an independent administrative unit called a shariah auditing unit, the function of which is to verify, evaluate and monitor the compliance of its banking operations with the opinions of the shariah consultative body.
- BDL Decision No. 9,956 of 21 July 2008, as amended by Intermediary Decision No. 10,706 of 21 April 2011 and Intermediary Decision No. 12,114 of 26 October 2015, relating to the boards of directors of Lebanese banks and the committees deriving therefrom, wherein the definitions of non-executive board member and independent board member are set out, and whereby it is provided

that for the purpose of enhancing the competence and efficiency of the board of directors, Lebanese banks must elect a sufficient number of independent and non-executive members of the board in order to fulfil the requirements of the said decision, notably regarding the establishment of the committees deriving from the board of directors. This decision also provides that the board must hold at least four meetings per year, at least two of which must be held in Lebanon, and provides for the creation, composition and tasks of the audit committee and risk committee. Moreover, by virtue of its amendment in October 2015, this decision now provides that each of the chairmen and members of the board of directors of banks operating in Lebanon are called to attend the corporate governance programmes that are prepared by the BDL specifically for them, and that the chairman and members of each of the audit committee, risk committee, remuneration committee and the committees that derive from the board of directors are called to attend the specific programmes that are prepared by the BDL in the specialisation field of the committee in which each one of them participates; the BDL sets the dates of all said programmes in coordination with the concerned banks.

- BDL Decision No. 10,224 of 13 August 2009, relating to the procedures of auditors' appointment, which provides that auditors are appointed for a renewable three-year period, provided that the principle of partner rotation is adopted by the audit firm, by changing the partner in charge every five years, and that, starting with fiscal year 2010, each bank operating in Lebanon must appoint two audit firms for auditing its accounts jointly and severally.
- BDL Decision No. 11,323 of 12 January 2013, as amended, relating to the creation of a compliance department, which provides for the composition, functioning, duties and prerogatives of the compliance department. By virtue of this decision, banks and financial institutions that are working in Lebanon must create, within a specific deadline, a compliance department that shall be divided into a legal compliance unit and an AML/CFT compliance unit.
- BDL Decision No. 11,821 of 6 August 2014, relating to the remunerations and bonuses granted to banks' employees, which provides that Lebanese banks should set a written remuneration policy, resolved by the board of directors, including all levels and categories of employees in banks and their branches located outside Lebanon. In addition, the board of directors of any Lebanese bank must establish a remuneration committee from the non-executive board members of the bank and composed of at least three members. The BDL's Central Council may, at its discretion and after taking the opinion of the Banking Control Commission, exempt a specific bank from the creation of such a committee based on the bank's size and the nature of its activities; in such a case, the board of directors shall undertake the activities of such committee as provided in this decision. This decision also provides that the board of directors of any Lebanese bank should set written regulations for evaluating the performance of the employees of various levels in an objective and transparent manner.
- BDL Decision No. 11,947 of 12 February 2015, relating to the principles for undertaking banking and financial operations with clients, which provides that banks and financial institutions operating in Lebanon, in the context of offering all sorts of banking and financial services and products, are required to instruct their clients, bring to their awareness and clarify to them their rights by publishing educational and awareness programmes in their head offices and all their branches and websites and other means of communication with their clients. By virtue of this decision, all banks and financial institutions operating in Lebanon must prepare a list of the rights and obligations of clients containing at least the information mentioned in the attachment to such decision; this list must be prepared in Arabic and in one additional foreign language chosen by the bank or financial institution, and must be placed at the clients' disposal in the head offices and all the branches; a copy of this list must be remitted to each client and the content thereof must be explained to the client by the relevant employee; the client must acknowledge, in writing, the receipt of this list and that its contents have been understood. The decision also provides, inter alia, that all banks and financial institutions operating in Lebanon must prepare a policy regarding the 'principles for undertaking banking and financial operations with clients' that must be approved by the board of directors, and put in place the measures relating thereto; and create a unit for the implementation of this policy, which will be related to the general manager but independent from the execution of operations, and to which the technical and human resources required to undertake its role (which is set out in the decision) must be allocated. Banks and financial institutions operating in Lebanon were granted until 30 September 2015 to comply with the provisions of this decision.

According to the Criminal Code (CC), issued by Law Decree No. 340 on 1 March 1943 (amended by several laws and decrees), board members and auditors are subject to fraudulent bankruptcy if they have published false statements or committed other fraudulent bankruptcy acts (article 692).

Laws and regulations for listed companies

The following laws and regulations are mandatory and must be complied with by all listed companies:

- Law Decree No. 120 of 16 September 1983 (amended by subsequent laws and law-decrees) concerning the organisation of the Beirut Stock Exchange (BSE).
- Decree No. 7,667 of 16 December 1995 (amended by subsequent laws and decree-laws) on the execution of the internal rules of the BSE.
- Article 91 of Decree No. 7,667 specifies several documents and information of concern to shareholders that should be submitted to the BSE. If the listed company fails to submit such documents and information within the specified time limits, it shall be obliged to pay a penalty. The BSE committee's decisions are mainly related to the submission of non-audited statements every three months.

The Capital Markets Authority (CMA) also published on its website on 27 August 2015 the Listing Regulations in English (the Listing Regulations), noting that they have not yet been enacted in the official Arabic version and that the CMA orally confirmed, on several occasions, that these draft regulations are currently being translated into Arabic and that they will be enacted soon. The purpose of the Listing Regulations is to: establish the requirements for an issuer to apply for listing of securities in Lebanon, establish the ongoing requirements to maintain a listing of securities, and set out requirements for maintaining sound standards of corporate governance by listed issuers.

Regarding corporate governance, the Listing Regulations provides under Part F titled 'Corporate Governance' that, subject to specific articles of the Listing Regulations, all listed issuers of equity securities must comply with the corporate governance standards set under Part F of the Listing Regulations; furthermore, a listed issuer must comply with any binding requirements on corporate governance set out in the laws, circulars of the BDL or other regulations that apply to the issuer. However, it is to be noted that a listed issuer may apply to the CMA for a waiver from one or more requirements of Part F of the Listing Regulations by submitting an application in writing to the CMA with details of the reasons for requesting a waiver from each requirement covered by the application.

By way of example of the requirements provided in Part F of the Listing Regulations, a listed issuer's board of directors must establish a written policy on its corporate governance system and practices, certain disclosures must be included in the annual reports of listed issuers and there are various requirements that concern the board of directors (notably regarding its structure, its responsibilities, conflicts of interest and board committees).

In addition there are the by-laws of companies, which may provide for corporate governance issues such as the creation of committees (noting that in the case of banks and Islamic banks, as mentioned above, the creation of certain committees is now mandatory).

There are also court precedents, which have taken into consideration corporate governance concerns not provided for in the laws or regulations such as the right for any shareholder to ask questions of the board concerning an operation mentioned in the agenda of the shareholders' meeting. The courts have decided that the board is required to answer these questions on the date of the meeting.

Capital markets laws and regulations

The following laws must be complied with:

- Law No. 161 of 17 August 2011 regarding Capital Markets (Law 161).
- Decision No. 1 issued by the CMA on 11 June 2013 (Decision 1) regarding the policy of disclosure of information with respect to joint-stock companies and collective investment funds, the shares or parts of which could be potentially listed on the regulated or unregulated capital markets.

  Article 1 of Decision 1 provides that joint-stock companies and collective investment funds working in Lebanon, the shares or parts of which are able to be traded in the regulated or unregulated (OTC) financial markets, and which have more than 20 shareholders or part holders, must put in place a disclosure policy so as to ensure that they follow best corporate governance practice, which allows the protection of the rights of the shareholders, part holders and stakeholders. Furthermore, article 2 of Decision 1 provides inter alia for an obligation to submit to the CMA the contemplated disclosure policy it wishes to adopt at least three months prior to the contemplated date of publication, and in case of any change in the contemplated disclosure policy at least one month prior to the contemplated date of publication. The disclosure policy shall be effectively adopted at the expiry of each of the aforementioned periods and provided the CMA has not, during such period, opposed to the disclosure policy or requested it be amended. Article 2 further provides for an obligation to publish, in a timely manner, all information, as well as any amendments thereto, regarding the companies, the funds, their deeds and financial instruments, and regarding which the public's knowledge could have an impact on the market price of said deeds and instruments.
- Decision No. 2 issued by the CMA on 11 June 2013 (Decision 2) regarding the disclosure requirements of joint-stock companies and the collective investment funds toward their shareholders or part holders.

  Article 1 of Decision 2 provides that joint-stock companies and collective investment funds working in Lebanon, the shares or parts of which are able to be traded in the regulated or unregulated (OTC) financial markets, and which have more than 20 shareholders or part holders, must put at the latter's disposal all the information that will allow them to fully exercise their rights. This information must be specific, true and accurate and shall include at least the information listed in article 1, including information related to the company's share capital and the value of the total of the collective investment scheme's parts, the company's or collective investment scheme's duration, yearly financial results, and so forth. Article 2 of Decision 2 further provides that the company or collective investment scheme must put in place and use the most effective means and processes to disclose the aforementioned information to their shareholders or part holders as well as any change in the said information. They should also inform the CMA of the means and processes that they intend to use, at least three months prior to the date on which they intend to use them and at least one month prior to the date on which they intend to adopt any change thereto. These means and procedures and any changes thereto will be effective respectively at the expiry of each of the aforementioned periods, provided the CMA has not, during such periods, opposed thereto or asked for an amendment thereto.
- Decision No. 4 issued by the CMA on 14 August 2013 (as amended) (Decision 4) concerning the committees, departments and units that should be present in certain joint-stock companies regarding compliance.
- Decision No. 5 issued by the CMA on 14 August 2013 (as amended) (Decision 5) concerning the committees, departments and units that should be present in certain joint-stock companies regarding internal audit.
- Decisions 4 and 5 of the CMA apply to three categories of companies (the relevant companies):
  - joint-stock companies working in Lebanon and the shares of which are traded on organised financial markets;
  - joint-stock companies working in Lebanon and the shares of which are able to be listed in the regulated or unregulated (OTC) market, the shareholders of which exceed 20, and the total earnings of which vary between 30 billion and 100 billion Lebanese pounds; and
  - joint-stock companies working in Lebanon and the shares of which are able to be listed in the regulated or unregulated (OTC) market, the shareholders of which exceed 20, and the total earnings of which exceed 100 billion Lebanese pounds.

  The provisions of these decisions do not apply to banks, financial institutions and financial brokerage institutions operating in Lebanon.
- Article 2 of Decision 4 imposes on the relevant companies the establishment of a compliance department to ensure the implementation of the applicable procedures, laws and regulations, as per the details provided for in article 7 of Decision 4, in order to ensure compliance with the best administrative practices that ensure the protection of the shareholders' and stakeholders' rights.
- Article 2 of Decision 5 imposes on the relevant companies the establishment of a framework of internal control that ensures an independent and objective evaluation of the work of all the departments and units of the company and their activities, with the aim of increasing the effectiveness and the efficiency of control and risk management in order to guarantee the protection of the shareholders' and stakeholders' rights.
- Article 3 of Decision 5 imposes on the relevant companies the establishment of an internal audit department composed of one or more persons depending on the size of the company and the variety and diversification of its activities and operations.

The CMA published on its website Series 3000 dated 4 November 2016 relating to the Business Conduct Regulation in its official Arabic version (along with its English translation) (the 3000 Regulations), which applies to the securities business activities of approved institutions (it does not apply to banking or credit activities regulated by the BDL). Approved institutions are institutions or entities that are licensed by the CMA to carry on securities business in Lebanon under the Licensing and Registration Regulation.

The purpose of the 3000 Regulations is to:

- establish the rules and code of conduct that an approved institution must comply with in carrying out securities business and dealing with clients;
- define the policies, procedures, systems and controls that an approved institution must establish and keep up to date;
- establish the rules on handling of client money and client assets by an approved institution;
- set out the requirements to notify or report certain matters to the CMA; and
- establish the rules and code of conduct that a registered person must comply with in carrying out his or her responsibilities at an approved institution.

Regarding corporate governance, the 3000 Regulations provide under Part C section 3201, titled 'Corporate Governance', that the governing body of an approved institution must: be clearly responsible for setting or approving (or both) the business strategy and objectives of the firm, comprise an adequate number and mix of individuals who have, among them, the relevant knowledge, skills, expertise and time commitment necessary to effectively carry out the duties and functions of the governing body, and have adequate powers and resources to enable it to carry out its duties and functions effectively. Furthermore, this section also provides that the senior management of the approved institution must be clearly responsible for the day-to-day management of the firm's business in accordance with the business strategy and objectives approved by the governing body.

Moreover, the CMA published on its website Series 2000 dated 10 January 2017 relating to the Licensing and Registration Regulation in its official Arabic version (along with its English translation), (the 2000 Regulations) which mainly addresses the licensing requirements for undertaking securities business activities in Lebanon.

The main purpose of the 2000 Regulations is to:

- establish the categories of licences required to carry on securities business in Lebanon;
- identify exclusions from the requirement to obtain a licence;
- establish the categories of registration required to carry out designated functions and activities on behalf of an approved institution;
- set the requirements and conditions for obtaining a licence as an approved institution; and

- establish the procedures that apply to applications, approvals, changes and termination of a licence or registration.

Regarding corporate governance, the 2000 Regulation provides under Part A, section 2002, titled 'Principles' that to be approved for a licence as an approved institution, an applicant must demonstrate that it has established adequate systems, policies and procedures covering corporate governance, finance, risk management, compliance, operations and controls to meet and comply with business and regulatory requirements.

The 2000 Regulations also provide under Part C, section 2204, titled 'Requirements for licence' that an applicant must demonstrate to the CMA inter alia that it has established sufficient systems, policies and procedures covering corporate governance, finance, risk management, compliance, operations and controls to enable it to meet and comply with its business and regulatory obligations for the kind of securities business that it proposes to carry on.

In addition, as aforementioned, the CMA published the Listing Regulations on its website, noting that they have not yet been enacted in the official Arabic version and that the CMA orally confirmed, on several occasions, that these draft regulations are currently being translated into Arabic and that they will be enacted soon.

Codes and guidelines drafted by NGOs such as the LTA and LCGTF

The Lebanese Code of Corporate Governance for Small and Medium-sized Enterprises (LCCG), a voluntary code launched by the Lebanese Transparency Association (LTA) and the Lebanese Corporate Governance Task Force (LCGTF) on 13 June 2006, is based mainly on the OECD Principles. It concerns:

- general rights of shareholders and key ownership functions;
- shareholders' rights with regard to shareholders' meetings;
- equal treatment of shareholders;
- protection of minority shareholders in board composition;
- board structure, membership and function;
- fiduciary duties of board members;
- monitoring board functions and accountability to shareholders;
- determining and disclosing the remuneration of the board of directors;
- the board and the role of stakeholders;
- internal audit; and
- external independent auditors.

The LCGTF has drafted a report on the amendments that need to be made to the LCC to improve corporate governance in Lebanon. The recommendations have been discussed by the parliamentary committee responsible for amending the LCC; however, there has so far been no change in the LCC itself as a result therefrom.

The Corporate Governance Guidelines for Listed Companies were launched in 2009 by the LTA and LCGTF.

The Reference Guidebook on the Corporate Governance of Family Owned Enterprises was launched in 2009 by the LTA and LCGTF.

The Code of Ethics and Whistle Blower Procedure for Small and Medium Enterprises, launched in 2009, was prepared by the Lebanon Anti-Bribery Network, in collaboration with the LTA and the Centre for International Private Enterprise.

A project was implemented in July 2006 by the Association of Banks in Lebanon (ABL) and the International Finance Corporation (IFC), concerning a survey conducted by Ernst & Young on corporate governance practices in the Lebanese banking sector and the legal and regulatory framework pertaining to the corporate governance of banks in Lebanon.

The Union of Arab Banks in association with the LCGTF and the LTA have issued a set of Guidelines for Corporate Governance in Arab Banks. Since then, the LTA also developed toolkits based on such guidelines with the Union of Arab Banks and Financial Services Volunteer Corps. Various training on this toolkit has been given by the LTA with the Union of Arab Banks in the region.

At present, the LTA is also working on a guidebook titled Corporate Governance for Lebanese State-Owned Enterprises, which will be based on the OECD Principles. The first edition of these guidelines was made public for experts' and stakeholders' comments in July 2011 but was not published other than on the LTA's website.

2 Responsible entities

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

There are no governmental agencies or entities that are per se responsible for making corporate governance rules and enforcing them. However, there are some supervisory and regulatory authorities that issue such rules.

The BDL and CMA in their capacity as regulators of the banking and financial sectors, and the capital markets sector, respectively, can render decisions concerning corporate governance that banks, financial institutions and specific companies are obliged to comply with, such as Decision No. 9,382 of 26 July 2006 regarding banks. Regarding banks and financial institutions, the Banking Control Commission will monitor the compliance of banks with such decisions. The BDL will impose penalties and other measures on defaulting banks or financial institutions. Regarding capital markets, the Capital Markets Control Unit will monitor compliance with the decisions of the CMA and the Sanction Committee shall have the authority to impose administrative sanctions and monetary penalties.

The BSE Committee manages the BSE, ensures the compliance of listed companies with the BSE's regulations, mainly those related to the communication of required information to investors, and may decide the interruption of operations of any defaulting listed company or take any other adequate measures. The BSE committee also has the power to issue circulars concerning corporate governance and enforce them, such as the requirement to provide the committee with the listed company's non-audited balance sheet every three months.

The competent commercial registry detects the failure of companies to comply with any corporate governance issue required by the law or the by-laws, at the time of registration of any minutes or any transaction or operation, and may refuse the registration in the event of non-compliance.

The courts may enforce corporate governance principles if these principles are provided by law.

The LTA and LCGTF are non-governmental organisations that undertake numerous activities in the area of corporate governance and promote better corporate governance in Lebanon.

Our answers to question 3 onwards are based on the assumption that the company is a Lebanese joint-stock company (also known as an SAL).

The rights and equitable treatment of shareholders

3 Shareholder powers

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

Appointment of board members

Pursuant to articles 147 to 149 of the LCC, the shareholders' ordinary general assembly (OGA) elects, by a simple majority vote of attending and represented shareholders, from the shareholders holding the minimum number of guarantee shares fixed by the SAL's by-laws, the board members for a maximum period of three years that may be renewed. Article 146 of the LCC also provides the possibility for the first board members of an SAL to be appointed in the by-laws, in which case their mandate is for a maximum period of five years.

Removal of board members

Pursuant to articles 150 and 151 of the LCC, the board members may be removed ad nutum by a simple majority vote of the OGA. However, the dismissed board member may claim for indemnity if such removal was abrupt, if the decision has been taken in an insulting context, and if the board member was not able to defend him or herself before the general assembly. Moreover, if such removal was not mentioned in the agenda of the OGA at which the decision to remove a board member was taken, the decision of removal must be confirmed by a new OGA, the agenda of which mentions such object. The auditors must call for the new OGA and chair it, noting that the new OGA must be held within a time limit of two months following the first OGA.

Legal writings provide that a shareholder may claim before the courts the removal of a board member, if evidence is made that the latter has committed wrongful acts.

The LCCG provides suggestions for strengthening the right of minority shareholders with respect to the appointment of board members.

Power of the assembly to require from the board a particular course of action

Pursuant to article 157 of the LCC, the board of directors has the most extensive powers to implement the resolutions of the assembly and perform all operations within the usual activity of the company and that are not considered as current affairs. These powers may only be limited or restricted by law or in the by-laws.

Hence, the general assembly may require a particular course of action from the board. Moreover, legal writings state that the general assembly may take a decision regarding a specific operation or issue instructions or directives, and that board members' liability could be engaged if they did not respect the general assembly's decisions, instructions or directives.

However, the assembly cannot encroach upon the prerogatives of the board, such as, for example, the appointment of the chairman of the board who is elected by the board itself (article 144 of the LCC).

The courts have decided that the judge for urgent matters may, upon the request of any shareholder, enforce the call for a board meeting, if there is an urgent need and if the chairman fails to call such meeting.

4 Shareholder decisions

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

Pursuant to the LCC, the shareholders can hold OGAs and extraordinary general assemblies (EGA).

Article 196 of the LCC provides that an OGA must be held each year at the end of the financial year: to approve the financial statements and distribution of dividends; to appoint the auditors; and to appoint board members if the term of their appointment has expired.

Article 196 also provides that an OGA may be held during the financial exercise, in unforeseen contexts, provided that such meetings are not held to modify the by-laws. Moreover, an OGA can in principle resolve on all issues that are not specifically reserved by law to the board or to the EGA. The main powers of the OGA are the following:

- appointment and removal of board members;
- appointment and removal of auditors;
- prior approval of transactions between the company and its directors;
- determination of the remuneration of its directors and auditors;
- repurchase by the company of its own shares; and
- issuance of bonds.

The required quorum at the first meeting is a number of shareholders representing at least one-third of the share capital and no quorum is required for the second meeting (held if the quorum at the first meeting is not met). In all cases where there are no provisions to the contrary, decisions are taken by simple majority (50 per cent plus 1) of the attending or represented shareholders.

Pursuant to articles 200 and 201 of the LCC, the EGA, held under stricter quorum and majority vote requirements, is the competent authority to resolve the amendment of the by-laws. However, the LCC provides that an EGA may not change the nationality of the company, increase the obligations of shareholders or undermine the rights of third parties.

Regarding decisions that change the object of the company or its legal form, the quorum must not be less than three-quarters of the share capital. For any other permitted modifications, the quorum is at least two-thirds of the share capital at the first meeting, half of the share capital at the second meeting (if quorum at the first meeting is not met), and one-third of the share capital at the third meeting (if quorum at the second meeting is not met). Decisions must be taken by a majority of two-thirds of the attending or represented shareholders.

Article 111 of the LCC provides that a decision of the general assembly undermining the rights associated to a specific category of shares cannot be implemented without the ratification of such decision by a special assembly of the owners of such category of shares (deliberating according to the conditions of quorum and majority of EGAs).

There is no mention in the LCC of matters that are required to be subject to a non-binding shareholder vote, and the concept of a non-binding shareholder vote is not a familiar concept under Lebanese law.

It is also worth noting that article 192 of the LCC provides that the decisions that are lawfully adopted, according to the conditions of quorum and majority required for each assembly, without fraud or misappropriation of power, bind all shareholders, even those who are absent or dissident.

5 Disproportionate voting rights

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

Every shareholder is entitled to take part in the different meetings held for the incorporation and operation of the company (articles 105 and 185 of the LCC) and to vote with a number of votes in principle equal to the number of shares he or she owns in the company (articles 116 and 186 of the LCC). Article 110 of the LCC sets the general principle according to which all shareholders must have similar rights and enjoy similar benefits.

However, articles 117 and 186 of the LCC provide an important exception to the one vote, one share principle: shareholders who own registered and fully paid shares for at least two years are entitled to a double voting right. Moreover, some court precedents and legal writings consider that the double voting right may not be excluded by the by-laws or waived by the shareholder. For the purpose of these articles, shares are deemed to have been owned by the same shareholder if transferred by donation, inheritance or will. By-laws can establish a voting cap for shareholders. The LCCG recommends the removal of the double-voting right by an amendment of the LCC.

The project of the ABL and the IFC suggests that the granting of any double-voting right becomes subject to the prior approval of the EGA.

6 Shareholders' meetings and voting

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

In principle, all shareholders have a right to receive advance notice of the shareholders' meeting, to attend the said meeting, to discuss the issues on the agenda and to vote on such issues. A shareholder may mandate another person to attend the meeting. This person must be a shareholder. However, the following should be noted:

- article 187 of the LCC provides that a shareholder may not vote, in his or her own name or as proxy, on any decision concerning a benefit to be granted to him or her or relating to a conflict between him or her and the company;
- the by-laws may require that the shareholder owns a determined number of shares to be able to vote;
- the by-laws may provide that shareholders may not attend a shareholders' meeting if they have not fully paid their shares after having been notified by the company to do so;
- co-owners must appoint a representative to vote on their behalf; and
- if a person holds the bare ownership right and another person holds the usufruct right, legal writings consider that the vote will be exercised by the person holding the bare ownership right in the EGA and by the owner of the usufruct right in the OGA.

The LCC does not provide for the possibility for shareholders to act by written consent without a meeting or for the possibility to hold virtual meetings of shareholders.

7 Shareholders and the board

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

According to articles 164 and 180 of the LCC, the board is, in principle, in charge of convening shareholders' meetings. However, article 176 of the LCC obliges the auditors to call a general assembly when the board fails to do so when required by the law or the by-laws, when required to do so by a group of shareholders representing one-fifth of the share capital or when they deem it convenient.

Furthermore, article 190 of the LCC provides that shareholders representing at least one-quarter of the attending shareholders may require the postponement of a shareholders' meeting if they deem that they have not been sufficiently informed about the issues deliberated at the said meeting. The postponed assembly would be held eight days later.

Moreover, if the company loses three-quarters of its share capital and the board does not convene the EGA as provided for in article 216 of the LCC, a quorum for such EGA was not met, or the EGA has rejected the company's dissolution, the shareholders may submit the question to the courts (article 217 of the LCC).

Furthermore, legal experts consider that when a specific group of shareholders is conferred a right to call for a general assembly, this group will have, justifying the quality of its members, to ask the board to call the assembly and indicate the issues to be placed on the agenda; the board's refusal to call the assembly would not only engage the directors' liability as per the terms of article 166 LCC, but would also entitle the shareholders to request from the court the designation of an ad hoc proxy for the convocation.

The LCC does not expressly provide for the shareholders' right to place items on the agenda or to circulate statements by dissident shareholders. The LCCG recommends that shareholders representing 10 per cent of the share capital be entitled to place items on the agenda of the general meetings, and that each company considers including the express right of shareholders to address written questions to the board prior to the shareholders' meeting. The LCCG further recommends that the board should answer such questions in writing at the beginning of the meeting at the latest. The LCCG also provides that shareholders representing a certain percentage of the shareholding may request the board to call the assembly to resolve upon issues proposed by the said shareholders; shareholders representing one-fifth of the company's shareholding may request the court to appoint a court representative to convene the general assembly to resolve upon issues proposed by the said shareholders; and any shareholder evidencing a legitimate interest may file an application with the court requesting the appointment of a court representative to call the general assembly to resolve upon issues proposed by the said applicant.

8 Controlling shareholders' duties

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

Article 192 of the LCC provides that decisions taken by the shareholders' meetings in compliance with the relevant quorum and voting requirements, and that have not been subject to fraud or abuse of rights, shall bind all shareholders including dissident and absent shareholders.

Controlling shareholders owe duties primarily to the company. However, they also owe duties to minority shareholders and resolutions should not only be regularly taken, but must also not undermine the interests of minority shareholders, such as postponement without reason of the distribution of dividends. Failure to take the interests of minority shareholders and the interests of the company into consideration shall constitute an abuse of majority. An enforcement action could be brought by minority shareholders claiming for the annulment of the decision. Courts may annul the resolution and appoint a court representative whose objective is to call for a new assembly, noting that the courts usually do not allow such representative to decide in place of the general assembly. Failure by the controlling shareholders to take the appropriate decision may lead the judge to impose indemnities and penalties on the controlling shareholders.

On the other hand, the minority shareholders owe duties to the company and to the controlling shareholders, and should not block a decision that must be taken in the interests of the company.

9 Shareholder responsibility

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

The general rule is that shareholders in joint-stock companies and limited liability companies are not liable for the company's debts beyond their proportion of the share capital. However, as mentioned in question 8, in cases of abuse of majority, fraud, violation of the applicable laws in taking a resolution or in the case of abuse of minority, the concerned shareholders may be subject to indemnities and penalties decided by the court.

Corporate control

10 Anti-takeover devices

Are anti-takeover devices permitted?

There are no express anti-takeover devices under Lebanese law.

The repurchase by the company of its own shares is recognised in Lebanon under certain conditions. It may allow the company to fight a hostile takeover by reducing the number of shares in circulation that the initiator can purchase, and raise the price of the shares in circulation, which makes the takeover more expensive. Moreover, article 118 of the LCC provides that a pre-emption right can be provided for in the by-laws in favour of either all the shareholders or some of them, or the company, noting that such right should be exercised within a time limit and at price conditions determined in the by-laws. However, the exercise of such right should not be abusive or lead to restricting the transferability of the shares. This pre-emptive right in addition to the consent rights (not expressly provided for by law but accepted in practice under certain conditions) could serve as a form of anti-takeover device.

11 Issuance of new shares

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

As mentioned above, only the EGA can modify the SAL's by-laws, notably in the event of an increase of capital by issuing new shares; therefore, any decision to increase the share capital of the company can only be taken by the EGA, according to the conditions of quorum and majority mentioned above in question 4. It is to be noted that article 205 of the LCC provides that the share capital of the company cannot be raised unless and until the previous share capital has been paid in full.

In the event of an increase of capital by the issuance of new shares to be subscribed to in money, articles 112 and 113 of the LCC provide that existing shareholders of all classes shall have, in principle, a priority right to subscribe to new shares, each in proportion to its existing shares. The EGA can, however, decide that the right to subscribe to the newly issued shares shall not be reserved to pre-existing shareholders, or that it shall only be partially reserved to them, or that it shall not be pro rata to the shares they already own.

12 Restrictions on the transfer of fully paid shares

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

In principle, shares in SALs are freely transferable to third parties. However, articles 89, 118 and 147 of the LCC provide for the following exceptions:

- the transfer of guarantee shares owned by board members may only become effective upon the granting of a release and discharge by the general assembly to such board members;
- shares representing in-kind contributions upon the company's incorporation may only be transferable after the general assembly

has approved the financial statements of the second year following incorporation; and
- pre-emptive rights, consent rights and tag-along rights may be included in the company's by-laws.

In limited liability companies, the parts of any given partner may not be transferred to a third party unless such assignment meets the approval of partners representing at least three-quarters of the capital in a partners' general assembly convened for this purpose. Furthermore, the company benefits from a pre-emptive right to the purchase of the assigned parts within 15 days starting from the date the company is notified of the deed of transfer. In the event that the company does not exercise this pre-emptive right, one or several partners may exercise it within one month starting from the date of their notification.

Also note that there may be other transfer requirements in the by-laws of each company on a case-by-case basis.

13 Compulsory repurchase rules

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

Article 115 of the LCC allows a company, under certain conditions, to repurchase its shares in order to amortise its capital. However, repurchase cannot be imposed on shareholders unless provided for in the by-laws. Moreover, article 209 of the LCC regulates the repurchase by the company of its shares in order to reduce the capital. Legal writings consider that the repurchase of shares can take place for other reasons. The company must pay the price of the shares from its profits or from its free or available reserves. The decision must be taken by the EGA in the event of amortisation or reduction of capital, and by the OGA in the event of repurchase for other reasons.

14 Dissenters' rights

Do shareholders have appraisal rights?

Lebanese law is silent on this matter. However, if the by-laws provide such appraisal rights, the company could repurchase the stock under certain conditions as provided in question 13.

The responsibilities of the board (supervisory)

15 Board structure

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

Lebanese law has adopted a one-tier structure with a board of directors appointed by the OGA. The board of directors appoints one of its members as chairman. It should be noted that, under the LCC, it is not possible to distinguish between the functions of chairman and general manager; the chairman–general manager may, however, suggest to the board the appointment of an assistant general manager who will act on the chairman–general manager's behalf and at his or her personal liability. The board may include executive directors.

16 Board's legal responsibilities

What are the board's primary legal responsibilities?

As specified in question 3, according to article 157 of the LCC, the board has two main areas of responsibility.

General responsibilities

The board's general responsibility is to manage the company. The board should therefore execute the decisions of the general assemblies; monitor the company's administration; and undertake all operations related to the usual operations of the company.

However, the board may not perform the current affairs of the company that are within the prerogatives of the chairman–general manager.

Specific responsibilities

Particular responsibilities of the board specified by law include:
- monitoring the regularity of the incorporation of the company;
- accomplishing the formalities of incorporation;
- publishing the financial statements and the names of board members and auditors in the Official Gazette, an economic newspaper and a daily newspaper each year;
- calling for extraordinary and ordinary general assemblies;
- constituting the reserves;
- setting up the financial statements;
- making financial statements, board and auditors' reports available to shareholders within a time limit of 15 days prior to the date of the assembly meeting;
- calling for an EGA in the event of a loss of three-quarters of the capital; and
- calling for a general assembly within a time limit of two months following the reduction of the number of board members to under half of the minimum number determined in the by-laws or to under three (the minimum required by law).

17 Board obligees

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

The board members represent the shareholders of the company and owe them the fiduciary duties of care, loyalty and compliance with corporate authority. In the discharge of their fiduciary duties, board members must at all times act in good faith, avoiding all potential or actual conflicts of interest. The board is entrusted with the duty of ensuring the proper management of the company in the best interests of the company and all shareholders in accordance with applicable laws and regulations. This duty may not be delegated and is exclusive to the board, which shall assume final responsibility to the company and its shareholders regardless of whether the board constitutes special committees or authorises other persons or entities to undertake specific operations.

18 Enforcement action against directors

Can an enforcement action against directors be brought by, or on behalf of, those to whom duties are owed?

Failure by the directors to comply with the duties entrusted to them by law or to exercise the fiduciary duties owed to shareholders will entitle shareholders to sue them.

Article 166 of the LCC provides that directors are liable, even with regard to third parties, for their fraudulent acts and breaches of the law and of the company's by-laws. Article 167 of the LCC further provides in its first paragraph that directors are also liable towards shareholders for their errors of management.

This article also provides that, as a general rule, the liability of directors for errors of management is not engaged towards third parties. The action mentioned under paragraph 1 of article 167 of the LCC belongs to the company; however, if the latter fails to file such an action, then any shareholder can act in lieu of the company within the limit of his or her interest in the share capital. The action in liability of directors should be brought by the company or the shareholders (as the case may be) within a time limit of five years from the date of the assembly in which the directors had to report on their management. For actions to be brought by third parties, the regular prescriptions provided by law shall be applicable. Also, if the matter is a criminal matter, then the prescriptions provided for under the Lebanese Code of Criminal Procedure shall be applicable.

The project of the ABL and the IFC recommends including adjudication procedures (such as administrative hearings or arbitration procedures organised by the BSE) for listed banks to allow for timely, confidential and cost-efficient processes for resolving disputes between shareholders, directors and managers.

19 Care and prudence

Do the board's duties include a care or prudence element?

Lebanese law does not expressly include a care or prudence element in the board's duties. However, under general principles of commercial law, all board members owe a fiduciary duty to the company and shareholders to act in their best interests and to act with due diligence and care. The duties of care and prudence could be deduced from the provisions of article 167 of the LCC, which specifies that directors shall be liable towards shareholders for management mistakes, and from the assembly's right to remove directors at any time. Established court precedents and legal writings confirm that directors must accomplish their functions conscientiously and in good faith, attend board meetings and refrain from disclosing any confidential information related to the company.

The LCCG recommends that companies adopt a directors' charter detailing the following directors' duties: duty of care, duty of loyalty and duty to comply with the corporate authority.

20 Board member duties

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

Lebanese laws do not differentiate between the duties of individual members of the board. However, courts tend to adopt a stricter approach towards directors who are professional, in the event of claim for failure by the said directors to exercise his or her duties properly.

Legal writings also consider that directors who have a specific function, such as chairman–general manager or technical director, also assume a specific liability for errors committed in the exercise of their specific function. The other directors would be responsible for such errors to the extent they have lacked diligence in the choice of such persons they entrusted with that specific function, or if they lacked diligence in the surveillance of their management.

21 Delegation of board responsibilities

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

Article 157 of the LCC provides that the board of directors may delegate some of its powers to the chairman or the assistant general manager, provided that such delegation is for a fixed limited period and that it is registered at the commercial registry. However, such a delegation cannot include the board's main powers such as calling an OGA or EGA, or the appointment of the chairman.

Article 153 of the LCC provides that if the chairman finds him or herself temporarily prevented from discharging his or her duties, he or she may delegate such duties, totally or partially, to a director for a limited period of time. This article also provides that the chairman–general manager may appoint a consultative committee composed of directors or managers that are not on the board. The members of such committee will have to study the matters deferred to them by the chairman–general manager, and the opinion of such committee shall not be binding upon the chairman or the board.

Moreover, if provided for in the company's by-laws, the board can mandate a director, a committee or a third party to undertake specific actions for a limited period of time.

The LCCG recommends the creation of the following board committees: audit committee, board member nomination and selection committee, compensation committee, regulatory compliance committee and stakeholder relations committee.

According to the BDL's decisions mentioned in question 1, banks and Islamic banks in Lebanon must also now establish specific committees (namely, an internal audit unit, a corporate governance unit and shariah auditing unit (for Islamic banks), an audit committee, a risk committee, a remuneration committee), the composition of which is provided for in the BDL's relevant decisions.

Moreover, according to the CMA's decisions mentioned in question 1, relevant companies must also now establish specific departments (notably an internal audit department and a compliance department), the composition of which is provided for in the CMA's relevant decisions.

22 Non-executive and independent directors

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

The LCC does not provide for such requirements.

Regarding Lebanese banks, however, and as mentioned above, Decision No. 9,956 of 21 July 2008 as amended, relating to the boards of directors of Lebanese banks and the committees deriving therefrom, provides the definitions of non-executive board member and independent board member, and also provides that for the purpose of enhancing the competence and efficiency of the board of directors, Lebanese banks must elect a sufficient number of independent and non-executive members of the board in order to fulfil the requirements of the said decision, especially regarding the establishment of committees deriving from the board of directors. Lebanese banks must also determine a number of non-executive and independent board members that exceed the minimum requirements set out in this decision and in accordance with the concerned bank's size, the degree of complexity of its operations and the scope of its risks (proportionality principle). According to this decision, a non-executive board member is defined as a board member that does not have any managerial position at the concerned bank and that is not assigned an executive mission at such bank or any of its branches or subsidiary units in Lebanon or abroad or is undertaking a consultative role for the bank's senior management (as defined in the BDL's decisions) at present or within the two years preceding his or her membership on the board; noting that the board member that is appointed at any subsidiary units abroad shall not be considered as an executive member in the context of this decision if the laws applicable to him or her in the foreign country do not grant him or her this quality. This decision also defines the independent board member as being the board member who fulfils the following criteria:

- being a non-executive board member;
- not being one of the major shareholders that own, directly or indirectly, more than 5 per cent of the bank's entire shareholding or voting rights relating to such shares, whichever is greater;
- being independent of any person in the concerned bank's senior management (as defined in the BDL's decisions) and of its major shareholders from the perspective of the inexistence of any work relations with any of them at present or within the two years preceding his or her membership on the board;
- not having any family ties up to the fourth degree with any major shareholders; and
- not being a debtor of the bank.

The LCCG recommends that at least 20 per cent of the board members be non-executive members who do not hold any management or executive position in the company.

The project of the ABL and the IFC in Lebanon recommends appointing a sufficient number of independent directors. An independent director is defined as a person who does not have any link whatsoever with the bank (beyond his or her directorship), with any of the bank's group companies or with the bank's management and who, as such, is deemed to be acting objectively. He or she shall not be a representative of dominant shareholders or have close business or family ties with them.

23 Board size and composition

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

Paragraph 1 of article 144 of the LCC provides that the management of a joint-stock company shall be entrusted to a board of directors consisting of between three and 12 members. The size of the board (within the minima and maxima imposed by law) may be determined in the by-laws or a shareholders' agreement. Article 146 of the LCC provides that if, during the period between two annual shareholders' meetings, the number of board members is reduced because of death, resignation or any other cause, below half the minimum number set by the by-laws, or below three, the remaining directors must convene a general meeting of shareholders within a maximum time limit of two months in order to fill the vacant posts.

Concerning the nationality of board members, paragraph 2 of article 144 of the LCC provides that, without prejudice to what may be provided for in special laws governing specific joint-stock companies (such as Lebanese holding and offshore companies, which are incorporated under the form of joint-stock companies but are subject to a special regime), the majority of the board members must be of Lebanese nationality (this requirement is no longer applicable to Lebanese holding and offshore companies).

Furthermore, pursuant to article 147 of the LCC, members of the board are elected among the shareholders who hold the minimum number of shares (that is, the guarantee shares) specified in the by-laws. These shares are registered shares and are marked with a stamp indicating their inalienability. They will be deposited at the company and allocated as a guarantee of the liability of board members for all their faults of management, whether such liability is personal or joint.

Article 148 of the LCC also provides that no person can be a board member if he or she has been declared bankrupt and has not been rehabilitated for at least 10 years, or if he or she has been convicted, in Lebanon or abroad, within at least the last 10 years, for having committed or attempted to commit a crime or a punishable offence of fraud, or for embezzlement of assets or securities, or a bad faith issuance of a cheque with no balance or an attempt against the financial credit or security of the state under articles 319 and 320 of the CC, or for concealment of the goods obtained by way of any of the aforementioned infractions. The same conditions shall apply to the representatives of legal entities within the board.

In addition, article 154 of the LCC provides that:
- no person can be the chairman of the board of more than four companies, and even in such a case this is conditional to the chairman designating an assistant general manager in at least two of such four companies;
- no person can be a member of the board of more than six companies having their head office in Lebanon. This number is reduced to two companies for persons over the age of 70; and
- the mandate of member or chairman of the board of several insurance companies having the same commercial trade name shall be considered as one mandate only.

Furthermore, pursuant to paragraph 3 of article 144 of the LCC, the board of directors elects one of its members to be chairman of the board. Therefore, the chairman must fulfil the same criteria required to be a member of the board, including holding, as with all other board members, the minimum number of guarantee shares.

Moreover, pursuant to the interpretation of paragraph 3 of article 144 of the LCC that is adopted by the Lebanese doctrine and in practice, the chairman must be a physical person.

It should be noted that, in addition to what is mentioned in the LCC, there are additional criteria and specific requirements that need to be fulfilled by board members and chairmen of Lebanese banks as provided for in the CMC and the BDL's decisions and circulars.

Concerning disclosure requirements relating to board composition, pursuant to article 101 of the LCC, every year the board must publish the balance sheet of the closed financial year, as well as the names of the board members and auditors, in the Official Gazette, an economic newspaper and a local daily newspaper, within a time limit of two months following ratification of the accounts by the annual general assembly. Furthermore, article 152 of the LCC provides that any change occurring in the composition of the board of directors must be registered by the board members at the commercial registry.

There are also specific disclosure requirements regarding banks, financial institutions, and listed companies, including the following.

Regarding banks and financial institutions, pursuant to BDL Decision No. 7 of 27 May 1982 concerning the legal documents and annual reports to be provided to the BDL, banks and financial institutions must promptly submit a number of documents, signed and certified as required, to the BDL's legal department following the holding of their annual general assemblies and in any event no later than 30 September of every year, including inter alia:
- two copies of the minutes and attendance sheet of the general assembly, one of which must be certified by the commercial registry, if they include the election of board members;
- three copies of the minutes of the board meeting, one of which must be certified by the commercial registry, if they include the election of the chairman or the confirmation or appointment of the assistant general manager; and
- three copies of a complete list, signed by the chairman, of the names of the chairman and board members for the current year, and the names of the major shareholders, and of the assistant general manager and directors and assistant directors, including also the following information: the surname, family name and nationality of each of the aforementioned persons, and the companies, of any nature whatsoever, in which any of them participates or presides, with a certificate evidencing the type of company and the nature of such person's relation with it (chairman, board member, director, major shareholder, partner, mandated partner, and so forth).

The BDL's legal department will deliver a copy of the aforementioned documents to each of the Banking Control Commission and the BDL's Corporate Governance Unit.

Regarding Lebanese banks, Decision No. 9,956 of 21 July 2008, as amended, relating to the boards of directors of Lebanese banks and the committees deriving therefrom, also provides inter alia that Lebanese banks must provide the BDL's legal department and the Banking Control Commission with, inter alia, the CVs of each board member.

The BDL also issued Decision No. 9,793 on 14 December 2007, concerning information requested on the management of banks and financial institutions, which provides, inter alia, that banks and financial institutions operating in Lebanon must provide the BDL's Corporate Governance Unit with compact discs that contain the personal, professional and financial information, which is set out in the annex to this decision, of the management teams of the banks, including, inter alia, the chairman, the board members, the general managers and assistant general managers, and must promptly provide such details again upon any change to the said information.

Regarding listed companies, Decree No. 7,667 regarding the implementation of the by-laws of the BSE provides for specific disclosure requirements. Article 91 provides, inter alia, in this respect that when applying to be listed, companies must submit an undertaking whereby they undertake to provide the BSE with all documents and necessary information about any major or minor change in the company's management, at the level of the general assembly or in the board of directors' composition, within 15 days from their publication or entry into force. This is further detailed in question 36.

24 Board leadership

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

Under the present applicable Lebanese law, it is not possible to separate the functions of chairman and general manager, and the position of CEO per se is not regulated in the LCC. The LCCG recommends that, until such separation becomes legally feasible, the board of directors appoint a deputy general manager who reports to the board. In practice, some companies appoint the CEO as a deputy general manager with additional powers delegated to the CEO by the board.

25 Board committees

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

Lebanese law does not provide for mandatory board committees. However, as mentioned in question 21, article 153 of the LCC provides that the chairman of the board may appoint a consultative committee comprised of members of the boards or even managers from outside the board. Members of this committee shall be entrusted by the chairman to study specific issues. The advice of this committee shall not bind the chairman or the board.

Moreover, as mentioned in question 21, the board may establish such committees unless otherwise provided for in the by-laws, and it shall be responsible for such committees.

There are no mandatory requirements for committee composition. The LCCG recommends that the nomination and compensation committees be comprised of a majority of non-executive board members.

However, according to the BDL's decisions mentioned in question 1, banks and Islamic banks in Lebanon must now establish specific committees (namely, an internal audit unit, a corporate governance unit and a shariah auditing unit (for Islamic banks) and an audit committee, a risk committee, a remuneration committee), the composition of which is provided for in the BDL's relevant decisions.

Moreover, according to the CMA's decisions mentioned in question 1, relevant companies must also now establish specific departments (notably an internal audit department and a compliance department), the composition of which is provided for in the CMA's relevant decisions.

26 Board meetings

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

There is no minimum number of board meetings per year required by law or regulation or listing requirements. The by-laws freely determine the frequency of board meetings. The LCCG specifies that the board should meet as frequently as necessary for the discharge of its governance obligations and to ensure the good functioning of the company. The LCCG also recommends that the board meets at least once every three months.

Regarding banks, BDL Decision No. 9,956, as amended, provides that the meetings of the board of directors shall not be less than four per year, at least two of which must be held in Lebanon.

27 Board practices

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

The disclosure of board practices is not required by the LCC.

The LCCG recommends that the company's annual report clearly show the number and dates of board meetings held during the year and the names of the board members present or absent at each board meeting. The board may also provide to the shareholders' general assembly a chart showing the number of meetings missed by every board member with the reason for such absence. Moreover, the LCCG recommends that committees established by the board produce quarterly reports to be submitted to the board for review and for inclusion in the company's annual report.

28 Remuneration of directors

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

Article 145 of the LCC provides that the remuneration of directors consists either of an annual remuneration, coupons for attendance, a percentage of the net profit or a combination of such benefits.

BDL Decision No. 9,382, as amended, also provides that the Code of Corporate Governance of banks operating in Lebanon should, inter alia, contain the criteria followed to calculate the compensation of board members and of the senior management (as such term is defined in such decision).

The LCCG recommends that the amount of the remuneration for each board member be commensurate with the contribution of that member to the operations of the company. The guidelines for assessing the remuneration will be developed by the compensation committee. Remuneration shall be determined by the said committee and shall become effective upon approval by the OGA. This power may not be delegated to the board or any corporate body other than the shareholders' assembly. The committee must be elected by the OGA.

Article 149 of the LCC provides that board members are appointed for a maximum of three years subject to re-election, unless appointed in the by-laws, in which case their term will be for a maximum of five years. Moreover, article 153 of the LCC provides that directors may fill administrative positions in the company for a salary that shall be fixed by the board, but in this event they shall not benefit from the provisions of the Lebanese Code of Labour unless they had been working for the company for at least two years by the time they succeeded to the post of director. The employment contract between the director and the company is subject to the procedure of prior approval by the OGA specified in article 158 of the LCC mentioned hereinafter.

The LCCG recommends that the contract term of executive board members should not in principle exceed three years, unless there is a valid and clear reason justifying a longer term. In the event of terms exceeding three years, the board must explain the reasons for extending the term beyond three years to the general assembly approving the said board member contract.

Article 158 of the LCC provides that any transaction between the company and a director is subject to the prior approval of the OGA, whether this transaction is concluded directly or indirectly or through an intermediary. Moreover, the said article specifies that any transaction entered into between the company and another establishment, which would be owned by one of the directors or in which the latter would be a joint partner, manager or director, requires the above-mentioned prior approval and the director that finds him or herself in such a case should declare it to the board.

However, acts covering day-to-day operations between the company and its customers are exempted from the prior approval procedure.

The project of the ABL and the IFC recommends including senior managers and major shareholders in the scope of article 158 of the LCC.

The board and the external auditor of the company must separately submit a special report on anticipated transactions to the assembly. The OGA's decision shall be taken in light of these two reports. The OGA's authorisation must be renewed yearly if the transaction includes long-term obligations. Directors are forbidden by the law (except when they are entities) to obtain in their favour from the company, in any manner whatsoever, a loan, an open current account, a guarantee or an endorsement of trade bills made out to the order of third persons; this prohibition does not apply, however, to banks if the aforementioned operations constitute usual operations within the scope of their activities. There are, however, specific rules governing the granting of loans by banks to their directors.

29 Remuneration of senior management

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

There is no law or regulation or listing requirement that determines the remuneration of the senior management, unless such senior managers are directors (see question 28).

However, Law No. 308, dated 3 April 2001, specifies that the bank's extraordinary assembly may authorise the board to grant the chairman and board members holding executive functions free option rights entitling them to subscribe to the bank's share capital.

Also, as mentioned in question 28, BDL Decision No. 9,382, as amended, provides that the Code of Corporate Governance of banks operating in Lebanon should, inter alia, contain the criteria followed to calculate the compensation of board members and senior management (as such term is defined in such decision).

The LCCG recommends that the management's remuneration be determined by the compensation committee.

30 D&O liability insurance

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

There are no regulations concerning D&O liability insurance. Such insurance is not common practice.

31 Indemnification of directors and officers

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

Lebanese law does not regulate this issue, and such indemnities are not common.

32 Exculpation of directors and officers

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

Legal experts believe that the provisions of articles 166 and 167 of the LCC, which were mentioned in question 18, may be considered to be public policy rules.

Indeed, regarding the provisions of article 166 and 167 of the LCC, legal writers argue that clauses in the by-laws, which state that actions under these articles can only be exercised after authorisation of the general assembly, may not be invoked against third parties or shareholders. However, clauses requiring the general assembly's opinion would be valid. Legal writers also mention, regarding the provisions of article 166 and 167, that the by-laws sometimes contain an arbitration clause, which cannot be applicable if the fact that generates liability is the violation of a rule to be considered as public policy. Therefore, directors' liabilities cannot be limited or precluded by the by-laws, and in this respect any agreement that provides the contrary would be considered null and void.

Article 169 of the LCC also provides that, for it to be opposable, the quietus granted by shareholders to the directors for their administration of the company must always be preceded by the auditing of the accounts of the company and of the report of the auditors, and that it only covers administration and management facts of which the general assembly was able to be aware.

33 Employees

What role do employees play in corporate governance?

Employees do not play a role in corporate governance in Lebanon.

The LCCG recommends that the board adopts a mechanism enabling the company's employees to report any improper behaviour of agents or fiduciaries of the company to the board, where such behaviour is unethical, illegal or detrimental to the company. The board should ensure that the employee addressing the board is afforded confidentiality and protected from any nuisance or negative reaction by other employees or the employees' superiors. Moreover, the LCCG recommends that the board invite employees' representatives or trade unions to the board meeting to discuss any issue of concern to the employees that is to be decided during the meeting.

34 Board and director evaluations

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

Lebanese law does not regulate this issue per se.

Disclosure and transparency

35 Corporate charter and by-laws

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

The by-laws of the company at the time of incorporation, as well as any amendments thereto, must be registered at the commercial registry. Moreover and pursuant to article 100 of the LCC, the company's by-laws must be posted on the noticeboard of the company's offices, and any person may obtain a certified copy thereof, for a reasonable fee.

36 Company information

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

Pursuant to article 101 of the LCC, the board must annually publish the balance sheet of the closed financial year, as well as the names of the board members and auditors in the Official Gazette, an economic newspaper and a local daily newspaper, within a time limit of two months following the ratification of the accounts by the annual general assembly.

According to article 152 of the LCC, any change occurring in the composition of the board must be registered by the board members at the commercial registry.

Moreover, Decree No. 7,667 (regarding the implementation of the by-laws of the BSE) requires that listed companies:

- provide the BSE with all of the minutes of the ordinary and extraordinary general meetings, and the board of directors submitted to the secretariat of the commercial register within a period of two weeks from the date of submission;
- notify the BSE committee and the public in accordance with the rules fixed by the committee of every element or change affecting its financial situation or activity;
- publish the balance sheets, and the annual consolidated and certified final accounts in the stock exchange official bulletin, within a maximum six-month period from the date of closing the accounts;
- publish its results every six months in the official bulletin of the BSE, in accordance with the rules set by the committee;
- explicitly notify its shareholders at any moment and under any circumstances about all of the information of interest to those shareholders, and treat them fairly without any discrimination regardless of the number of securities they own – the issuer is also committed to abstain from any undertaking that may mislead on the price of the traded security;
- provide the committee with all of the information and documents concerning it or any of its branches within a 15-day period from the date of publication or entering into force of these documents (a branch means any joint-stock company owned directly or indirectly by the issuer up to more than 50 per cent and that represents more than 10 per cent of the consolidated net value of the assets belonging to the group). Such information includes:
  - any essential change in the nature of the operations carried out by the company;
  - any total or partial change in the company's administration, general management or board of directors;
  - any appointment of new auditor for the company;
  - any selling or transfer of ownership of the company's assets, when the operation exceeds 5 per cent of its market capitalisation;

Update and trends

There have been two key developments in corporate governance over the past year in Lebanon.

First, the Institute for Finance and Governance (IFG) was created at the initiative of the BDL (officially inaugurated on 25 June 2015) to develop a centre of expertise in finance and governance in Lebanon. Its management has been entrusted to the Ecole Supérieure des Affaires (ESA). The IFG provides its expertise to the BDL and commercial banks in Lebanon and the MENA region and offers ongoing training in governance and finance.

Secondly, Tamayyaz, in collaboration with International Finance Corporation (IFC) (which is a private sector branch of the World Bank) now offers a corporate governance programme for corporate directors in banks, small and medium-sized enterprises and family-owned enterprises (and in general, private sector enterprises), noting that the IFC issues a certificate at the outset of the programme and after an online exam.

- anything that may positively or negatively affect the price of the company's financial securities; and
- any amendment to the number of voting rights enjoyed by any of the shareholders, when the issuer is aware of it, and when the variation exceeds 2 per cent for the general manager, the assistant general manager, or a member of the company's board of directors, or 10 per cent for the other shareholders directly or indirectly enjoying more than 10 per cent of the voting rights in the company whose shares are priced in the stock exchange;
- provide the committee of the BSE, immediately and free of charge, with any documents addressed to the shareholders and any statement published in the newspapers, in order to give an opportunity to the public to read them freely;
- provide the committee with every notice addressed to the shareholders or security bearers to attend any ordinary or extraordinary general assembly, at least 20 days before the expected date, and payment of the fees for publishing the notice in the stock exchange official bulletin; and
- include in the company's by-laws a text fixing the voting rights at 10 per cent for each shareholder not having explicitly declared beforehand to the issuer's board of directors that he or she has reached or exceeded this proportion. The shareholder should explicitly inform the board of any change exceeding 10 per cent in terms of the number of voting rights.

Also, by virtue of BDL Decision No. 9,382 of 26 July 2006, as amended, all banks operating in Lebanon must, inter alia, publish a summary of their Code of Corporate Governance on their website and in their annual report, and provide the Banking Control Commission with a soft and a hard copy of such Code and of any amendments thereto.

In addition to the above, and as mentioned in question 1, Decision 2 lists the minimum information that should be disclosed to the shareholders or funds' part holders by the joint-stock companies and collective investment funds working in Lebanon, the shares or parts of which are able to be traded in the regulated or unregulated (OTC) financial markets, and which have more than 20 shareholders or part holders.

Hot topics

37 Say-on-pay

Do shareholders have an advisory or other vote regarding executive remuneration? How frequently may they vote?

As mentioned in question 28, article 145 of the LCC provides that the remuneration of directors consists either of an annual remuneration, coupons for attendance, a percentage of the net profit or a combination of such benefits.

The law in Lebanon is silent regarding executive remuneration, and the latter can be as decided in the by-laws. Hence, the by-laws of the company may determine if the executive remuneration is to be decided by the board or by the OGA.

If the by-laws grant the right to decide on the executive remuneration to the OGA, the shareholders would have a vote regarding executive remuneration through their vote in the OGA, in compliance with the conditions included in the by-laws, notably regarding the required quorum and majority for such meeting as well as the frequency at which shareholders may vote in this respect.

It is, however, important to note the provisions of the aforementioned BDL Decision No. 11,821 regarding the remunerations and bonuses granted to banks' employees.

The LCCG recommends that the amount of remuneration for each board member should be commensurate with the contribution of that member to the operations of the company. The guidelines for assessing executive and non-executive board members' remuneration and benefits will be developed and applied by a compensation committee and made available in writing to all shareholders at the time their shares are registered and whenever requested by any shareholder. Indeed, the LCCG recommends that a compensation committee be formed, whose objective shall be the recommendation of remuneration packages and agreements of board members and management. The recommendation of the compensation committee shall be submitted to the board for submission to and approval by the shareholders' general assembly. The compensation committee shall be elected by the OGA every two years and shall consist of at least one-third of shareholders with less than 10 per cent ownership in the company who are nominated by the board and elected to that committee by a vote of all shareholders owning individually less than 10 per cent of the company's share capital at the time of the general assembly. It is recommended that the compensation committee include a maximum of one executive board member if any, noting that executive board members may not in any event constitute more than 30 per cent of the compensation committee members and may not vote on their own remuneration. In conclusion, board members' remuneration should be determined by the compensation committee and shall become effective upon approval by the OGA. The power to determine and approve the remuneration of the board may not be delegated to the board or any corporate body other than the shareholders' assembly. The total remuneration, including all benefits, of board members and top management should be disclosed in the company's annual report or other company's reports.

38 Shareholder-nominated directors

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

The shareholders may not nominate directors – they are elected by the OGA. According to article 147 of the LCC, the OGA elects board members among the shareholders that own a minimum number of shares determined in the by-laws.

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39 Shareholder engagement

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

The applicable laws and regulations do not expressly address shareholders' engagement with the company. However, and as mentioned above, according to article 147 of the LCC, members of the board of directors are elected from among the shareholders who hold the minimum number of shares specified in the by-laws; hence, members of the board of directors are also shareholders. Customarily, and in principle, shareholders are involved in the company's business and operations; this is even more true in family-owned enterprises and small and medium-sized enterprises. Therefore, the company's engagement with its shareholders, and even directors, senior management, outside counsel and so forth, is determined on a case-by-case basis, taking into account a variety of factors, such as the number of shareholders, the composition of the board of directors (and whether there are any committees of the board), the activities of the company, the provisions of the company's by-laws and the provisions of the shareholders' agreement (if any).

In the case of minority shareholders, their engagement may be less impactful than the engagement of majority shareholders given that, in principle, they would not be granted the right to nominate members of the board of directors, and hence are not as well represented on the board of directors as majority shareholders are.

* *The authors would like to acknowledge the work of their colleagues Carine Farran and Yara Romanos in the 2017 update of this chapter.*

Luxembourg

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Sources of corporate governance rules and practices

1 Primary sources of law, regulation and practice

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

Corporate governance in Luxembourg is primarily based on statute law, which consists mainly of the Civil Code, the Law of 10 August 1915 on Commercial Companies, as amended (the Companies Act) and, for listed companies, the rules and regulations of the Luxembourg Stock Exchange (the Rules and Regulations). The statute law contains only very general governance rules or principles. The Luxembourg Stock Exchange (LSE) has published a set of principles on corporate governance, which first came into effect on 1 January 2007. A third revised version was published in May 2013 (the LSE Principles). They were drawn up to provide guidelines for the best practice in corporate governance for all Luxembourg companies listed on the regulated market of the LSE. Luxembourg companies, the shares of which are admitted for trading on a regulated market operated by the LSE, must apply the LSE Principles, whereby they are asked to comply with the recommendations included therein or explain why they are departing from them.

2 Responsible entities

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

In general, the LSE is the primary institution for making and enforcing such rules. Monitoring solely by the market would not have been sufficient, thus, a combined approach has been chosen, handing over the monitoring of compliance with the LSE Principles to the companies' shareholders, the boards of directors and the LSE.

The rights and equitable treatment of shareholders

3 Shareholder powers

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

The Companies Act organises the management of a company under a single-tier system (ie, board of directors) or a two-tier system (ie, management board and supervisory board).

Single-tier system

Directors are appointed by the shareholders in a general meeting. They shall be appointed for a term set by the general meeting of shareholders, however their term of office may not exceed six years. Directors may be removed at any time by the shareholders in a general meeting.

Two-tier system

Members of the supervisory board are appointed and removed by the shareholders in a general meeting. They shall be appointed for a term set by the general meeting of shareholders. The duration of their office may not exceed six years. They may be removed at any time by the shareholders in a general meeting. Members of the management board are appointed by the supervisory board unless the articles of association reserve such competence to the general meeting of shareholders. The duration of their office may not exceed six years. They may be removed by the supervisory board or by the general meeting of shareholders, if provided by the articles of association.

Directors are elected and removed by a resolution of the general meeting of shareholders adopted by a simple majority of the votes.

4 Shareholder decisions

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

The general meeting of shareholders has powers reserved to it under the Companies Act. An amendment to the articles of association, an increase in the capital of the company and a reduction of the capital require the approval of the general meeting of shareholders (both by a two-thirds majority of the votes cast at an extraordinary general meeting, the quorum for which is at least 50 per cent of the issued share capital). An increase in the commitments of the shareholders requires a unanimous vote of the shareholders in a general meeting.

At least one general meeting of the company must be held in the Grand Duchy of Luxembourg every year, within six months of the end of the financial year. The annual accounts, the auditor's report and the directors' report (which are available for prior inspection) must be approved by the annual general meeting of shareholders. The annual dividend is also approved by the shareholders' annual general meeting, though, if provided for in the articles of association of a company, the board of directors may proceed to the payment of interim dividends.

Further, in cases of mergers, divisions or liquidations, the approval of the general meeting is also required, generally, by a two-thirds majority and a 50 per cent quorum.

The Companies Act does not set out specific matters that are required to be subject to a non-binding vote.

5 Disproportionate voting rights

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

Luxembourg corporate law is governed by the 'one share, one vote' rule.

However, where shares are of unequal value or where there is no indication of value, each share, unless otherwise provided for in the articles, shall ipso jure carry the right to a number of votes proportionate to the corporate capital represented by it, with one vote being allocated to the share which represents the lowest proportion.

The articles of association may provide that the board of directors or the management board, as the case may be, can suspend the voting rights of any shareholder in breach of his or her obligations as foreseen in the articles or the subscription deed.

6 Shareholders' meetings and voting

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

There are no special legal requirements to attend shareholders' meetings or to vote. The articles of association may, however, provide rules in this respect. Shareholders can, if the articles of association allow, attend the general meeting by any telecommunications method that allows the identification of the shareholder and guarantees their effective participation in the meeting.

It is also possible for companies to allow their shareholders to vote in advance by post.

The Law of 24 May 2011 on the exercise of certain rights of shareholders in listed companies provides, in principle, that only shareholders holding shares of the listed company on the record date may participate and vote at a general meeting of shareholders. The record date is set at midnight (Luxembourg time) on the date falling 14 days before the date of the general meeting of shareholders. Shareholders of a listed company may now freely transfer their shares at any time before the general meeting of shareholders and are no longer subject to transfer restrictions and blocking of shares prior to the meeting. The articles of association of a listed company may authorise shareholders to vote by correspondence or electronically prior to a shareholders' meeting by means of a voting form provided by the company.

Pursuant to the Law of 6 April 2013 on dematerialised securities, the holders of dematerialised securities may participate in the general meeting provided that they hold these securities at the latest on the 14th day before the meeting at midnight, Luxembourg time.

The shareholders may not act by written consent without a meeting. However, shareholders in private limited liability companies (SARL) having less than sixty shareholders (except in the event of amendments to the articles of association), may cast their votes in writing upon receipt of the text of the decision to be adopted.

7 Shareholders and the board

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

In a public limited liability company, shareholders representing one-tenth of the capital of the company may request the holding of a meeting, with an agenda indicated by them. Such meeting must be convened by the board of directors so as to be held within one month of the request. In addition, shareholders representing at least 10 per cent of the capital of the company may request the addition of items to the agenda of the shareholders' meeting if such request is sent to the registered office of the company by registered mail at least five days prior to the holding of the meeting.

In a private limited liability company, general meetings may be convened by the members representing more than half of the capital.

In listed companies, shareholders representing at least 5 per cent of the share capital are entitled to request that additional items be put on the agenda of any shareholders' meeting and to submit draft resolutions for items on the agenda. Requests for both must be addressed, by letter or electronic means, to the address mentioned on the shareholders' convening notice and reach the company at the latest on the 22nd day preceding the date of the meeting.

The agenda items requested by the sufficient shareholding percentage may include director nominations, even against the wishes of the board. Shareholders may not, however, force the board to circulate any kind of statements since they shall be under duty not to divulgate any information which they have concerning the company, the disclosure of which might be prejudicial to the company's interests, except where such disclosure is required or permitted by a legal or regulatory provision applicable to the company or is in the public interest.

8 Controlling shareholders' duties

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

Controlling shareholders do not owe any particular duty to the company or to the non-controlling shareholders under the Companies Act. However, pursuant to the Law of 19 May 2006 on takeover bids, if a shareholder acting alone or in concert acquires securities of a company whose securities are admitted to trading on a regulated market that, when added to any existing holdings of those securities, give him or her voting rights representing one-third of all of the voting rights attached to the issued shares in the company, such person is, in principle, obliged to make a bid for the remaining shares in the company. Also, the Law of 11 January 2008 on transparency requirements for issuers of securities, as amended, provides that a shareholder shall make a notification to the company, where Luxembourg is the home member state of the company and the shares of the company are admitted to trading on a regulated market, if the shareholder acquires or disposes of shares so that the proportion of shares held by that shareholder reaches, exceeds or falls below the thresholds of 5 per cent, 10 per cent, 15 per cent, 20 per cent, 25 per cent, one-third, 50 per cent or two-thirds. The Law of 21 July 2012 on mandatory squeeze-out and sell-out finally provides that the majority shareholder, when it acquires or disposes of securities resulting in attaining, falling below or exceeding a previously attained threshold of 95 per cent, must notify the company and the Luxembourg Supervisory Commission of the Financial Sector as soon as possible and no later than four days thereafter.

9 Shareholder responsibility

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

In Luxembourg, companies may be set up by limited or unlimited members. Unlimited members will be jointly and severally liable without limitation for all obligations of the company. Examples of corporate forms that may have unlimited members include general partnership (SNC), limited partnership (SCS), cooperative company (SC), partnership limited by shares (SCA), temporary association and equity association. The liability of limited shareholders is limited to the amount of share capital they have subscribed. Examples of corporate forms that have only limited members are the public limited liability company (SA) and the private limited liability company (SARL).

Limited shareholders of an SCA or SCS, not being permitted to get involved in the external management activities, will be indefinitely liable for any commitments of the SCA or SCS in which they participated despite the aforementioned prohibition. Such a limited member will also be indefinitely liable to third parties for commitments in which he or she did not participate, if he or she has regularly managed the business of the SCA or SCS in relation to third parties. The Companies Act lists certain management acts for which the liability of the limited shareholder is not unlimited in relation to third parties.

Under Luxembourg bankruptcy law, in the event of the bankruptcy of a company, shareholders may be held liable if they behaved as de facto directors and carried out acts that contributed to the insolvency of the company.

Corporate control

10 Anti-takeover devices

Are anti-takeover devices permitted?

Under Directive 2004/25/EC on takeover bids (the Takeover Directive) the target's board should remain passive before the takeover bid (the 'board-passivity' rule). In addition, the Takeover Directive provides that restrictions on the transfer of shares, or on the voting rights of a target company (whether statutory or contractual), are not effective in relation to the bidder during the acceptance period for a bid (the 'breakthrough' rule).

The law implementing the Takeover Directive in Luxembourg gives Luxembourg companies the choice as to whether to apply the board passivity and breakthrough rules.

Companies that apply the board passivity and breakthrough rules can be exempted from applying those rules if they become the object of a takeover bid launched by a company not applying those rules, provided authorisation is given at a general meeting of shareholders of the target company.

11 Issuance of new shares

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

The board is only permitted to issue new shares if so authorised. Authorisation to increase the capital on one or more occasions up to a specified amount (the authorised capital) may be granted to the board by the articles of the company or the general meeting by means of amendment of the articles and shall be valid only for a period of up to five years from publication of the constitutive instrument or the amendment of the articles or, if so provided by the articles, from the date of the constitutive instrument or the instrument amending the articles. Shareholders generally have pre-emptive rights to acquire newly issued shares in the proportion of the capital represented by their shares. However, if new shares are issued within an authorised share capital increase, the articles may authorise the board to withdraw or restrict pre-emptive rights.

12 Restrictions on the transfer of fully paid shares

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

The transfer of fully paid shares in an SA may not, in principle, be restricted. Clauses such as pre-emption rights, rights of first refusal or prior board approval are, however, acceptable, to the extent that the transferability of the shares is not restricted absolutely. Lock up provisions must be limited in time. Corporate units of an SARL may not, however, be transferred to non-members unless members representing three-quarters of the corporate units agree on the transfer; however, the articles of association may lower this majority to half of the corporate units.

13 Compulsory repurchase rules

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

A compulsory share repurchase is, in principle, not acceptable under Luxembourg law. As an alternative, the voting and dividend rights may be restricted in certain circumstances.

In listed companies, if following a takeover bid made by a shareholder (alone or in concert), a shareholder becomes a majority shareholder or a majority shareholder acquires additional securities, the remaining shareholders may require their securities be sold out by the majority shareholder under certain conditions laid down by the Law of 21 July 2012 on mandatory squeeze-out and sell-out.

14 Dissenters' rights

Do shareholders have appraisal rights?

Generally, shareholders do not have appraisal rights by law. Only the members of an SC may resign under certain conditions in the case of a merger. However, the articles of a company can grant shareholders appraisal rights.

The responsibilities of the board (supervisory)

15 Board structure

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

The predominant board structure for (listed) companies organised under Luxembourg law is one-tier. In this case, a company is only managed by a board of directors, which is vested with the broadest powers to act in the name and on behalf of the company.

The two-tier structure was introduced into Luxembourg corporate law by the Law of 17 August 2006. In a two-tier system, the company is managed by two bodies: a management board, which is in charge of the day-to-day management of the company, and a supervisory board, which is in charge of controlling the management board.

16 Board's legal responsibilities

What are the board's primary legal responsibilities?

The board of directors or the management board can take any action oriented towards realising the corporate object of the company, apart from those powers vested in the shareholders' meeting by the articles of association or by law. Limitations upon the powers of the board of directors or the management board are normally not enforceable towards third parties.

17 Board obligees

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

The board of directors or the management board represents the company. The directors or members of the management board must act with loyalty, honesty and in good faith for the exclusive benefit and in the corporate interest of the company. The notion of corporate interest is thereby not limited to the interests of the shareholders, but also entails the interests of employees, minority shareholders, third parties and creditors.

18 Enforcement action against directors

Can an enforcement action against directors be brought by, or on behalf of, those to whom duties are owed?

The liability of the directors or the members of the management board and of the supervisory board in the performance of their mandate is conceived as a contractual liability with regard to the company. The shareholders cannot sue the directors as individuals; it must be a collective decision.

There is an exception to this general rule, however. Where there is a violation of Luxembourg corporate law or a violation of the articles of association of the company, the directors, members of the management board and supervisory board are jointly and severally liable with regard to the company and third parties, including individual shareholders, if the individual shareholders or third parties have suffered a distinct and independent prejudice. The directors and members of the management committee shall be discharged from such liability in the case of a violation to which they were not a party provided no misconduct is attributable to them and they have reported such violation, as regards members of the board of directors, to the first general meeting and, as regards members of the management committee, during the first meeting of the board of directors after they had acquired knowledge thereof.

The foregoing rules do not restrict the ability of the company's individual shareholders and third parties to sue on the basis of general tort rules when the directors have engaged in tortious conduct (as opposed to a mere management fault).

19 Care and prudence

Do the board's duties include a care or prudence element?

The directors or the members of the management board must exercise their duties with as much care, diligence and skill as would be displayed by a reasonable person in the same circumstances. If the directors or members of the management board are professionals, one might expect a higher standard, namely that which would be displayed by a reasonably competent member of the same profession.

20 Board member duties

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

The standard of care is that of a reasonable person acting in the same circumstances. Hence, if the director or the member of the management board is a professional, a higher standard of care (customary for such profession) can be expected.

21 Delegation of board responsibilities

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

The daily management of the company cannot be delegated to members of the supervisory board. The board of directors or the management board may delegate the day-to-day management and the power to represent the company to one or more directors, members of the management board as the case may be, managers, officers, or other agents acting either alone or jointly. If authorised by the articles of association of the company, the board of directors may also delegate its management powers to a management committee or to a managing executive officer. However such delegation may not comprise the general policy of the company or the whole of the actions reserved to the board of directors pursuant to the law.

22 Non-executive and independent directors

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

The Companies Act does not contain any provisions on independent directors. It merely states that directors are obliged to report any conflict of interest to the board of directors and subsequently to the next general meeting.

The LSE Principles recommend having an appropriate number of independent directors depending on the nature of the company's business activities and on the structure of its shareholder base. The guideline recommends to have at least two independent directors. To be considered independent, a director must have no significant business relationship with the company, close family relationship with any executive manager, 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.

23 Board size and composition

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

The Companies Act does not contain any provisions on the criteria that an individual director or the board as a whole must fulfil or related disclosure requirements.

Depending on the corporate form, the board of directors submits to different rules relating to the minimum number of seats. For example:

- an SA may be managed by one director as long as it has a sole shareholder. In the case of plurality of shareholders, the SA shall be managed by a board of directors comprising at least three directors, irrespective of whether they are shareholders; and
- an SARL is managed by one manager or several managers appointed by the shareholders' general meeting. If several managers are appointed, they may constitute a board of managers, irrespective of whether they are shareholders.

The size of the board is determined by the shareholders' general meeting in accordance with the Companies Act and the articles of association. The Companies Act does not define a maximum number of seats.

The shareholders' general meeting has the power to appoint directors on newly created directorships. Besides the general meeting, the board of directors of an SA has the power to co-opt a temporary director whose mandate shall be confirmed at the next general meeting.

The LSE Principles recommend that the board is composed of competent, honest and qualified persons. In their backgrounds diversity, the members of the board represent a contrast of experiences and knowledge and, as far as possible, the board should have an appropriate representation of both genders, as well as geographical origin. In order to ensure effective deliberation and decision-making, a maximum of sixteen directors may be considered as a reasonable limit. A list of the board members should be disclosed in the corporate governance chapter of the companies' annual report which shall contain information regarding each board member's level of independence. With a view to the tax treatment of companies in certain cases, a genuine presence in Luxembourg may be required, which in turn can necessitate that the majority of the board having the power to bind the company are Luxembourg residents or non-residents who are taxable in Luxembourg for at least 50 per cent.

24 Board leadership

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

The combination of the function of board chairman and CEO is not regulated by the Companies Act. The LSE Principles recommend that the board shall make a clear distinction between the duties and responsibilities of its chairman and the CEO and set this out in writing.

25 Board committees

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

The board of directors may decide to create committees. The composition and the duties of such committees shall be determined by the board of directors and they shall exercise their activities under the responsibility of the board of directors. Companies that constitute 'public interest entities' in the sense of the Law of 23 July 2016, such as listed companies, credit institutions, insurance undertakings and pension funds, shall have an audit committee.

The LSE Principles provide in general terms that the board of directors shall ensure the setting up of special committees necessary in order to review specific issues determined and to advise the board of directors on these issues. Special committees shall ideally be composed of four members. In addition, the LSE Principles recommend that the board shall establish an audit committee to assist in the areas of financial reporting, internal control and risk management; a nomination committee to assist in the selection of directors; and a remuneration committee to assist, among others, in drawing up of a remuneration policy, assess the performance of the executive management and submit proposals regarding their remuneration.

26 Board meetings

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

There must be at least one board meeting a year to approve the annual accounts and to convene the annual general meeting of shareholders. The Companies Act does not set a minimum number of board meetings a year, except for European companies where the board shall meet at least once every three months.

27 Board practices

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

For listed companies, appendix B of the LSE Principles sets out transparency requirements regarding the main aspects of the company's corporate governance, such as a description of the company's governance structure; the essential features of the corporate governance framework; the policy implemented by the board regarding transactions in

Update and trends

By the stability of Luxembourg's corporate governance system, shareholders are offered a valuable protection. Although most shareholders in Luxembourg companies are passive, it is expected that boards of large or listed companies will be under closer scrutiny in the future.

Last year was marked by the adoption of the law of 10 August 2016, which modernises the law of commercial companies of 10 August 1915. The new regime came into force on 23 August 2016.

The modernisation of the law on commercial companies aimed at asserting the attractiveness of Luxembourg as a major financial centre for international investors. The reform brought significant changes to the legislation, including corporate governance. As examples, we cite the possibility to create committees at the level of the board of directors, which is now specifically provided, the reinforcement of certain minority shareholders' rights (eg, extension of the right to request information on management decisions), and the recognition under certain conditions of agreements governing voting rights.

Corporate governance is expected to continue to evolve in the coming years. Besides focusing on performance, boards will have to take into consideration various issues such as compliance, data protection, diversity policy, sustainability, corporate social responsibility, as well as the adoption of new international regulations impacting Luxembourg companies.

the company's securities and other contractual relationships; and a description of the risk management system.

28 Remuneration of directors

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

Directors, as such, are not employees of the company and so general rules on mandates and corporate law will apply. The only rule to mention is on conflicts of interest (see question 22). In the event that directors should receive remuneration, this can be determined either by the articles of the company, by the directors themselves or by the general meeting. If the articles are silent on this topic, the general meeting has the right to decide on remuneration and to determine the modalities. The LSE Principles recommend the setting up of a remuneration committee to deal with these issues. Directors may not be appointed for a period exceeding six years but are eligible for reappointment after this period.

29 Remuneration of senior management

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

Senior management will normally be employees of the company. As such, the relationship is governed by Luxembourg labour law. The LSE Principles on remuneration policies will also apply if the company is listed.

30 D&O liability insurance

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

Directors can have their potential liability insured with an insurance company. Such insurance contract is, in practice, often concluded by the company itself and covers the company's regularly appointed directors. The insurance will cover the liability of the directors towards the company and third parties as well as the liability resulting from a management fault, a violation of the Companies Act or of the articles of association and from torts.

However, as a general matter, insurance law disallows claims if the damage was caused by a serious mistake, such as gross negligence or a wilful act of the insured.

31 Indemnification of directors and officers

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

Luxembourg law does not allow contractual limitations on directors' liability or an arrangement between the company and its directors that, without actually limiting the liability of the directors, would have the same effect. Such an indemnification arrangement would have the effect of excluding the company from the group of persons who by law are given the right to bring an action against the directors, which is illegal.

The situation is different if the company only agrees to indemnify the directors in the case of a third-party action against the directors. Third parties include the shareholders if, and to the extent, they have personally suffered from damage caused to the company. Far from affecting the composition of the group of persons entitled by law to bring an action against the directors, such an indemnification arrangement merely shifts some risk from the directors to the company.

32 Exculpation of directors and officers

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

Shareholders may not preclude or limit the liability of directors and officers towards the company or other shareholders but may agree that directors and officers are not liable towards themselves (see also question 31).

33 Employees

What role do employees play in corporate governance?

The board of directors of an SA employing at least 1,000 employees over a three-year period must be composed of a minimum of nine directors, one-third of whom shall represent personnel. Also, undertakings employing at least 150 employees over a three-year period must have a joint-works council, which has the right to be informed and consulted in certain defined cases, for example, in decisions that have a significant influence on the company's structure or level of employment.

34 Board and director evaluations

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

In accordance with the LSE Principles (which are applicable to listed companies only), the board of directors is required to discuss its operation, the effective fulfilment of its remit and compliance with good governance rules at least once every two years.

Disclosure and transparency

35 Corporate charter and by-laws

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

The articles of association and all amendments thereto are filed with the Register of Commerce and Companies and are published in the Recueil Electronique des Sociétés et Associations (the official gazette).

However, only extracts of the instruments or the deeds establishing SNCs, SCSs and special limited partnerships (SCSps) shall be published. The extract must contain, on pain of being declared inadmissible, some particulars such as:

- a precise designation of the members who are jointly and severally liable;

- the denomination of the company, its object and the place where its registered office is located;
- the designation of the managers, their signatory powers and, as regards SNC, the nature and the limits of their powers; and
- the date on which the company commences and the date on which it ends.

The extract of company instruments shall be signed, in the case of notarial deeds, by the notary who retains the complete deed or in the case of private instruments, by all members who are jointly and severally liable.

36 Company information

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

Luxembourg companies must file their annual accounts and appendices with the Register of Commerce and Companies. This must be done within one month of their approval by the shareholders' general meeting. In addition, any amendments of the articles of association must be filed. The same applies to resignations and appointments of directors and statutory or agreed independent auditors, as the case may be. Further publication, filing and storage requirements apply to periodic and ongoing information of issuers whose securities are admitted to trading on a regulated market pursuant to the Law of 11 January 2008 on transparency requirements for issuers of securities, as amended. The Regulation 596/2014 of the European Parliament and of the Council of 16 April 2014 on market abuse also requires that under certain conditions, inside information may be disclosed to the public.

Hot topics

37 Say-on-pay

Do shareholders have an advisory or other vote regarding executive remuneration? How frequently may they vote?

The general meeting of shareholders, to be held at least yearly, may resolve on the remuneration of directors. Further, the delegation of the day-to-day management within the one-tier system in favour of a member of the board of directors shall entail the obligation for the board to report each year the delegate's salary, fees and any advantages granted to the ordinary general meeting. In addition, the LSE Principles provide for the establishment of a remuneration committee from among the members of the board formulating a remuneration policy for directors and managers. The Law of 19 December 2002 regarding the Register of Commerce and Companies as well as accounting and annual accounts of companies, as amended, provides that the compensation of members of the supervisory board, and members of the board of management or of the board of directors are written on the annex of the annual accounts and only given on a global basis for each category of members.

38 Shareholder-nominated directors

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

The directors are appointed by the shareholders' general meeting. One or more shareholders who together hold at least 10 per cent of the capital may request that items such as the nomination of a director be put on the agenda. Such a request needs to be sent to the company at least five days before the general meeting.

The Law of 24 May 2011 reduces the aforementioned threshold to a minimum of 5 per cent of the capital in the case of listed companies. The request must reach the listed company at the latest on the 22nd day preceding the date of the meeting and the company must make a revised agenda available at the latest on the 15th day preceding the meeting. As a result, shareholders who are allowed to nominate directors may have their appointment included in the relevant convening notices and powers of attorney at the company's expense.

39 Shareholder engagement

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

Shareholders are invited to play an active role in the life of the company. Shareholders' meetings shall have the broadest powers to adopt or ratify any action relating to the company. Even if an annual general meeting must be held at least every year in Luxembourg, the shareholders of the company representing one-tenth of the corporate capital may request, at any time, the management board, the board of directors, as the case may be, and the supervisory board and the statutory auditors to convene a general meeting within one month. As already mentioned in question 38, one or more shareholders representing together at least 10 per cent of the corporate capital may request that one or more additional items be put on the agenda of any general meeting.

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Sources of corporate governance rules and practices

1 Primary sources of law, regulation and practice

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

The Law on Trade Companies (LTC), published in 2004, and the Securities Law (SL), published in 2005, are recognised as the primary sources of law relating to corporate governance.

The LTC allows for an adjustable structure in trade companies' management, by letting the company opt between a one-tier or two-tier management structure, subject to the application of mandatory rules for certain joint-stock companies. The LTC is the general law that stipulates the manner of establishment, structure and functioning of the management bodies of the companies. The subsequent changes in the LTC have strengthened the position of the shareholders' meeting, introduced independent directors and imposed the internal audit, as a separate organisational unit in the companies. With the frequent changes of the LTC, the protection of the shareholders remains the focus. The shareholders' position is strengthened by granting them the right to challenge the interested-party transaction in a court procedure if, inter alia, the arm's-length principle in entering such a transaction was not obeyed, as well as by stipulating the requirement for mandatory external auditor's opinion as one of the conditions for approving an interested-party transaction for listed companies if certain thresholds are met.

The SL regulates the manner and conditions for the issuance and trading with shares, and sets the general legal framework of the capital market and of the licensed market participants, disclosure obligations of joint-stock companies with special reporting obligations, and other issues with regard to shares.

Another law important for corporate governance in Macedonia was the Takeover Law passed in 2002, which applied only to reporting companies. It regulated the manner and conditions for the purchase of shares by a person that has acquired or intends to acquire participation ensuring over 25 per cent of the voting rights deriving from the shares of a reporting company. In May 2013, the new Takeover Law was passed regulating the manner, the conditions and the procedure for takeover of shares issued by listed joint-stock companies and reporting companies, extending its application for a year after the companies delist or no longer meet the requirements for a reporting company. The new Takeover Law introduced thresholds of acquired voting shares of the target company for a mandatory bid. The trigger for a mandatory takeover bid is still acquisition of more than 25 per cent of the voting shares as the control takeover threshold. The additional takeover threshold is set as acquisition of an additional 5 per cent of the voting shares within a period of two years as of the successful takeover, and the final takeover threshold is at least 75 per cent of the voting shares of the target company acquired in the takeover procedure, after which the obligation for submission of a takeover bid terminates.

Established as an autonomous and independent regulatory body with public authorisations prescribed by the SL, the Law on Investment Funds and the Takeover Law, the Securities and Exchange Commission (SEC) passed a number of secondary legislation deriving from the laws mentioned above, further regulating the corporate governance.

In addition, the Corporate Governance Code for Companies listed on the Macedonian Stock Exchange (MSE) is based on the OECD Corporate Governance Principles and provides for the 'best-practice provisions' for the managers, directors and shareholders of the companies listed on the MSE. Though voluntary in nature, the 'comply-or-explain' principle imposes an obligation for the listed companies to explain the level of compliance with the best-practice provisions and the reasons for non-compliance.

The MSE has also prescribed the Listing Rules for the companies, which sets out the basic conditions that have to be met for the listing on the MSE official market, as well as the ongoing disclosure requirements for the listed companies. The SL changes passed in January 2013 reintroduced mandatory listing for joint-stock companies that fall under the criteria set with the MSE Listing Rules. With this step the number of the listed companies, whose corporate governance is affected by the obligation to comply with the MSE Listing Rules and that continuously disclose and notify the MSE for any changes thereof qualified by SL and MSE Listing Rules as price-sensitive information, is significantly increased.

Mandatory listing was introduced as an interim measure to boost the capital market and will apply until April 2018. Until then, all the companies that fulfil criteria for mandatory listing determined by the MSE Listing Rules on 31 December 2015 and 31 December 2016 are obliged by 30 April in the following year to file for request for listing on the mandatory-trading tier to the MSE. Furthermore, such companies cannot be excluded from the mandatory listing save in the case of liquidation or bankruptcy.

MSE Listing Rules are mandatory for all listed companies, and any default in complying with the Rules is sanctioned as a misdemeanour. Furthermore, MSE can render measures in case of non-compliance such as a warning and publication of the warning, suspension of the trading of the securities issued by the non-compliant company, transfer of the listed shares from one tier into another lower-trading tier and finally excluding the securities from listing. The last two measures cannot be rendered to listed companies on the mandatory-trading tier.

2 Responsible entities

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

The assembly of Macedonia adopts the statutory rules on corporate governance, by passing laws on the basis of proposals by the government.

There is no central agency for enforcement of corporate governance rules in Macedonia. Instead, most of the mandatory corporate governance rules are enforced through private litigation in civil courts.

The SEC has certain powers of enforcement in the context of securities trading and the disclosure obligations of reporting companies, taking into consideration its authorisation to monitor the legality and the efficiency of the capital market and the protection of investors' rights. The SEC acts ex officio or upon reports filed by shareholders or companies. The SL has introduced another mechanism for protection or implementation of the shareholders' rights related to trade transactions on the MSE, by providing for arbitration. The MSE has adopted the Arbitration Rules for resolving these disputes. Arbitration in settlement of disputes in connection with the company's charter is also stipulated with the LTC.

The MSE acts as a watchdog for the listed companies. The MSE Listing Rules have vested certain authorisations with the MSE if the listed company does not comply with the disclosure requirements or has contravened the Rules.

The rights and equitable treatment of shareholders

3 Shareholder powers

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

The members of the board of directors in the one-tier system, and the members of the supervisory board in the two-tier system, are elected at the shareholders' meeting by a majority of the voting shares from the quorum of the meeting, unless a greater majority is stipulated by the charter, in the manner and pursuant to the terms of the charter. If stipulated by the charter, the election of the members of the board of directors or the supervisory board may be carried out by cumulative voting, thus allowing the minority shareholders to have their nominee elected.

Executive members of the company are elected from among the members of the board of directors. The manner of election of the executive members of the board of directors is determined by the company's charter. The resolution for election of the executive members of the board of directors may be adopted unanimously by all the members of the board of directors. One of the executive members of the board of directors may be appointed as executive director, chief executive officer or with other title that will be compatible with the performance of the function that the executive member of the board of directors has. If the board of directors has more than one executive member, the members of the board of directors, with majority of votes, determine which one of the executive members shall be responsible for employee-related matters and relations with the employees.

If the company opts for a two-tier management system, the management board members are elected by the supervisory board in a procedure stipulated by the company's charter.

The shareholders' meeting may remove all the members of the board of directors, the supervisory board or a member thereof prior to the expiry of their term of office. The resolution for removal requires the same majority of the voting shares as in the case of electing these members, unless the company charter stipulates a greater majority. The charter may also stipulate additional terms for adoption of the resolution.

An executive member of the board of directors may be removed at any time by the board of directors, with or without an explanation, in which case the member shall be suspended until the next general meeting at which it shall be decided whether that member will be removed prior to the expiry of the term of office.

Shareholders representing at least one-tenth of the voting shares may request a meeting of the board of directors to be called. The request shall be submitted to the president of the board. If the president fails to call the meeting within 15 days after the filing of the written request, the members of the board of directors may call the meeting in the manner further provided in the LTC, thus allowing for the shareholders to have initiative rather than actual power to convene the meeting.

4 Shareholder decisions

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

The LTC makes a clear distinction of the corporate governance roles by vesting the powers of the shareholders' meeting to only pass resolutions upon issues expressly set out by the LTC or the charter, and excluding matters related to the operational governance or the management of the company's operations, which are under the competence of the management bodies, unless otherwise determined by the LTC.

The shareholders decide in particular about:

- the amendment of the charter;
- the approval of the annual accounts, financial statements and the annual report on the operations of the company for the preceding business year, and on the distribution of the profits and covering the losses;
- election and removal of members of the board of directors and of the supervisory board;
- approval of the operations and management of the company's business by the members of the management body and supervisory board;
- alteration of the rights attached to particular types and classes of shares;
- increase or decrease of the company's principal capital;
- issue of shares and other securities;
- appointment of the certified auditor to audit the financial statements, if the company is obliged to prepare them; and
- transformation of the company into another form of company and reorganisation and termination of the company.

The shareholders' meeting approves interested-party transactions and major transactions, if the thresholds for these corporate transactions as stipulated for in the LTC or in the company's charter are met.

There are no matters that are subject to a non-binding shareholder vote; however, the management board (ie, executive members of the board of directors) may differ resolving certain issues relating to corporate governance, which is subject to obtaining prior approval by the board of directors or the supervisory board to the shareholders' meeting, when the board of directors or the supervisory board fails to grant its consent.

5 Disproportionate voting rights

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

The 'one share, one vote' principle applies to Macedonian joint-stock companies.

Preferred shares with disproportionate voting rights, owned by Macedonia (state-owned shares), may grant specific rights under the condition of their issuance. By the entry into force of the LTC they cannot be transferred to third parties, unless they are converted into common shares.

The company may issue preferred shares as voting shares or as non-voting shares, provided that the total nominal value of the preferred non-voting shares does not exceed 30 per cent of the principal capital of the company. The total nominal value of the preferred shares, including both voting and non-voting shares, cannot exceed the total nominal value of the common shares in the principal capital of the company.

Issuance of shares of the same type that confer different voting rights for an identical nominal value is prohibited.

Limits on the exercise of voting rights are determined within the LTC when the shareholders' meeting resolves to exempt a shareholder personally from: a liability; payment of a receivable towards the company; or obligations. The shareholders' meeting may also resolve to grant the shareholder certain advantages or privileges by the company, or initiate court or other proceedings against the shareholder. In such cases, the shareholder cannot exercise its voting right personally or through a proxy representative.

If the shareholders' meeting is altering or restricting any right deriving from a certain type of shares, such resolution shall be considered valid if the shareholders holding that respective type of share give their consent through the adoption of a resolution for consent, passed with a majority determined by the LTC or the charter. These shareholders may vote or consent at a separate meeting or at the same shareholders' meeting with other shareholders present, but through a separate vote.

Consent by the owners of preferred shares shall be required for a resolution that cancels a preferential right, as well as for the issue of preferred shares that have priority in the distribution of profit or when making payment of a part of the remainder of the liquidation or bankruptcy estate of the company.

6 Shareholders' meetings and voting

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

Each shareholder that intends to participate in a shareholders' meeting is obliged to report its attendance at the meeting (registration for attendance) prior to the commencement of the scheduled meeting, which can occur, at the latest, moments before the meeting is due to start.

A list of registered shareholders is prepared by the management body and it is compared with the excerpt of the book of shares obtained from the Central Securities Depository (CSD) not later than 48 hours prior to the scheduled general meeting. This list is then signed by each present shareholder or his or her proxy representative, and it certifies his or her presence at the meeting (certified participant). Following the certification of the list, the chairman of the shareholders' meeting shall confirm that the meeting has an operating quorum.

The LTC stipulates the possibility for the reporting companies and listed companies to offer their shareholders at least one of the following means for participation in the shareholders' meeting:
- direct transmission of the meeting;
- two-way live audio and video communication, which allows shareholders to address the shareholders' meeting from any remote location; and
- electronic means for voting, before or during the meeting, without the necessity to authorise a proxy who would attend the session.

It can be stipulated in the company's charter that the voting of the shareholders at the shareholders' meeting may be performed by phone or another electronic device that is a part of the public communication network. In order to vote in such a way, the following must be determined with absolute certainty: the identity of each shareholder, the voting right, the communication network that will be used between the company and its shareholders that will make the voting available to each shareholder, and the means to record such voting. The shareholder who votes by phone or another electronic device is considered as present at the shareholders' meeting (ie, he or she will be considered as part of the quorum of the shareholders' meeting). The voting will be considered as null if the identity of the shareholder who voted by phone or other electronic device cannot be determined.

Voting by way of correspondence prior to the day of the shareholders' meeting may be made available to the shareholders. Before allowing the shareholders to vote by correspondence, the company may first ask the shareholders to confirm their identity by submitting personal ID documentation in original or copy, and without the obligation for the relevant copy to be certified by notary public or by domestic or foreign state authority. The company may use its own system of registration of shareholders as substitute for the procedure of identification of shareholders described above.

The shareholders are entitled to exercise their voting rights either in person or to delegate them to an authorised proxy by written power of attorney. Unless otherwise stipulated by the LTC, the proxy is given in written form, verified by a notary public. This requirement does not apply in reporting companies and listed companies where shareholders may appoint a proxy in writing without an obligation to verify by a notary. In such a case, the shareholder has to immediately notify the company for granting the proxy, default of which shall be considered that the proxy has not been granted.

In certain cases, the right to vote may not be exercised if the respective decision would lead to a conflict of interests for a particular shareholder, or if the decision concerns a possible claim against that shareholder.

7 Shareholders and the board

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

The management body of the company is entitled to convene a shareholders' meeting, if the interests of the company so require. Though not directly entitled, the shareholders may submit a request to the management body for convening a meeting, if they hold at least one-tenth of the voting shares. The management body decides on the convening of the meeting within eight days of the receipt of such a request. If the request is submitted by shareholders who own a majority of the voting shares, then the failure of the management body or the supervisory board to convene a meeting within 24 hours of the request, entitles the shareholders to file a request to the court. The right to convene the shareholders' meeting by the court is granted to the shareholders if the management body has not decided to commence the meeting within the term of eight days.

Shareholders who individually or jointly own at least 5 per cent of the total number of voting shares may request an amendment to the agenda by adding new agenda items for the convened shareholders' meeting, while simultaneously providing an explanation for the proposed item or proposing a draft resolution on the proposed item, within eight days from the date of publication of the agenda for the meeting. Such a request cannot be refused, except in certain cases strictly determined by the LTC, such as missing the deadline, or if the item does not fall under the competence of the shareholders' meeting.

In exercising this right, the shareholders may propose, inter alia, agenda items, resolutions and director nominations to be put to a shareholder vote.

The corporate body that convened the shareholders' meeting is obliged to send the request for the amendment of the agenda by adding new agenda items for the convened shareholders' meeting to all shareholders (ie, to publish it in the same manner in which the invitations for convening the shareholders' meeting were sent).

The body that convened the shareholders' meeting, that is the person determined by the court to convene the shareholders' meeting, shall send the request for including one or more points to the agenda of the convened shareholders' meeting to all shareholders, and shall publish it in the same manner in which the invitations were sent, no later than eight days prior to the date of the shareholders' meeting.

The LTC provisions governing the convening and holding of shareholders' meetings in reporting companies and listed companies require for the company to publish, without delay, the agenda and materials for the meeting, including draft resolutions proposed by the shareholders, on its website. The public announcement for convening shareholders' meetings in reporting companies and listed companies should contain a description of the procedures in accordance with which the shareholders participate and vote at the shareholders' meeting, and in particular how they can include points in the agenda of the shareholders' meeting and propose resolutions, how the shareholders can raise questions to the company regarding the points of the agenda of the shareholders' meeting and information regarding the time period in which they can do so.

A shareholder or a group of shareholders holding at least 10 per cent of the principal capital of the company, based on suspicion of possible irregularities in the keeping of the trade books and the activities of the company (ie, suspicion that the company acts contrary to the provisions of the LTC), has the right to request the management body to convene a shareholders' meeting of the company. At said meeting, an authorised auditor shall be appointed for performing audit, inspection, certification or related services within the scope of activities of the company regarding which the suspicion has been addressed in the request about the existence of possible irregularities. The shareholders may request the competent court to adopt a decision to appoint an authorised auditor if:

- the shareholders' meeting is not convened within a period of eight days as of the submission of the request referred to above;
- the shareholders' meeting refuses to appoint an authorised auditor; or
- the shareholders' meeting fails to adopt a decision for appointing an authorised auditor within a period of 60 days as of the submission of the request referred to above.

8 Controlling shareholders' duties

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

The LTC prohibits the controlling shareholder as a parent company from using its influence in order to mislead the subsidiary as a controlled company into undertaking harmful legal affairs, or undertake or fail to undertake actions, unless the parent company assumes the obligation to compensate the controlled company for any damages. If it fails to compensate the company for damages, then the controlling shareholder shall be jointly and severally liable with the controlled company with regard to the third party.

Enforcement action in such a case may be initiated in the name and on behalf of the controlled company or individually by the shareholders, regardless of the damages caused to them resulting from the damages caused to the controlled company.

If the parent company misleads the subsidiary as a controlled company to undertake legal operations or actions, thereby causing irreparable damage or bankruptcy, the parent will be jointly and severally liable for the claims that cannot be collected from the controlled company.

If the controlling shareholder misleads the company into undertaking a legal operation or action, or failing to undertake such an action or operation, thereby causing damage to shareholders of a controlled company, the controlling shareholder and the company shall be jointly and severally liable for the shareholder's claims.

However, no liability for compensation shall arise if the management of the company has acted with due care and diligence, thus undertaking the legal transaction as any management of an independent company would have undertaken or failed to undertake an equivalent legal transaction or operation without being misled by the controlling shareholder.

9 Shareholder responsibility

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

Shareholders cannot generally be held responsible for the acts or omissions of the company. The company itself is only liable to third parties for the obligation it has incurred with all of its assets. Only in a few exceptional cases, which the LTC singles out as special liability of the shareholders for the obligations of the company, may they be held jointly and severally liable if there is a major violation of good faith principles or the company's legal form has been used in order to carry out transactions and pursue objectives prohibited to them as individuals, or in an abusive manner to harm creditors, or the company's assets were used as if they were their own, contrary to the law, or the company's assets were decreased for their own benefit or for the benefit of a third party when they were aware or should have been aware that the company was not capable of settling its liabilities to third parties.

Piercing the corporate veil, except in these exceptional cases determined by the LTC, is not possible.

Corporate control

10 Anti-takeover devices

Are anti-takeover devices permitted?

Anti-takeover devices are generally not permitted within the scope of the Takeover Law. Before a takeover bid is published, the management may implement a number of measures based on shareholders' resolutions. These measures are designed to protect the company in the event of a hostile takeover and may include:

- converting ordinary shares into preference shares without voting rights (up to 50 per cent of the registered share capital);
- issuing new preference shares or convertible bonds; and
- providing for increased majority requirements for the removal of members of the management and supervisory boards.

The management body of the target company, in the course of conducting the takeover bid procedure, must act in the interests of the company as a whole and must not dissuade the holders of securities from the possibility of deciding on the advantages of the takeover bid. It should prepare a document expressing its opinion about the effect of the implementation of the bid over the employment and business operations of the company as stated in the takeover bid and the reasons on the basis of which it is adopted.

Once a takeover bid is published, and the management receives notification from the bidder, the Takeover Law imposes restrictions on the actions of the management body of the target company, by prohibiting, without a resolution passed by at least a three-quarters majority of the shareholders votes that represent the principal capital of the company at the time of the adoption of the resolution:

- an increase in its principal capital;
- the undertaking of activities other than the company's regular operations;
- the undertaking of activities that might jeopardise the company's future operations;
- the acquiring of treasury shares or securities resulting in the right to exchange or acquire treasury shares; and
- the performance activities that have the sole purpose to obstruct or aggravate the procedure and acceptance of the takeover bid.

The resolutions of the management on matters stipulated above adopted before the announcement of the intention to take over that are not completely implemented require additional approval by the shareholders' meeting of the target company before their implementation by at least a three-quarters majority of the shareholders' votes representing the registered principal capital, except in the case of resolutions that fall under the ordinary course of business of the company and whose implementation does not obstruct or aggravate the takeover bid.

11 Issuance of new shares

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

If provided in the company's charter, the management body may be authorised to increase the principal capital up to a certain nominal value (authorised capital) by the issue of new shares, for a maximum period of five years following the registration of the company's foundation, or five years following the entry of the resolution to amend the charter in the trade registry if such possibility was not stipulated by the charter.

The nominal value of the authorised capital may not exceed half of the principal capital at the time when the authorisation for the conditional increase of the principal capital was granted.

New shares may be issued only if the consent of the majority of the non-executive board of directors' members or the majority of the supervisory board members is provided. In such a case, it is the provision in the company's charter that has the legal effect of a resolution to increase the capital.

A pre-emptive right to subscribe for new shares exists in the LTC; however, the implementation of these provisions is postponed until Macedonia assumes full membership in the EU. Therefore, for the time being, in general, the shareholders do not have a pre-emptive right to acquire newly issued shares. Such right is granted in a limited number of cases, for example, when the shares are issued as private offer if the assumptions stipulated in the law are met.

12 Restrictions on the transfer of fully paid shares

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

LTC stipulates that shares are unlimitedly transferable and free to be traded with at the secondary securities market.

There are no statutory restrictions on the possibility to transfer shares, provided that encumbrances registered in the account of the shareholder maintained by the CSD may contain such restriction.

There are certain regulatory requirements that have to be met in order to have a valid and legal transfer, such as that the trade transactions should be carried out on the MSE, or requested documents for execution of non-trading transfers to the CSD must be presented.

Any encumbrance on shares restricting ownership rights and changes in the shares ownership rights are recorded in the CSD in the account of the shareholder, and may arise only from the act of issuance, a pledge, an effective court decision, an act of the SEC or an act issued by the Public Revenue Office.

Only shares that are free of any liens and restrictions may be the subject of settlement of transactions, except when the restriction applies to voting rights or dividends or another restriction that is not related to disposition and that is limited by a decision of a competent authority or an authorised person. If any right arising from the ownership of securities is restricted and evidenced in the shareholders' book maintained by the CSD, such securities may not be part of the procedure of clearance and settlement.

13 Compulsory repurchase rules

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

There are no compulsory share repurchase rules, save in the case of exercising dissenters' shareholder rights in the case of a merger, accession and division, and during transformation of the company, when the company is obliged to repurchase the shares of the shareholders who have not accepted the offer to receive shares, as a mandatory buyback.

The company may acquire treasury shares by way of repurchase, either itself or through a third party acting in its name but on behalf of the company, the validity of which is subject to the following conditions:

- a resolution for the acquisition of shares by repurchase should be granted by the shareholders' meeting, determining the manner of repurchase, the maximum number of shares to be acquired, the time period in which the repurchase shall be executed, which shall not be longer than a year from the date of adopting the resolution on the acquisition of the company's treasury shares, and the minimum and maximum value that may be paid for the shares;
- the nominal value of the acquired shares, including the shares the company has previously acquired or which are in possession of the company, shall not exceed one-tenth of the principal capital;
- the acquisition of the company's treasury shares shall not lead to the decrease of the assets of the company below the amount of the principal capital and the reserves, which, pursuant to the law or the charter, the company is obliged to maintain, and which shall not be used for payments to the shareholders; and
- only shares fully paid may be acquired via repurchase.

As an exemption, the company may acquire treasury shares when such acquisition is necessary in order to prevent serious and imminent damage to the company. The management body is authorised to adopt the resolution on such acquisition and is obliged to inform the shareholders' meeting at its next meeting of the reasons and the objectives of the implemented acquisition of treasury shares.

The share repurchase shall be carried out without application of the requirements determined above:

- if, on the basis of a resolution of the shareholders' meeting, the withdrawal of the shares is carried out in connection with the procedure for decrease of the principal capital;
- free of charge or when a bank, investment fund or other financial institution purchases shares in its own name out of the commission obtained from the purchase of the shares;
- as a consequence of the universal succession of the assets;
- in the enforcement procedure for settling of a company's claim on the basis of a court decision;
- in the case of a merger, accession and division, and during transformation of the company, if the company is obliged to repurchase the shares of the shareholders who have not accepted the offer to receive shares (mandatory buyback);
- in the case of exclusion of a shareholder;
- on the basis of an obligation stipulated in law or on the basis of a court decision; and
- as compensation for a debt or in a procedure of reorganisation of the debtor in accordance with the Law on Bankruptcy.

The company may be authorised by its charter to issue shares with the right of the company to repurchase such issued shares within a certain time period. The repurchase shall be valid if the following conditions are met:

- the terms and the manner of repurchase must be stipulated by the company charter;
- the shareholders' meeting shall adopt a resolution on the repurchase of such shares prior to their subscription;
- the shares should be paid up in full;
- the repurchase shall only be effected by funds that exceed the amount of the principal capital plus the reserves that may not be distributed to the shareholders under the LTC and the charter; and
- an amount that is not less than the nominal value of the issued shares shall be set aside into a reserve that shall not be distributed, under the LTC and the charter, except in the case of a decrease of the principal capital.

14 Dissenters' rights

Do shareholders have appraisal rights?

Under the LTC, shareholders have appraisal rights in certain situations – in the procedure for reorganisation of the company and the transformation of the company.

In certain cases of company reorganisation (acquisitions and mergers) and changes of legal form, a shareholder can sell his or her shares to the reorganised company for an appropriate cash compensation if the shareholder has formally objected to the reorganisation on the shareholders' meeting. A company shall buy back the shares at a price based on the adopted balance sheet as determined in the resolution for the transformation of a company (offered price) from a shareholder who, by way of a written statement, objected to the reorganisation of the company.

In a case of reorganisation, the shareholders are entitled to a court examination of the exchange ratio if the ratio has been determined to be too low, in which an additional payment may be requested that shall not exceed 10 per cent of the nominal value of the exchanged shares.

The adequacy of the cash compensation must be reviewed by the official auditor of the reorganisation.

Any dissenting shareholder can file an application with the court in order to assess the appropriate sum.

In squeeze-out proceedings, the minority shareholders must be granted appropriate compensation for their shares, under the same conditions under which the takeover was carried out.

The responsibilities of the board (supervisory)

15 Board structure

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

The predominant board structure for listed companies is the one-tier structure.

Out of 108 companies listed on the MSE, 67 companies have a one-tier management system and the other 41 have a two-tier management system.

16 Board's legal responsibilities

What are the board's primary legal responsibilities?

The board of directors manages the company within the scope of the authorisations provided for by the law and the charter and the authorisations expressly granted by the shareholders' meeting. The board of directors has the broadest authorisations in managing the company within its scope of operations and acts, in all circumstances, on behalf of the company, except for matters falling within the authorisations explicitly granted to its non-executive members.

With the exception of the authorisations explicitly granted to the board of directors pursuant to the law, the executive members manage the company's operations and have the broadest authorisations to undertake all matters related to the management, implementation of the board of directors resolutions and execution of the day-to-day activities of the company, as well as to act on behalf of the company in all circumstances. The board of directors entrusts the representation of the company in relations with third parties to its executive members. The non-executive members, in addition to the authorisations provided for by the LTC concerning the exercise of the right of supervision over the executive members' management, is entitled to inspect and verify the books and documents of the company as well as its assets and, in particular, the petty cash of the company and its securities and goods.

In the two-tier management system, the management board undertakes all matters related to the management, the implementation of resolutions and the execution of the day-to-day activities of the company, as well as acting on behalf of the company in all circumstances, while the supervisory function is vested in the supervisory board.

There are certain issues that the executive members (ie, the management board) cannot resolve without obtaining prior consent of the board of directors or supervisory board, respectively. These concern the registered scope of activities or the establishment or termination of long-term cooperation or capital investments that involve more than 10 per cent of the income of the company, as well as essential internal organisational changes in the company, establishment and termination of branch offices, decrease or expansion of the scope of business operations and establishment and termination of a trade company participating in the principal capital of the company with more than one-tenth in the principal capital of the company.

17 Board obligees

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

The management board (ie, the executive members of the board of directors) represents the company in relation to third parties while the supervisory board (ie, the non-executive members of the board of directors) represents the company in relation to its management board (the executive members). All members of the management board (ie, the board of directors) are under a general duty to manage the company with the due care of a prudent and diligent manager and in the best interests of the company and all the shareholders. The supervisory board is also under a general duty to control the management, which it owes to the company and its shareholders.

The duties of the management board and of the supervisory board (ie, the board of directors) are primarily owed to the company and are carried out in the interests of all shareholders.

18 Enforcement action against directors

Can an enforcement action against directors be brought by, or on behalf of, those to whom duties are owed?

Members of the management body who violate their legal duties by failing to apply the care of a prudent and diligent manager are jointly and severally liable to the company for damages caused, unless the respective action was based on a legal and valid resolution of the general meeting, or the member of the management body has opposed such a resolution and voted against the course of action. Under specific conditions stipulated in the LTC, shareholders may file for a claim for the damages suffered by the company by the management bodies. The non-executive members of the board of directors, or the members of the supervisory board, shall be jointly and severally liable with the executive members of the board of directors or the members of the management board for the damage caused, if they failed to act with due care and diligence when giving their prior consent.

Neither the management body nor the supervisory board, however, can be held liable for the poor performance of the company based on entrepreneurial business decisions taken with the due care of responsible managers, even if these decisions subsequently turn out to be failures (business judgement rules).

19 Care and prudence

Do the board's duties include a care or prudence element?

All members of the management bodies are under a general duty to fulfil their duties pursuant to the authorisations granted to them by the law or charter, in the interests of the company and all the shareholders with the due care of a prudent and diligent manager.

Set as a legal standard, due care and diligence determines the responsibilities of persons in charge of the management and supervision of companies and the care which these persons should apply while executing entrusted tasks in the company and the requirement that they act in a diligent manner (in the operations of the company) as skilled (professional) persons, pursuant to which they shall be liable for negligent behaviour while executing operations with which they have been entrusted, unless another law specifies that they shall only be liable for gross negligence.

20 Board member duties

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

Formally, all members of the management bodies represent and manage the company collectively and are jointly responsible for all business areas, irrespective of individual skills and experience. Internally, however, the members of the management bodies are in most cases entrusted with different operational responsibilities.

The Corporate Governance Code recommends making a provision for the division of duties within the management body or the supervisory board and describing the procedure of the management body or the supervisory board in the charter and other acts of the company. Also, it is recommended that the board of directors or the supervisory board should include in its regulations a paragraph dealing with its relations with the management board or executive directors, the external certified auditor and the shareholders' meeting.

It further recommends that the management body or the supervisory board defines and proposes a profile of its members and the size and composition of the management body or the supervisory board, taking into account the nature of the business, its activities and the desired expertise and background of members of the management body or the supervisory board. At least one of the non-executive members of the board of directors or one member of the supervisory board must be a financial expert. The annual report should disclose the name of this member of the management body or supervisory board.

21 Delegation of board responsibilities

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

A member of the management body or supervisory board may not transfer his or her authorisations to another member of the management body or supervisory board.

When performing duties granted pursuant to the law and the company's charter, the member of the management body or the supervisory board may rely on information, opinions or reports prepared by independent legal advisers, independent authorised accountants and certified auditors and other persons, believed to be trustworthy and competent for the matters they perform, but this shall not exempt the member from the obligation to act with due care and diligence.

The executive members of the board of directors manage the operations of the company and have the broadest authorisations to undertake all matters related to the management, implementation of the decisions of the board of directors and realisation of the day-to-day activities of the company (save for the authorisations explicitly awarded to the board of directors in accordance with the LTC) and act on behalf of the company in all circumstances. For the purpose of exercising these authorisations, the executive members can appoint managerial persons who shall run the daily management of the activities of the company, in accordance with the decisions, directions and orders of the executive members of the board of directors.

In a two-tier management system, the members of the management board jointly represent the company in its relations with third parties, unless otherwise determined by the company's charter. The management board, with an approval of the supervisory board, can authorise one or more members of the management board to represent the company. In that case, the other members of the management board shall be excluded from the representation. The supervisory board can at any time revoke the representation authorisation.

22 Non-executive and independent directors

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

A board of directors may have a minimum of three and a maximum of 15 members. The general rule is for non-executive members to outnumber executive members. If the board of directors has up to four non-executive members, at least one of them shall be an independent member. If the board of directors has more than four non-executive members, at least a quarter of them shall be independent members of the board of directors. The same ratio applies for the supervisory board structure.

'Independent non-executive member' means a natural person who, along with their family members:

- has not had any material interest or business relation with the company directly as a business partner, a member of the management body, supervisory body or an officer of the company within the five preceding years;
- has not, within the five preceding years, received and does not receive from the company any additional income to his or her salary;
- is not related to any of the members of the management body, supervisory board or the officers of the company; and
- is not a shareholder who owns more than one-tenth of the shares in the company or who represents such a shareholder.

The definition of the 'non-executive member of the board of directors' stipulates that such a member is a natural person, a member of the board of directors who has no executive function in the company and whose powers refer primarily to the general governance and supervision over the management of the company.

General governance and supervision over the management of the company is the distinction with the responsibilities of the executive directors.

23 Board size and composition

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

A board of directors may have a minimum of three and a maximum of 15 members, while in the one-tier management system, the number of the members of the management board and the supervisory board is at least three and at most 11 members in each management board and the supervisory board. Notwithstanding the above, the companies that have principal capital lower than €150,000 may appoint a manager instead of a management board. The structure of the board of directors (ie, the management board and the supervisory board) is determined by the company's charter.

Prior to the election of a member of the board of directors or the supervisory board, certain disclosure requirements should be met by publishing, in writing, data regarding the age, gender, education and other professional qualifications, working experience and how it was gained, in which companies he or she is or has been a member of the management body or the supervisory board and other important positions held by him or her, the number of shares he or she owns in the company and in other companies, as well as loans and other liabilities owed towards the company.

Members of the management bodies of the reporting companies have an obligation to disclose to the SEC any shareholding they have in the company, as well as any further changes by submitting an ownership report.

Listed companies have further disclosure requirements for their members of the management bodies, related to the number of shares with voting rights as well as the percentage of the total number of shares issued by the company that they represent, within 14 days of their election, as well as ongoing disclosure requirements for the sale of company shares by the members of the management bodies of the value of €10,000 or higher during one trading day, the cumulative value of all purchases (or sales) of shares of the value of €10,000 or more within 30 calendar days, and every purchase or sale of shares representing 0.5 per cent of the total voting shares of the company.

The Central Registry of the Republic of Macedonia maintains a register on persons who cannot be members of management bodies. The negative criteria imposed by the LTC, which are the basis for entry in this registry, are related to previous managing functions in insolvent companies until bankruptcy proceedings have been initiated, as well as anyone who has been found guilty with enforceable court decisions of false bankruptcy or damaging creditors and who have been punished with a ban on performing such an activity, profession or duty, while the legal consequences of such a ban are still in force.

If certain members of the board of directors, that is the supervisory board, stop to perform their duties during their mandate, or there is an obstacle to their performing their duties, the other members continue with the work of the relevant board until the fulfilment of the empty spot by the shareholders' meeting. If the number of members of the board of directors that is the supervisory board is decreased under the minimum determined with the charter, but no lower than the minimum required by the law, the board of directors that is the supervisory board may, in the period of 90 days from the day of termination of the function of the relevant member, fill the empty spot by the appointment of an acting director – a member of the board of directors that is the supervisory board until the following shareholders' meeting. The resolutions passed by the board of directors (the supervisory board) during this period shall remain valid. If the number of members of the board of directors (supervisory board) decreases below the minimum required by law, the remaining members must, within a period of three days, convene a shareholders' meeting in order for the number of members of the board of directors (supervisory board) to be in accordance with the law. If the shareholders' meeting is not convened in this three-day period, than the meeting shall be convened by the non-executive members of the board of directors (that is the management board), within a period of three days from the expiry of the previously given period. If the number of the members of the board of directors (supervisory board) is not filled in the manner described above and within the deadlines provided by law, then any person with legal interest may request the court to appoint an individual who will convene the shareholders' meeting for appointment of a member of the board of directors (supervisory board).

24 Board leadership

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

Corporate governance rules in Macedonia require separation of the functions of board chairman and CEO. In companies with a one-tier management system, the president of the board of directors (board chairman) is elected from the non-executive members of the board of directors. One of the executive members of the board of directors may bear the title that is typically associated with the performance of his or her duties (general director, or chief executive director, or other appropriate titles), and the other executive members may bear the title that is typically associated with the performance of their duties, entrusted to them as executive members of the board of directors.

In the two-tier management system, the management board and the supervisory board have their own presidents. The president of the management board, appointed by the supervisory board, coordinates the work of the management board and assumes certain representative functions, and has a casting vote in the case of a tie, unless otherwise stipulated in the company's charter.

The company's charter may provide for additional rights and responsibilities of the presidents of the managing bodies and the supervisory board.

25 Board committees

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

In accordance with the LTC, the management body or the supervisory board may establish one or more committees from among its members and other persons. The committees shall neither decide on issues falling under the competence of the management body or the supervisory board, nor shall their rights and liabilities be transferable. The composition, terms, the scope and the manner of operations of such committees shall be regulated in detail by the charter and the by-laws of the company adopted in accordance with the charter. All activities of the committees shall be subject to approval by the management body or the supervisory board.

The Corporate Governance Code entitles the board of directors or the supervisory board to consider whether to appoint a selection and nomination committee, an audit committee and a remuneration committee. Its best-practice provisions stipulate that the members of the committees appointed by the board of directors or the supervisory board cannot be executive members of the board of directors or management board members. Within the committees, at least one of the members is an independent member of the board of directors or the supervisory board.

26 Board meetings

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

The LTC obliges the board of directors and the supervisory board to convene at least four regular meetings during the year, one every three months, provided that one of the meetings is convened within one month prior to convening the annual general meeting of shareholders.

27 Board practices

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

The board of directors and the supervisory board must present a written report to the annual general meeting of the shareholders setting forth, inter alia, how and to what extent it has supervised the activities of the management body during the business year.

The executive members of the board of directors and the members of the management board submit a written report on the operations of the company to the board of directors or the supervisory board at least once every three months and they shall also submit annual accounts, annual financial statements and an annual report on the company's operations, following the expiry of the business year.

Upon request by the non-executive members of the board of directors or the supervisory board, the executive members of the board of directors and the members of the management board shall prepare a special report on the state of affairs of the company or on particular issues related to its operations.

28 Remuneration of directors

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

The statutory provisions determine that the shareholders' meeting must pass a resolution specifying the monthly lump sum or lump sum per meeting of the non-executive members of the board of directors or the supervisory board members. The non-executive members of the board of directors or the supervisory board members have the right to reimbursement of all their expenses incurred (travel and other expenses), a right to life insurance and other types of insurance, as well as other rights related to the performance of their function (usage of the business premises, necessary assets for operation, etc).

The executive members of the board of directors and the members of the management board are entitled to a salary, or a monthly remuneration, a right to life insurance and other types of insurance, compensation of travel and other expenses and other rights. The executive members of the board of directors and the members of the management board may enter into managerial agreement with the company, determining in more detail their rights and obligations. Regarding specially entrusted matters, performed for the company by a member of the management body or a member of the board of directors, an additional bonus may be granted to that member and paid out of the operating costs.

The company may not grant a credit to a member of the management body or the supervisory board, their close family members, or to a member of the management body or the supervisory board of a controlled company or to their close family members. The prohibition shall not apply to the obligations assumed by the company pursuant to the managerial agreement if a resolution has been approved by the shareholders' meeting to this effect with a two-thirds majority of the voting shares represented at the general meeting.

Members of the management bodies and supervisory board members are elected for a term as stipulated in the company charter, which cannot be longer than six years. If the company charter does not stipulate the term of office, then it is a legal assumption that they are elected for a term of four years. Each of the members may be re-elected, regardless of the number of terms of office they have been previously elected for, unless otherwise determined by the company's charter.

Transactions between the company in which the members of the management bodies and the supervisory board members have an interest are considered interested-party transactions, for which a special corporate approval procedure applies. A default in the procedure for approving the transaction may lead to its nullity, and exposes the interested parties to liability for damages if the transaction is proved to be harmful for the company.

29 Remuneration of senior management

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

There are no requirements regarding the remuneration of senior management. The company cannot grant credit to members of the board of directors, the supervisory or management board or their close family members. Exceptions are stipulated obligations undertaken with the managerial agreement, confirmed by a resolution of the shareholders' meeting, with a two-thirds majority of the votes.

Transactions between the company and senior managers are subject to interested-party transaction provisions. General conflict-of-interest provisions apply.

30 D&O liability insurance

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

The company may agree to pay insurance premiums as part of its contractual arrangements with the directors or officers. Liability insurance is not restricted but is rare in practice. It is also subject to the availability of products by the local insurance companies.

Update and trends

With the entry into the post-election period, as of December, 2016, there have been no proposals for new legislation or secondary regulation in the country. This is a welcome pause in the frequent amendments to the relevant legislation, as it will allow for the provisions affecting important themes such as interested-party transactions, shareholders' duties, and in general, the concept of corporate governance matters to be absorbed. We note that some of the practices have not been developed, and neither has a doctrine on certain aspects. Therefore, it may be the subject of further modifications and amendments.

The focus has shifted from legislation changes to addressing the current corporate governance trends in the Corporate Governance Code for Companies listed on the MSE. A working group comprised of the Macedonian Stock Exchange, Securities and Exchange Commission and Institute of Directors prepared a revised draft of the Corporate Governance Code addressing the need for a sustainability agenda for the private sector. With the aim of preparing a Corporate Governance Code that includes oversight of environmental and social risks in the Western Balkans region, the working group is determined to include social and environmental questions in the Corporate Governance Code.

31 Indemnification of directors and officers

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

Generally, only the company can be held liable by third parties for the actions of its management on behalf of the company. Personal liability of management body members in relation to third parties is very rare and mainly limited to damages from tort and breach of certain statutory management duties with gross negligence.

If a member of the management body grossly violates his or her obligation to act with due care and diligence, the creditors of the company may request compensation for damages if they fail to settle their claims against the company.

32 Exculpation of directors and officers

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

The LTC stipulates joint and several liability of the management body members for the damage caused as joint debtors towards the company if they violate their obligations and fail to operate and act with due care and diligence. If a member of the management body grossly violates his or her obligation to act with due care and diligence, the creditors of the company may request compensation for damages if they fail to settle their claims against the company. The non-executive members of the board of directors or the members of the supervisory board shall be jointly and severally liable with the executive members of the board of directors or the members of the management board for the damage caused if they failed to act with due care and diligence when giving their prior consent.

Liability in relation to the company cannot be precluded or limited, either in the charter or in a private agreement.

However, the member of the management body who acted on the basis of a resolution adopted by the shareholders' meeting although he or she had pointed out that the resolution was contrary to the law, as well as the member of the management body who objected to the resolution by setting out his or her opinion in the minutes of the meeting of the management body in a separate manner and voting against the resolution, shall not be held liable.

Under the Law on Obligations, the company is liable towards third parties for the damage cause by its management bodies in the performance of their functions in the management of the company. If the damage is caused by wilful action or gross negligence, the company is entitled to compensation from the member of the management bodies who caused the damage to the third party.

Further, the liability of employees in relation to their company can be limited as long as the employee acts within his or her professional capacity. If these conditions are met, an employee can also be entitled to be discharged from third-party liability by the company. If the damage is caused by wilful action or gross negligence, the company is entitled to compensation from the employee who caused the damage to the third party. Since members of the management bodies (executive members or the management board members) are usually employees of the company, these principles apply to them.

33 Employees

What role do employees play in corporate governance?

When determining the management systems of the joint-stock company, the LTC stipulates that the participation of the employees in the management of the company shall be stipulated by law.

However, there is no such law adopted as yet, therefore the employees' participation in the corporate governance is not yet regulated by Macedonian law.

There are provisions in the LTC that stipulate the possibility for the company in its charter to create a fund from which the employees can acquire shares in the company for free or at a discount price, up to one-tenth of the principal capital of the company. This option for the companies has been effective since 1 January 2012, and it was intended to have employees as active participants in the shareholding structure of the company through their participation in and voting at the shareholders' meeting. However, up to the present time, there is no relevant practice to show whether this provision has been implemented by companies.

34 Board and director evaluations

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

The Corporate Governance Code for Companies listed on the MSE through its 'best-practice provisions' encourages periodical self-evaluation of the members of the management and supervisory board (ie, the board of directors) in listed companies.

There is no requirement to publicly disclose anything in relation to such evaluations.

In any case, the shareholders have the final say in evaluation of the members of the management body as a whole and for each member individually. The annual shareholders' meeting is obliged to decide on approving the work and the management of the company by the members of the management body and the work of the members of the supervisory board. Voting on the approval of the work of members of the company's management bodies is done separately for each member of the management bodies.

If the annual shareholders' meeting does not approve the work of the management body or supervisory board or the work of the members thereof, it can decide to elect all the members of the management body or elect new members of these bodies to replace those whose work was not approved. This decision must be made at the same annual meeting.

Listed companies are obliged to publish the decisions on approval or non-approval of the work of the management body adopted at the shareholders' meeting on the MSE.

Disclosure and transparency

35 Corporate charter and by-laws

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

The company is obliged to keep the charter and the other by-laws and all amendments thereto along with the consolidated texts at the company's premises, and each shareholder is entitled to inspect the corporate documents of the company, in a manner set forth in the company charter.

A copy of the company charter may be obtained from the trade registry maintained by the Central Registry; however, there is no requirement to publicly disclose the by-laws of the companies.

36 Company information

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

The disclosure requirements of a company depend on the status the company has in accordance with the SL, whether it is a listed company, reporting company or joint-stock company that is not registered in the register of joint-stock companies with special reporting obligations maintained by SEC.

The information reporting companies disclose includes:

- the annual financial statements, the management reports and interim reports;
- the issuance of a new shares and dividends policy;
- information on certain shareholding thresholds being exceeded by a single shareholder (5 per cent of the voting shares), and information regarding the members of the management bodies, including their respective percentage ownership in the principal capital; and
- information about interested-party transactions entered into by members of the management board or the supervisory board and the affiliated entities of the company.

Reporting companies comply with the disclosure requirements by submitting to the SEC annual and semi-annual reports. Such a company must also immediately disclose any price-sensitive information, that is, all circumstances that are not yet public knowledge, but which may have a significant influence on the share price if they become public information (ad hoc disclosure). Listed companies must annually deliver to the MSE a comprehensive report outlining whether and to what extent the company complies with the recommendations of the Corporate Governance Code, and give reasons in the case that recommendations were not applied (compliance statement).

In general, listed companies are obliged to immediately publish:

- certain information on business operations (eg, signing or cancelling a significant contract that has a value of 10 per cent or more of the capital of the company, determined on the basis of the last audited annual financial statements);
- certain information related to the capital (increase or decrease of the principal capital, change of the rights deriving from the issued shares, etc);
- important changes in their financial situation (acquisition or disposal of 5 per cent or more of the assets of the company determined on the basis of the last audited annual financial statements, adopted decisions regarding interested parties transactions and the opinion of the auditor, if the value of the transaction or the cumulative value of interconnected transactions over the past 12 months is or exceeds 10 per cent of the assets of the company, etc);
- their dividend calendar;
- notifications regarding publicly held shares; and
- notifications regarding the shareholders' meeting.

These companies should further publish a notification regarding all changes in ownership in which certain owners have acquired 5 per cent of the voting shares. This notification must state the identity of the new owners, the number of shares and the new percentage of voting rights. The LTC further stipulates that listed companies must publish a notification on every performed interested-party transaction, in at least one daily newspaper, on the company's website and on the MSE website, immediately or the next business day, at the latest.

Further to this, the MSE Listing Rules stipulate specific disclosure obligations for certain companies depending on which trading tier on the official MSE market their shares are listed.

Joint-stock companies that are not listed on the MSE and are not registered as reporting companies are obliged to publish data concerning total revenues, before tax, profit for the business year, net cash flow, profit per share for the business year and dividend per share, changes in ownership structure over 10 per cent, reorganisation of the company, changes in management and governance, new issuance of shares as well as price-sensitive information on the web page of the MSE.

Hot topics

37 Say-on-pay

Do shareholders have an advisory or other vote regarding executive remuneration? How frequently may they vote?

Under the LTC, the shareholders generally do not have a say in the determination of executive remuneration, the only exception being when deciding on the executive members or the manager's right to participate in the profit. Such participation, as a general principal, consists of a share in the annual profit of the company (payment in cash, shares, royalties, bonuses or in another manner).

The approved participation in the annual profit of the company shall be calculated on the basis of the portion of the annual profit of the company that remains after the reduction of the realised profit for the amount of the total losses transferred from the previous years, and the amounts are set aside as legal and statutory reserves. A resolution contrary to this provision shall be null and void. Though not explicitly stipulated, from the manner in which the approved participation is determined it is evident that the shareholders may resolve upon on the annual meeting of the shareholders.

Further involvement of the shareholders in the executive remuneration may be stipulated in the managerial agreement, by determining the situations when the financial condition of the company shall be deemed to be significantly deteriorated, owing to which the earnings of the executives present a burden to the company and on the basis of which the shareholders' meeting, the non-executive members of the board of directors, or the supervisory board may reduce the total earnings and other rights of the member of the management body.

The remuneration of the members of the board of directors and supervisory board is subject to regulation in the charter or a shareholders' resolution. There is no explicit provision determining the frequency of voting when resolving on the remuneration of the members of the board of directors and supervisory board.

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38 Shareholder-nominated directors

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

Any shareholder may nominate directors in the joint-stock company. Considering the majority for election of the members of the board of directors in the one-tier system, and the members of the supervisory board in the two-tier system as a majority of the voting shares from the quorum of the meeting, it is most unlikely that without the required majority owned by the nominating shareholder the nominee would be elected. If stipulated by the charter, the election of the members of the board of directors or the supervisory board may be carried out by cumulative voting, thus allowing the minority shareholders to have their nominee elected.

The listed and reporting companies are required to publish and make available all resolutions that are proposed under each of the items of the agenda, as well as all the materials for the convened shareholders' meeting on their official websites, including the proposed resolutions regarding the appointment or revocation of directors (ie, members of the board of directors in the one-tier system and the members of the supervisory board in the two-tier system).

For the companies that are neither listed on the MSE nor have reporting obligations, the requirement is to provide information on how the materials and documents for the convened shareholders' meeting will be made available to the shareholders in the invitation (ie, the public announcement for convening the shareholders' meeting).

39 Shareholder engagement

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

Shareholder engagement occurs in shareholders' meeting sessions.

In accordance with the LTC, each shareholder has the right to raise questions on each of the points on the agenda, and the company is obliged to respond to questions raised by the shareholders, through its management bodies or a senior officer who covers the particular matter to which the question is addressed. The right of shareholders to raise questions and the obligation of the company to answer such questions can be preconditioned by the need to verify the personal identity of the shareholders raising the questions, maintain the order in chairing and operation of the shareholders meeting session, or to undertake actions in order to preserve the confidentiality of the work and the business interests of the company. The company can give a collective response to questions with the same content. Questions raised by shareholders are considered to be answered if the answers are available on the web page of the company in the questions and answers form.

The LTC provisions governing the convening and holding of shareholders' meetings in reporting companies and listed companies require the public announcement convening shareholders' meetings to contain a description of the procedures in accordance with which the shareholders participate and vote at the shareholders' meeting, and in particular how they can include points in the agenda of the shareholders' meeting and propose resolutions, how the shareholders can raise questions to the company regarding the points of the agenda of the shareholders' meeting, and information regarding the time period in which they can do so.

Nigeria

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Sources of corporate governance rules and practices

1 Primary sources of law, regulation and practice

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

The main sources of law relating to corporate governance are as follows:
- the Companies and Allied Matters Act 1990 (CAMA);
- the Investment and Securities Act 2007 (ISA);
- the Financial Reporting Council of Nigeria Act 2011 (FRCA);
- the Banks and Other Financial Institutions Act 1991 (BOFIA);
- the Central Bank of Nigeria Code of Corporate Governance for Banks and Discount Houses in Nigeria (the CBN Code);
- the Insurance Act 2003;
- the National Insurance Commission Act 1997 (the NAICOM Act);
- the NAICOM Code of Corporate Governance for the Insurance Industry in Nigeria (the NAICOM Code);
- the Code of Corporate Governance for Licensed Pension Operators (the PENCOM Code);
- the Nigerian Stock Exchange Listing Requirements (the Green Book);
- the Securities and Exchange Commission Code of Corporate Governance in Nigeria (the SEC Code);
- the Securities and Exchange Commission Rules and Regulations (the SEC Rules);
- the SEC Code of Conduct for Shareholders' Associations (SCCSA); and
- the Nigerian Communications Commission Code of Corporate Governance for telecommunication companies (the NCC Code).

The Green Book requires mandatory compliance with listing rules.

2 Responsible entities

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

The primary government entities responsible for making such rules are:
- the Corporate Affairs Commission (CAC), created under CAMA, which oversees the registration of companies and compliance by corporate bodies with the provisions of CAMA;
- the Securities and Exchange Commission (SEC), created under the ISA, which regulates the capital market;
- the Central Bank of Nigeria (CBN), which regulates banks and other financial institutions in Nigeria;
- the National Insurance Commission (NAICOM), established under NAICOM Act 1997, which ensures compliance by insurance companies with the provisions of the NAICOM Act and the Insurance Act;
- the National Pension Commission established under the Pension Reform Act, which regulates Pension Fund Administrators and Pension Fund Custodians; and
- the Financial Reporting Council of Nigeria (FRCN), created under the FRCA, which is empowered to enforce and approve compliance with accounting, auditing, corporate governance and financial reporting standards in Nigeria. The FRCN is charged with ensuring good corporate governance practices in the public and private sector. The Directorate of Corporate Governance, created under the FRCA, has the responsibility to issue the code of corporate governance and guidelines and to develop a mechanism for periodic assessment of the code and guidelines.

There are several shareholder activist groups in Nigeria. These include: Progressive Shareholders' Association of Nigeria (PSAN), Lagos Zone Shareholders' Association, Renaissance Shareholders' Association, Association for the Advancement of the Rights of Nigerian Shareholders, the Independent Shareholders' Association of Nigeria (ISAN), Dynamic Shareholders' Association of Nigeria, Nigerian Shareholders' Solidarity Association, Proactive Shareholders Association of Nigeria and the Pacesetter Shareholders' Association of Nigeria. The various groups are more active in participating in annual general meetings, influencing decision-making at such meetings and protecting shareholders' rights.

It should be noted that the regulatory authorities such as the SEC and the FRCN adopt a consultative process in making regulations in order to obtain the views of various stakeholders, including shareholder groups. The SCCSA is one of the means through which the SEC seeks to ensure the highest standard of conduct among association members and the companies with which they interact as shareholders and to ensure that association members make positive contributions in the affairs of public companies. The SCCSA prescribes that shareholders' associations be registered with the CAC in order for their views to be considered by the SEC during consultations on corporate governance issues.

The rights and equitable treatment of shareholders

3 Shareholder powers

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

Shareholders in a general meeting have the power to appoint or remove directors by way of a resolution. Though the board of directors of a company is empowered to appoint new directors to fill casual vacancies created by death, resignation, retirement or removal, such appointments are, however, subject to ratification by the shareholders in a general meeting. Generally, unless the articles of association provide otherwise, the directors, when acting within the powers conferred upon them by CAMA or the articles, are not bound to obey the directions or instructions of the shareholders in general meetings provided the directors act in good faith and with due diligence. This notwithstanding, the shareholders may make recommendations to the board regarding actions to be taken by the board and may ratify or confirm any action taken by the board. The SEC Code provides that the board is to ensure that all shareholders are given equal treatment and minority shareholders are adequately protected from the abusive actions of controlling shareholders. Also, there should be adequate shareholder representation on the board proportionate to the size of shareholding.

A shareholder can bring a court action to restrain the directors from entering into an illegal or ultra vires transaction, or perpetuating a fraud. Members holding 5 per cent of the total voting rights in the company could circulate a resolution to be voted upon at a general meeting, indicating a course of action that should be adopted by the directors of the company.

The votes required to elect a director are a simple majority of the votes cast by shareholders of a company either in person or by proxy at a general meeting.

Under CAMA, a company may, by ordinary resolution, remove a director before the expiry of his or her tenure of office, notwithstanding anything in its articles or in any agreement between the company and the director. By ordinary resolution, the votes are a simple majority of the votes cast by shareholders of a company either in person or by proxy at a general meeting. However, CAMA requires that a special notice be given to the company in order to move such resolution, which must be provided no less than 28 days before the meeting at which the resolution is to be moved. The company shall also give its members notice of such resolution at a minimum of 21 days before the meeting where the removal of the director is to be considered.

4 Shareholder decisions

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

The shareholders in a general meeting are empowered to appoint and remove directors of the company, determine directors' remuneration, appoint auditors and approve their remuneration, alter the company's share capital, alter the memorandum and articles of association of the company, approve the conversion of the company from a private to a public company and vice versa, and from a limited company to an unlimited company and vice versa, change the company's name and declare a dividend on the recommendation of the board.

CAMA provides that, subject to the provisions of the articles of association of a company, there are certain powers of the board that cannot be restricted by the shareholders in a general meeting. These include powers over the day-to-day running of the company and the powers of the directors to institute actions on behalf of the company. Where the board fails to institute or defend an action on behalf of the company when it ought to do so because the board is itself in the wrong or there is a deadlock on the board, then the shareholders may apply to court to bring the action on behalf of the company.

Where the articles of association of a company expressly vest the board with certain powers, it cannot be bound to obey the instructions of the shareholders especially when it acts in good faith and with diligence. In such situations, the shareholders may only amend the articles of association of the company such that those powers are now made exercisable by the shareholders in a general meeting and not by the board of directors.

5 Disproportionate voting rights

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

CAMA expressly prohibits disproportionate voting rights and the limitation of voting rights. The basic rule is 'one share, one vote' and no company may by its articles or otherwise authorise the issue of shares that carry more than one vote in respect of each share or that do not carry any rights to vote. There are, however, a few exceptions. Preference shareholders, if the articles of the company so provide, can have more than one vote per share:

- upon consideration of any resolution where a dividend on the preference share remains unpaid after the due date of the dividend;
- upon any resolution that seeks to vary the rights attached to the preference shares;
- upon any resolution to appoint or remove an auditor; and
- upon any resolution for winding up the company.

Also, any special resolution of a company increasing the number of any class may validly resolve that any existing class of preference shares carry the right to such votes, in addition to the one vote per share necessary to preserve the existing ratio that the votes exercisable by the holders of such preference shares bear to the total votes exercisable at the meeting. The right of members to vote upon their share may also be limited by the company's articles until all calls or other sums payable to the company by them in respect of the shares have been paid.

6 Shareholders' meetings and voting

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

All shareholders are entitled to attend and vote at the company's general meeting. It should be noted, however, that until the name of a person having shares in a company has been entered as a member in the register of members, which companies are statutorily required to maintain, such person will not be deemed a member of the company and may therefore not attend meetings of the company or be allowed to vote at such meetings.

The articles of a company may also provide that members who have not made payments on all calls on their shares shall not be entitled to attend meetings.

Shareholders of a private company can act by way of written resolution. CAMA provides that a resolution of the shareholders of a company would be effective only if it is passed at a general meeting. However, the shareholders of a private company may act by a written resolution signed by all the shareholders entitled to attend and vote at the general meeting of the company where the resolution would have been passed.

CAMA does not provide for virtual meetings. By the provisions of CAMA, all statutory and annual general meetings shall be held in Nigeria and the notice calling for such meetings should contain the place for the meetings. An extraordinary general meeting has no such restrictions and therefore can be a virtual meeting. In practice, a company may provide for the holding of virtual meetings in its articles of association.

7 Shareholders and the board

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

The duty to call general meetings of shareholders is one held by the board of directors. However, a shareholder or shareholders representing at least one-tenth of the shareholding (or voting rights in a company not having share capital) of the company may requisition a general meeting at any time. Where the board refuses to convene the requisitioned meeting within 21 days, the requisitionists are authorised to convene the meeting (within three months of the requisition) after issuing the required notices and any reasonable expenses incurred in relation to the meeting shall be repaid by the company.

The nomination of a person to the board of directors can be put to a vote at a general meeting, provided that prior notice (not less than three or more than 21 days prior to the meeting) outlining his or her intention to propose such person for election has been given, signed by a shareholder qualified to attend and vote at the meeting and accompanied by a notice in writing signed by the nominated person of his or her willingness to act.

8 Controlling shareholders' duties

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

There are no statutory provisions that expressly provide that controlling shareholders owe legal duties to the company or minority shareholders. However, the CBN Code, the SEC Code and the NAICOM Code each provide that it is the responsibility of the board to ensure that minority shareholders are protected from the overbearing influence of controlling shareholders of a company and to ensure the fair treatment of all shareholders. Further, if a controlling shareholder infringes on the rights of a minority shareholder, or commits a fraud on either the company or the minority shareholder, which the directors fail to redress (due to the wrongdoer being in control of the company or otherwise), the non-controlling shareholder may apply to court for injunctive relief.

A shareholder may also bring an application to the court for relief on the grounds that the actions of the company are being conducted in an unfairly prejudicial and oppressive or discriminatory manner.

Further, a shareholder may bring a derivative action on behalf of the company where the wrongdoers are in effective control of the company, the directors refuse to act, the application is brought in good faith, and it is in the best interest of the company. Evidence that the majority shareholders have approved any such wrongdoing will not in itself prevent a shareholder from seeking relief from the courts.

A shareholder who possesses, either directly or through a nominee, shares in a public company that entitles the shareholder to exercise 10 per cent of the unrestricted voting rights at any general meeting must notify the company of his or her interest. The duty also arises where the shareholding falls below 10 per cent.

9 Shareholder responsibility

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

Shareholders are generally not liable for the acts or omissions or debts of the company as the liability of shareholders is limited to the amounts paid or yet to be paid on their shares. In the case of an unlimited company, the liability of members for the debts of the company is unlimited. The company is a separate legal personality from its members. However, the courts may 'lift the corporate veil' where a company is a mere sham or is being used as a tool to perpetrate illegality. A shareholder may also be liable where, to his or her knowledge the company operates with less than two directors.

Corporate control

10 Anti-takeover devices

Are anti-takeover devices permitted?

There are generally no rules prohibiting anti-takeover devices. The directors have a duty to act in the best interests of the company in all situations. Major shareholders of a company may enter into a lock-in arrangement.

The ISA mandates directors of a target company to send circulars to members of the target company expressing their opinion one way or the other on a takeover bid. A dissenting director can also circulate his or her opinion to the shareholders.

11 Issuance of new shares

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

Subject to any limitations in the articles of a company, the power to issue shares is vested in the company. The power is exercised by the general meeting unless the articles specify otherwise and the general meeting may grant the authority to issue new shares to the board.

The articles of a company should determine whether shareholders have pre-emptive rights to acquire newly issued shares. Where the articles do not provide for such rights, none can be said to exist. The articles of private companies usually provide for pre-emptive rights.

12 Restrictions on the transfer of fully paid shares

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

The transfer of shares of a private company is subject to restrictions as specified in its articles of association. Restrictions commonly employed include provisions on pre-emptive rights in the articles of association. The right of pre-emption gives the other shareholders the first option to buy any shares a shareholder wishes to sell or transfer. Another restriction employed are clauses in a company's articles giving the board of directors and in some cases the shareholders a discretion to refuse to approve or register transfer of shares to persons or entities of whom they do not approve.

Public companies are expressly precluded from restricting the transfer of fully paid shares.

13 Compulsory repurchase rules

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

There are certain situations in which a company may repurchase its shares. These are where the company does so in order to settle a debt or claim against the company, to eliminate fractional shares, where the company has entered into an agreement to purchase shares from an officer or employee of the company or in order to satisfy the claims of a dissenting shareholder, or in compliance with a court order in the course of an arrangement or compromise. CAMA provides that an agreement with a company providing for the acquisition by a company of its shares is specifically enforceable against the company, to the extent that the company can perform the agreement without breaching the provision of CAMA on repurchase of shares. Any public company seeking to repurchase its own shares is also required to obtain the approval of the SEC and comply with the SEC Rules.

Where the shares are to be repurchased by the company, the shares may only be repurchased out of profits that would have been otherwise distributed as dividends or out of the proceeds from a fresh issue of shares made specifically for the purpose of the purchase of such shares.

Further, redeemable shares shall not be purchased at a price greater than the lowest price at which they are redeemable.

14 Dissenters' rights

Do shareholders have appraisal rights?

The ISA provides that where the approval of nine-tenths of the shareholders has been obtained, the shares of the dissenting shareholders (those who have not approved a scheme of merger) may be acquired, with notice, at the value agreed by the consenting shareholders except where the dissenting shareholders apply to court to have those terms varied. Aggrieved shareholders may petition the court to make an order compelling the company to buy them out at a price to be determined by the court.

The responsibilities of the board (supervisory)

15 Board structure

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

The board structure for listed companies can best be described as one or single-tier, comprising both executive and non-executive directors.

The SEC Code provides that the board should be of a size relative to the size and complexity of the operations of the company. It further recommends that the board of a public company should be made up of at least five directors but sets no upper limit for the number of directors on a board. The SEC Code further recommends that the majority of the board members should be non-executive directors and at least one should be an independent director.

16 Board's legal responsibilities

What are the board's primary legal responsibilities?

The board's legal responsibilities include directing and managing the affairs of the company, securing its assets, performing its duties in the interest of the company and furthering the purposes for which the company was formed.

17 Board obligees

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

The board represents the company and owes its duties primarily to the company. The board is to perform its duties in the interest of the company and all its shareholders as a whole, and not in the interest of a specific shareholder or a section of the shareholders. The board is also to take into consideration the interests of the employees in general, in performing its duties. However, the interests of the company must always come first, regardless of whether the actions of the board may adversely affect a shareholder.

18 Enforcement action against directors

Can an enforcement action against directors be brought by, or on behalf of, those to whom duties are owed?

The directors owe their duty to the company. The company can bring an action against a director to enforce any duty imposed by law. A shareholder may bring an action to prevent or redress a breach of duty by the directors.

A shareholder may also, with the leave of court, bring a derivative action on behalf of the company where the wrongdoers are directors who are in control and thus will not redress the wrong done to the company. A shareholder may also apply for relief from the court on the grounds that the affairs of the company are being conducted in an unfairly prejudicial and oppressive manner.

19 Care and prudence

Do the board's duties include a care or prudence element?

The directors of a company owe a duty of care and skill to the company and are to exercise such degree of care and skill that a reasonably prudent director would exercise in comparable circumstances. A director is required to exercise the powers and duties of his or her office honestly, in good faith and in the best interests of the company.

20 Board member duties

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

The same standard of care in relation to the duties of a director is expected of all members of the board including executive and non-executive directors. The relationship is a fiduciary one and directors are trustees of the company's assets, and are bound to exercise their powers in the interest of the company.

However, there may be additional contractual liabilities and benefits for executive directors under the principles of 'master and servant' where there is a contract to that effect.

21 Delegation of board responsibilities

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

The board is empowered, subject to any specific provisions in the articles to the contrary, to delegate any or all of its powers to a managing director or to committees made up of members of the board. The managing director or committee shall, in the exercise of such responsibilities so delegated, conform to any directions or regulations of the board. However, such delegation should not be done in such a way that it amounts to an abdication of duty.

The SEC Code provides that it is the responsibility of the board to facilitate the effective discharge of its duties and responsibilities through committees. While membership of these committees is exclusively reserved for board members, senior managers are allowed to be in attendance during their meetings to provide all necessary information needed by the committee to make informed decisions on behalf of the board. Even after delegating its powers, the overall responsibility of directing and managing the affairs of the company still ultimately lies with the board.

22 Non-executive and independent directors

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

The SEC Code recommends that there be at least five members of the board with a mix of both executive and non-executive directors. The CBN Code and the SEC Code provide that the number of non-executive directors on the board should exceed the number of executive directors. The CBN Code provides that for banks, at least two of the non-executive directors should be independent directors, and for discount houses at least one of the non-executive directors should be an independent director. The SEC Code provides for a minimum of one independent director.

The SEC Code describes an independent director as a non-executive director who:

- is not a substantial shareholder of the company, that is, one whose shareholding, directly or indirectly, does not exceed 0.1 per cent of the company's paid-up capital;
- is not a representative of a shareholder that has the ability to control or significantly influence management;
- has not been employed by the company or the group of which it currently forms part, or has not served in any executive capacity in the company or the group for the preceding three financial years;
- is not a member of the immediate family of an individual who is, or has been in any of the past three financial years, employed by the company or the group in an executive capacity;
- is not a professional adviser to the company or group, other than in the capacity of a director;
- is not a significant supplier to or customer of the company or group;
- has no significant contractual relationship with the company or group and is free from any business or other relationship that could materially interfere with his or her capacity to act in an independent manner; and
- is not a partner or an executive of the company's audit firm, internal audit firm, legal or other consulting firm that have material association with the company and has not been a partner or an executive of any such firm for three financial years preceding his or her appointment.

The PENCOM Code describes an independent director as one who has no relationship with the company, its related companies or officers that could interfere, or be reasonably perceived to interfere, with the exercise of his or her independent business judgement. The NAICOM Code provides that the board of insurance companies should have a minimum of seven and a maximum of 15 members and that the maximum number of executive directors should not exceed 40 per cent of the members of the board. The PENCOM Code provides that the number of non-executive members (excluding the chairman) of the board shall equate to the number of executive directors. The NAICOM Code and PENCOM Code each provide for a minimum of one independent director.

Non-executive directors are those whose roles are strictly supervisory and who do not participate in the day-to-day running of affairs of the company but are nevertheless important members of any board in the sense that they play a key role in the transparency, integrity and credibility of the board. An independent director on the other hand serves the function of bringing an objective, unbiased perspective to the board in carrying out its functions.

23 Board size and composition

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

Generally, persons of unsound mind, persons under the age of 18, persons previously convicted of fraud or breach of duty in connection with the promotion, formation or management of a company and insolvent persons are statutorily disqualified from being directors. There are criteria that must be met to be a director in a company and any person who is or proposes to be a director of a company must meet these criteria. A company may by its articles require directors to hold a specified number of shares. Failure of a director of such a company to obtain the share qualification within two months of his or her appointment will result in the person vacating his or her office until he or she obtains the shareholding qualification. The PENCOM Code provides that a director of a pension fund administrator (PFA) must not be a director, an employee, a principal officer or shareholder in a pension fund custodian (PFC) with which the PFA conducts business.

Managing directors and key management operating in certain industries may be required by the regulations and guidelines governing those industries to have specific qualifications. The SEC Code permits public companies to have a governance or remuneration committee whose function is to establish the criteria for board and board committee membership and to periodically evaluate the skills, knowledge and experience required on the board. The CBN Code prescribes that members of the board shall be qualified persons of proven integrity and be knowledgeable in business and financial matters in accordance with the extant CBN Assessment Criteria for Approved Persons' Regime for Financial Institutions. The NAICOM Code emphasises competence and integrity.

There is no restriction on the nationality of directors. Non-Nigerian citizens are permitted to be directors.

A person over 70 years of age or more who is or is to be appointed as a director in a public company is required to disclose his or her age to the members of the company in a general meeting and failure to do so amounts to an offence under CAMA. Special notice of the resolution approving or appointing such a director must be given by the company to its members, disclosing the age of the director. An appointee to the board of a public company is also expected to disclose his or her membership of boards of other companies to enable the shareholders to give full consideration to his or her other obligations and commitments in determining his or her suitability as a board member.

CAMA requires every company to have a minimum of two directors at all times but does not provide for the maximum number of directors a company may have. CAMA provides, however, that the number of directors shall be determined in writing by the subscribers of the memorandum of association or a majority of them with the power of the shareholders at a general meeting to increase or reduce the board. The laws and regulations governing particular industries may also set the minimum and maximum number of board seats. The CBN Code prescribes a minimum and maximum board size of five and 20 directors respectively. The SEC Code prescribes a minimum of five directors while directing that the board of a company be of a sufficient size relative to the scale and complexity of the operations of the company. The NAICOM Code prescribes a minimum of seven and a maximum of 15 board members for insurance companies. The PENCOM Code prescribes that the board of a company shall not exceed a size that will allow it to employ simple and effective methods of work to enable each director to feel a personal responsibility and commitment to the company and the board is to take into cognisance the scope and nature of the operations of the company.

The NCC Code requires the composition of a board to include a mix of skills, diversity, experience and gender. The number of directors should reflect the scale, size, complexity and reach of the business of the company and the skills and resource requirements of the company have to be taken into consideration. A majority of the board should be non-executive directors with at least one independent director holding not more than 0.1 per cent of the shareholding directly or indirectly in the company. One-third of the non-executive directors is also required to retire yearly by rotation subject to reappointment and for larger companies, non-executive directors should not remain on the board for a continuous period in excess of 15 years.

Vacancies on the board may be filled by the shareholders of a company in a general meeting. The board of directors of a company is also empowered to appoint new directors to fill casual vacancies created by death, resignation, retirement or removal of a director. Such appointments are, however, subject to ratification by the shareholders at the next general meeting.

24 Board leadership

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

The SEC Code recommends that the board of a company should not be dominated by any one person and the positions of chairman and CEO should be separate and be held by different individuals. Also, the chairman of the board should be a non-executive director in order to ensure the effective operation of the board. While the role of the CEO is to see to the day-to-day running and management of the company, the chairman's role is to provide overall leadership, direction and supervision of the board. The separation of the roles of board chairman and CEO is considered best practice.

The CBN Code and the NAICOM Code make it mandatory that no one person shall hold or combine the office of chairman of the board and that of CEO or managing director. The CBN Code further provides that no executive vice-chairman shall be recognised in the board structure. The PENCOM Code and the NCC Code also require the position of the chairman of the board and the CEO to be occupied by two separate individuals.

25 Board committees

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

Every public company is required to set up an audit committee consisting of an equal number of directors and shareholders' representatives up to a maximum of six members. Members of an audit committee are not entitled to remuneration and are subject to re-election annually. The functions of the audit committee include:

- ascertaining whether the accounting and reporting policies of the company are in accordance with legal requirements and agreed ethical practices;
- reviewing the scope and planning of audit requirements;
- reviewing the findings on management matters in conjunction with the external auditor and departmental responses thereon;
- keeping under review the effectiveness of the company's system of accounting and control;
- making recommendations to the board with regard to the appointment, removal and remuneration of the external auditors of the company; and
- authorising the internal auditor to carry out investigations into any activities of the company that may be of interest or concern to the committee.

The various corporate governance codes require that members of the audit committee should be able to read and understand basic financial statements, and be in a position to make valuable contributions to the committee. The SEC and CBN Codes provide that at least one member of the committee should be financially literate. The SEC Code further provides that, when necessary, external professional advice may be sought by the committee.

The board of a public company is permitted by the SEC Code to establish a risk management committee and a governance or remuneration committee in addition to its audit committee. The risk management committee is to serve the function of assisting in the oversight of the risk profile and the risk management framework to be determined by the board, while the governance or remuneration committee serves the function of periodically evaluating the skills and experience required by the individual members of the board and the board as a whole and making recommendations on the compensation structure for the executive directors of the company.

Banks and discount houses in Nigeria are directed by the CBN Code to establish a committee responsible for the oversight of risk management and audit functions and a board governance and nominations committee. The CBN Code further provides that the risk management and audit functions may be carried out by one committee, particularly in small institutions. The CBN Code proscribes the chairman of the board from being a member or chairman of any committee and provides that board committees must be headed by non-executive directors. The board remuneration committee must have at least two non-executive directors, while the board audit committee must have at least three members consisting only of non-executive directors and be headed by an independent director.

The PENCOM Code requires PFAs and PFCs to constitute a nominating committee (NC) whose duty is to make recommendations to the board on all board appointments. The NC shall consist of three directors including the chairman of the board and an independent director.

It is common practice among quoted companies to have various board committees assist the boards in administering the affairs of such companies and strengthen corporate governance. These committees, which may be known by different names in different companies, include nomination, general purpose, remuneration or compensation, risk assessment, strategy, corporate governance, finance, etc.

26 Board meetings

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

There are no statutory minimum requirements on the number of board meetings per year. However, directors are required to meet no later than six months after the incorporation of the company. The directors may otherwise regulate their meetings.

The PENCOM Code, CBN and SEC Codes recommend that board meetings be held at least quarterly in each financial year. The NAICOM Code provides that the board shall meet not less than four times in a year.

27 Board practices

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

CAMA provides that, where a director presents him or herself for re-election, a record of his or her attendance at meetings of the board during the preceding year shall be made available to members at the general meeting where he or she is to be re-elected. Where a person to be appointed or re-elected as a director is 70 years old or older, notice of his or her election or re-election shall disclose the age of the person to the shareholders.

The CBN Code requires the board to disclose the total number of board meetings held in the financial year and attendance by each director in its annual report. The CBN Code also provides that members of the board be appraised by an independent consultant annually on all aspects of the board's structure, composition, responsibilities, processes and relationships and the report of the independent consultant must be presented to the shareholders in the general meeting and to the CBN.

In addition, the SEC Code provides that the board of a public company is to include a corporate governance report in its annual reports, to be circulated to members and the regulatory authorities. The corporate governance report may contain information on the composition and responsibilities of board committees, and records of attendance at board and shareholders' meetings by directors during the period covered by the annual report. The SEC Code goes further to provide that the company's annual report ought to make sufficient disclosures on its accounting and risk management issues, indicating the board's responsibility for the process of risk management as well as its opinion on the effectiveness of the process.

Public companies are also to disclose the details of any director's interests in contracts with the company, its subsidiaries or holding companies and should also disclose any service contracts and any other significant contracts with controlling shareholders. Directors are required by the SEC Code to disclose any other directorship positions in other companies so that the members of the company can take into consideration a director's other responsibilities in assessing his or her suitability as a director in the company.

The directors are required to disclose their shareholdings in the company. Directors are also required to disclose loans made by the company to directors, their interest in contracts involving the company and any conflicts of interest in relation to the company.

28 Remuneration of directors

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

CAMA provides that the remuneration of directors should be determined by the company in a general meeting, while the SEC Code provides that the remuneration of executive directors should be set by a remuneration committee consisting wholly of non-executive directors. The SEC Code also provides that the remuneration for non-executive directors should be fixed by the board and approved by the members in a general meeting and that, where share options are granted as part of remuneration for directors, the board should ensure that they are not priced at a discount except with the approval of the SEC. The CBN Code also requires the remuneration of directors to be fixed by a committee composed of non-executive directors and the remuneration for non-executive directors should be strictly limited to directors' fees, sitting allowances for board and board committee meetings and reimbursable travel and hotel expenses. Executive directors do not receive sitting allowances and directors' fees. The CBN Code further provides that stock options offered as part of executive remuneration shall be tied to performance subject to the approval of shareholders in general meeting, may only be exercisable after one year of the expiry of the director's tenure and may only be priced at a discount on the authorisation of relevant regulatory agencies.

The remuneration of each director should be proportionate to his or her skill and experience and should be sufficient to attract, motivate and retain skilled and qualified persons. The remuneration of directors is to be disclosed in the yearly financial statements of the company.

The CBN Guidelines for the appointment of independent directors restricts the term of office of independent directors to a single term of four years and a maximum of eight years of two consecutive terms. In relation to other non-executive directors, their tenure is limited to a maximum of three terms of four years each. With respect to the tenure of the chief executive officer of a bank, the CBN Code allows for a tenure of 10 years which may be broken down into periods not exceeding five years at a time.

CAMA discourages directors' service contracts beyond a five-year term and provides that, before a service contract for a term beyond five years is executed, it must be approved by a resolution of the company. The SEC Code, while subjecting the tenure for directors to the provisions of CAMA, recommends that all directors should be submitted for re-election at regular intervals of at least once every three years. The SEC Code also provides that non-executive directors of public companies should serve for reasonable periods on the board but emphasises the necessity to continually reinforce the board by injecting new energy, fresh ideas and perspective and that the board should ensure the periodic appointment of new directors to replace existing non-executive directors.

Companies are prohibited from making loans to directors and are also not allowed to guarantee such loans. There are, however, two exceptions provided in CAMA:

- the company can grant a loan to a director where such loan will enhance the performance of his or her duties in the company; and
- the company can also grant a loan to a director where money lending is one of its ordinary businesses and the lending is done in the ordinary course of business.

In addition, substantial property transactions between a company and its directors are prohibited unless approval is granted by the company by way of an ordinary resolution at a general meeting. If a director is in any way, whether directly or indirectly, interested in a contract or proposed contract with the company, he or she is required to declare the nature of his or her interest at a meeting of the board. Banks are also required to disclose details of insider-related credits in their financial statements. Such insider-related credits include transactions involving directors, shareholders, employees and their related interests.

CAMA makes it unlawful for a company to make payment to a director as compensation for loss of office or as consideration for or in connection with his or her retirement from office unless particulars of the proposed payment and amount have been disclosed to the members of the company and approved. Under CAMA, members' approval is also required for compensatory payments to be made where, in connection with the transfer of the whole or part of the undertaking or property of a company, it is proposed to make any payment to a director as compensation for loss of office or as consideration for or in connection with his or her retirement from office.

29 Remuneration of senior management

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

The remuneration of the managing director is determined by the board. In addition to the response stated in the penultimate paragraph of question 28, banks are required by the CBN to disclose details of insider-related credits including the aggregate amount of insider-related loans, advances and leases outstanding with non-performing components further analysed by security, maturity, performance, provision, interest-in-suspense and name of borrowers in their financial statements.

30 D&O liability insurance

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

Directors' and officers' liability insurance is permitted. It is not common practice for companies to take out such insurance, though some companies, in keeping with international best practices, take out liability insurance for their directors and officers.

31 Indemnification of directors and officers

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

Companies are permitted to indemnify their directors and officers for liabilities incurred in their capacities as directors and officers of the company except in cases of negligence, fraud or breach of trust in relation to the company.

32 Exculpation of directors and officers

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

A company may ratify the act of an officer or director even where such an act or conduct is irregular. The company may also, by its articles (or by the director's contracts of service), limit the liability of a director except in cases of negligence, fraud or breach of trust of which a director or officer may be guilty in relation to the company.

Further, a company may also provide that the liability of a director be unlimited, regardless of the fact that the company itself is a limited liability company, provided that the director is given notice before he or she takes up the appointment that his or her liability shall be unlimited. The company may also, by special resolution, amend its memorandum so as to render the liability of its directors or managers unlimited.

33 Employees

What role do employees play in corporate governance?

The CBN and SEC Codes require every public company to establish 'whistle-blowing' procedures that encourage staff to report unethical activity or breaches of corporate governance to, in the case of the CBN Code, the bank and CBN and under the SEC Code, the company. The ISA also makes provision for employees of publicly quoted companies to report suspected criminal activities or non-compliance with any legal obligation within the company. The law provides that any such whistle-blower shall be protected from detriment as a result of his or her actions. Where he or she suffers any detriment, the SEC may, on his or her complaint, order that the employee be reinstated or compensated, or both. The CBN Guidelines for Whistle Blowing in the Nigerian Banking Industry, 2014 provide similar protection for employees of financial institutions.

In addition, the managing director and executive directors, as employees of the company, are responsible for the implementation of corporate governance policies.

The PENCOM Whistle Blowing Guidelines for Pensions (WBGP) provides that the directors, management, employees and any other persons that have dealings with a pension fund administrator (PFA) or pension fund custodian (PFC) shall have the responsibility to report breaches to PENCOM and requires that all PFAs and PFCs undertake not to victimise employees that comply with the WBGP. Where victimisation nonetheless occurs, the WBGP provides that PENCOM shall employ appropriate regulatory tools to offer redress to the employee concerned.

34 Board and director evaluations

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

Under the NCC Code, the board is required to establish a system for periodic evaluation of its own performance, that of its committees, chairman, chairmen of its committees and individual directors. This should be done at least annually and a statement of evaluation is required in the company's annual returns to state whether evaluation had been conducted during the period under the review. The evaluation is to be an objective and independent process. The CEO appraisal is to be done by the board or such committee of the board made up of non-executive directors.

The SEC Code also requires a board to establish a system to undertake an annual and rigorous evaluation of its own performance, its committees, chairman and individual directors. The chairman is to oversee the evaluation of the performance of the CEO while the CEO is to do the same for the executive directors. The result of the evaluation is to be communicated and discussed by the board as a whole while that of the independent directors is to be communicated and discussed by the chairman with them. The board may engage the services of external consultants to facilitate the evaluation. The cumulative result of the performance evaluation of the board and independent directors is to be used as a guide for re-election. The SEC Code further recommends training for any director whose performance is unsatisfactory or where not feasible, removal from office.

The PENCOM Code has similar provisions to the SEC Code and NCC Code and requires that the outcome of the evaluation shall be prepared in two copies, one of which must be submitted to the Pension Commission along with the company's annual report on corporate governance.

The CBN Code requires an annual formal assessment of the effectiveness of the board as a whole and the contribution by each individual director (including the chairman) to the effectiveness of the board. The Nomination Committee is to recommend the evaluation procedure and propose objective performance criteria, which should be approved by the board. The issues to be evaluated should include attendance at meetings, contributions to discussions at board meetings and board committee meetings, business referrals or support of the institution, public standing of the director and the beneficial effect of this on the business of the institution. The performance indicators should include the compliance status of the institution, the overall performance of the institution, regularity of board meetings and the overall contribution of the board to the performance of the institution.

Under the PENCOM Code, the evaluation should answer questions such as:

- how well the board performed against any performance objectives that have been set;
- what the board's contribution to the testing and development of strategy has been;
- whether the composition of the board and its committees is appropriate with the right mix of knowledge and skills to maximise performance in the light of future strategy;
- if the board responded to any problems or crises that have emerged and whether these could have been foreseen;
- how well the board communicates with the management team, company employees and others;

Update and trends

The Financial Reporting Council of Nigeria National Code of Corporate Governance (the FRCN Code) was issued to take effect in 2016 in three parts: the Public Sector Governance Code, the National Code of Corporate Governance for the Private Sector and the Not-For-Profit Organisations Governance Code. However, on 9 January 2017 the Federal Ministry of Industry, Trade and Investment suspended the implementation of the FRCN Code pending resolution of certain issues raised, including whether the FRCN Code complied with the provisions of the FRCA.

On 27 February 2017, the CBN issued an exposure draft of the Code of Corporate Governance for Other Financial Institutions. Prior to the release of the draft code, there was only the CBN Code which applied generally to banks and discount houses. The aim of the CBN with the release of the draft code is to have distinct codes of corporate governance for the following institutions: bureaux de change, development finance institutions, finance companies, mortgage refinance companies, microfinance banks and primary mortgage banks, taking into consideration issues specific to each of these financial institutions.

The CBN Code for Bureau De Change (the BDC Code)
This code aims to complement the extant operational guidelines and regulations on bureau de change (BDC) business. The BDC Code limits the size of the board of the BDCs to three and a maximum of five people, with at least one independent director. It emphasises that members of the board should be qualified persons of proven integrity and knowledgeable in business and financial matters, in accordance with the extant CBN Guidelines on Fit and Proper Persons Regime.

The CBN Code for Development Finance Institutions (the DFI Code)
This code aims to guide licensed DFIs towards entrenching good corporate governance standards and practices, to ensure that they are managed safely and soundly and risk-taking activities and business prudence are appropriately balanced to maximise shareholders' returns and protect the interests of all stakeholders. The DFI Code limits the minimum size of the board of DFIs to seven and a maximum of 11 people. Except for DFIs established by an enabling law, the Code requires CBN's prior approval for an equity holding of 5 per cent and above by anyone. However, where such shares are acquired through the capital market, the banks are mandated to apply for a no objection letter from the CBN immediately after the acquisition.

The CBN Code for Finance Companies (the Finance Companies Code)
This code is aimed at complementing the operational guidelines for finance companies, which were revised in 2014. The Finance Companies Code is expected to enhance good governance practices, engender public confidence to attract investments and promote efficiency and transparency in the sub-sector. The Finance Companies Code is issued pursuant to the relevant provisions of the Central Bank of Nigeria Act, 2007, BOFIA, other relevant laws and extant CBN Guidelines and Circulars.

The Finance Companies Code stipulates that the size of the board of finance companies shall be a minimum of five and a maximum of nine people, with at least one independent director. The board also has the responsibility of specifying the approval limits for transactions. Under the code, the maximum tenure for non-executive directors is 12 years. For the Chief Executive Officer of a finance company, the Code stipulates a maximum tenure of 10 years.

Under the Code, the approval of the CBN is required for an individual, group of individuals, their proxies or corporate entities or their subsidiaries to have a controlling interest in more than one finance company.

The CBN Code for Microfinance Banks (the MFB Code)
This code aims to address the poor governance practices in microfinance banks (MFBs). The MFB Code separates the positions of the chairman and the managing director/chief executive officer and stipulates that the size of the board of MFBs will be a minimum of seven and a maximum of 15 directors. Where a MFB is part of a holding company, not more than two members of the same family should be allowed to serve on the boards of the MFB and the holding company.

The MFB Code provides that non-executive directors must be at least twice the number of the executive directors at any point in time, and further requires that the board of state and national MFBs have a minimum of one and a maximum of two independent directors. The MFB Code also seeks to discourage government from holding majority shares in MFBs and requires that government direct and indirect equity holding in any MFB should be divested to private investors within a maximum period of five years from the date of licensing or investment. The code provides that government shareholding after the five-year period should be a maximum of 10 per cent.

The CBN Code for Mortgage Refinance Companies (the MRC Code)
This code aims at guiding mortgage refinance companies (MRCs) in their governance arrangement. Except for investors established by an enabling law, the MRC Code requires the CBN's prior approval for an equity holding of 5 per cent and above by any investor. It also requires that where such shares in an MRC are acquired through the capital market, the bank should apply for a no objection letter from the CBN immediately after the acquisition.

The MRC Code stipulates that the size of the board of an MRC should be a minimum of seven and a maximum of 15 persons. Where the MRC is part of a holding company, not more than two members of the same family shall be allowed to serve on the board of the MRC and the holding company and the members of the same family cannot occupy the positions of chairman and managing director or chief executive officer of the MRC and subsidiary at the same time.

The CBN Code for Primary Mortgage Banks (the PMB Code)
This code is aimed at addressing the poor governance practices in primary mortgage banks (PMBs) with the view that the safety and soundness of a financial institution depends on the effectiveness of the board of directors in discharging their oversight functions. The PMB Code stipulates that the size of the board of the PMBs shall be a minimum of seven and maximum of 15 persons. Where the PMB is a member of a holding company, not more than two family members shall be allowed to serve on the boards of the PMB and the holding company and two members of a family cannot occupy the positions of chairman and managing director/chief executive officer or executive director of the PMB and chairman or managing director/chief executive officer of a PMB's subsidiary at the same time.

Compliance with the various codes by the relevant institutions is mandatory. Each of the relevant institutions' external auditors are to report annually to the CBN the extent of their compliance with the provisions of the applicable codes, while the institutions themselves are to make returns on their compliance semi-annually. The board of each relevant institution has been given the ultimate responsibility to ensure compliance. Failure to comply with the Code will, however, attract appropriate sanctions in accordance with the BOFIA, one of which is the revocation of the operating licence.

In the past year, there have been renewed calls by shareholders for additional fora aside from the general meetings, for shareholders' engagement. The usual forum for engagement between the directors, management and shareholders of companies has been at annual general meetings or extraordinary general meetings of the companies and in some cases, pre-AGM fora or dinners.

- how effectively the board uses mechanisms such as the annual general meeting;
- whether the board as a whole is up to date with the latest developments in the regulatory environment and the market;
- whether sufficient board and committee meetings of appropriate length are held to enable proper consideration of issues; and
- whether board procedures are conducive to effective performance and flexible enough to deal with all eventualities, etc.

Disclosure and transparency

35 Corporate charter and by-laws

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

The memorandum and articles of association and other statutory filings of companies are available to the public at the Corporate Affairs

Commission. Copies can be obtained upon application and subject to the payment of prescribed fees.

36 Company information

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

The annual reports and accounts consisting of the directors' report, auditor's report and financial statements are to be filed with the Corporate Affairs Commission after every annual general meeting of a company. These documents can be accessed by the general public upon payment of the requisite fee. Other information filed with the Corporate Affairs Commission, which is available to the public, includes any changes in the composition of the board of directors, return of allotment of shares, change of registered address, charges on the company's assets, appointment of receivers, appointment of liquidators, etc. Outside the statutory requirements, companies are encouraged to also include corporate governance reports laying out the company's governance structure, policies and practices in their annual reports.

Quoted companies are required to make certain disclosures to the Nigerian Stock Exchange and the SEC from time to time. Such disclosures include:

- information on acquisitions of other companies or businesses;
- preliminary results for any year, half-year, quarter and comparative figures in respect of the profits before and after taxation, even if this calls for qualification that such figures are provisional or subject to audit;
- information on any proposed changes in the capital structure of the company or redemption of securities;
- financial statements; and
- interim reports such as first-quarter, half-year and nine-months' accounts.

In addition, the annual reports shall disclose, among other things, the directors' direct and indirect holdings in the issued shares, substantial shareholdings representing 5 per cent or more of issued shares and a five-year financial summary. The CBN and SEC Codes also require the board to disclose its risk management policy in its annual report.

Hot topics

37 Say-on-pay

Do shareholders have an advisory or other vote regarding executive remuneration? How frequently may they vote?

Shareholders have a direct say in directors' remuneration. CAMA provides that directors' remuneration be determined by the shareholders in a general meeting. Such votes take place at the annual general meeting of a company. However, the board fixes the remuneration of executive directors. The SEC and CBN Codes stipulate that only the non-executive directors should be involved in decisions regarding the remuneration of executive directors.

38 Shareholder-nominated directors

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

Shareholders can nominate a director to be appointed to the board at the general meeting. The law states that a motion for nomination will be treated as a motion for his or her appointment.

A member may leave at the registered address of a company a signed notice in writing of his or her intention to propose a person for election to the office of a director in place of a retiring director at a general meeting. The notice must be given not less than three days or more than 21 days before the date appointed for the meeting and must be accompanied by a notice in writing signed by that person of his or her willingness to be elected.

One or more members representing not less than one-twentieth of the total voting rights of members entitled to vote at a general meeting or 100 or more members holding shares on which there has been paid up an average sum per member of at least 500 naira, may requisition the company to circulate notice of a resolution they intend to be moved at a general meeting. The proposed resolution can propose the appointment of a new director. The company has a duty to give notice of the resolution to members entitled to receive notice of the next annual general meeting where the resolution is intended to be moved. The notice of the resolution shall be given in the same manner and so far as practicable, at the same time as notice of the meeting and where not practicable, soon thereafter. The company is, however, not bound to give notice of any requisition unless a duly signed copy is deposited at the registered address of the company and a sum deposited or tendered, which is reasonably sufficient to meet the company's expenses in giving effect to it. The company may also decide to bear the expenses of circulating notice of the proposed resolution.

39 Shareholder engagement

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

The process of engaging with the shareholders is typically led by the directors and senior management of the company. Generally, companies engage with their shareholders through the holding of general meetings. It is usual for directors, senior management, external counsel, auditors and other specialists or consultants engaged in relation to matters to be discussed or decided during a general meeting of the company to be involved in such engagements. Some quoted companies also organise pre-AGM fora or dinners for directors, management, investors, major customers etc to interact.

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The SEC Code provides that the general meetings of the company should be the primary avenue for meeting and interaction between the shareholders, management and board of a company. It further requires that general meetings should be conducted in an open manner allowing for free discussions on all issues on the agenda such that sufficient time is allocated to shareholders to participate fully and contribute effectively at the meetings.

The NAICOM Code provides that directors should always communicate information that is understandable and accessible to shareholders in a timely manner and on a regular basis and encourage shareholders to participate in annual general meetings. Under the CBN Code, banks are encouraged to communicate with their shareholders via their website. Information to be provided through this means shall include major developments in the bank, risk management practices, executive compensation, local and offshore branch expansion, establishment of investment in subsidiaries and associates, board and top management appointments and sustainability initiatives and practices.

The NCC Code provides that there should be a dialogue and engagement between the board and the shareholders to align appreciation and attain the mutual understanding of corporate objectives of telecoms companies.

Poland

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Sources of corporate governance rules and practices

1 Primary sources of law, regulation and practice

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

The Polish corporate governance rules are primarily based on the following legal acts:

- the Commercial Companies Code establishing basic governance rules for commercial companies;
- the Civil Code, including rules regarding commercial proxies;
- the Public Offer of Financial Instruments Act establishing rules for the functioning of public companies which are only partly regulated in the Commercial Companies Code;
- the Act on Freedom of Conducting Business Activity establishing principles for performing economic activity;
- the Act on the National Court Register establishing registration principles of corporate entities;
- the Unfair Competition Law establishing the notion of unfair competition and rendering mechanisms for its prevention;
- the Act on Anti-Money-Laundering and Combating of Terrorism establishing the position of the General Inspector of Finance Information as well as procedures preventing money laundering and financing of terrorism; and
- the Bankruptcy and Reorganisation Act including obligations of the members of the management board to file in bankruptcy petitions.

Further, Polish non-statutory corporate governance principles have been developed by the Best Practices Committee, consisting of representatives of various communities related to the capital markets, and published in the document 'Best Practices in Public Companies 2002'. In 2007, the supervisory board of the Warsaw Stock Exchange (WSE) adopted rules of corporate governance called the 'Best Practices of WSE Listed Companies'. The aim of the 'Best Practices of WSE Listed Companies' is to strengthen the transparency of listed companies, improve the quality of communication between the companies and investors, and strengthen the protection of the rights of shareholders while not imposing additional burdens on listed companies. Compliance with the 'Best Practices of WSE Listed Companies' is based on the 'comply or explain' principle, which requires listed companies to issue an annual report stating whether or not they comply with the code and explaining the reasons for any non-compliance. Reports are forwarded by the listed companies to the WSE and published on the listed companies' websites. The latest updates to the 'Best Practices of WSE Listed Companies' took effect on 1 January 2016. The 'Best Practices of WSE Listed Companies' include six general principles, 20 recommendations and 70 specific principles which should be respected by companies and are subject to a reporting obligation in the electronic stock exchange reporting system.

To a certain extent, in case of ambiguities, the corporate governance rules are also being continuously developed by the Polish courts, especially by virtue of verdicts and resolutions of the Supreme Court.

2 Responsible entities

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

The statutory corporate governance rules in Poland are adopted by the parliament and also require the approval of the president. Any required specifications of the statutory rules are made directly by governmental ministry bodies in the form of ordinances.

There is no particular agency for the enforcement of corporate governance rules. Generally, the mandatory corporate governance rules are enforced through litigation in civil courts. However, there are also authorities like the Polish Financial Supervision Authority entitled to supervise the banking, capital markets, insurance, pension scheme and electronic money institutions.

There are also non-governmental organisations in Poland that represent entrepreneurs in the public debate, such as the Entrepreneurs of the Republic of Poland, the Business Centre Club, the Union of Polish Craftmanship and Confederation Lewiatan, which announce their own economic programmes containing demands with respect to the promotion of entrepreneurs in Poland. All of these organisations also represent the interests of entrepreneurs in governmental institutions. For example, they are members of the Tripartite Commission of Social Dialogue, which is involved in establishing indicators of wage growth in enterprises and in the budget sector. They are also involved in influencing the state budget process and may speak on matters of economic and social importance.

The rights and equitable treatment of shareholders

3 Shareholder powers

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

As a result of the two-tier board structure in Poland, shareholders of a joint-stock company only have an indirect influence on the appointment, removal and decisions of the members of the management board. In general, members of the management board are appointed and dismissed by the supervisory board and not by the shareholders, unless the articles of association of the company state otherwise. However, the shareholders have an irrevocable right to dismiss or suspend members of the management board by way of a resolution adopted at a general meeting. Such resolution requires an absolute majority of votes at the general meeting and is valid irrespective of the number of shares represented. The articles of association may also grant specific rights to individual shareholders, including the right to appoint or dismiss members of the management board. Also, a shareholder may be appointed as a member of the management board.

A member of the management board may be dismissed at any time by the supervisory board. The articles of association of the company may include other provisions, limiting the right to dismiss a member of the management board to situations where significant reasons exist. Nonetheless, this does not affect the rights of such a dismissed member of the management board under the employment relationship or another legal relationship applicable to his or her service.

Shareholders are not allowed to issue directions to the management board. At the general meeting, shareholders may only decide on management issues if so requested by the management board. The impact of the shareholders on the company's daily business is rather limited.

4 Shareholder decisions

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

Statutory law stipulates that the following matters require a resolution of the general meeting:

- consideration and approval of the report of the management board on the operations of the company and of the financial report for the previous financial year;
- granting of approval of the performance by the members of the company governing bodies of their duties;
- adoption of a resolution on distribution of profits or financing of losses,
- decisions concerning claims for redress of damage caused upon formation of the company or in the course of management or supervision;
- transfer or tenancy of enterprise or its organised part and the creation of a limited right in rem on them;
- acquisition and transfer of real estate, the right of perpetual usufruct or a share in real estate, unless the articles of association provide otherwise;
- issuance of convertible bonds or bonds with the right of priority, and issuance of subscription warrants;
- acquisition of the company's own shares in cases stipulated by law;
- conclusion of contracts by virtue of which a dominant and a dependent company enters into an agreement which provides for management of the dependent company or a transfer of profits by such company; and
- conclusion by the company of a credit, loan, surety or another similar agreement with a member of the management board, supervisory board, a commercial proxy or a liquidator or for the benefit of any such person.

Furthermore, contracts for the acquisition by the company of any property for a price exceeding 10 per cent of the share capital paid, from any founder or any shareholder, or for the dependent company from any founder or any shareholder, concluded before the end of two years of the date of registration of the company, require a resolution of the general meeting (a majority of two-thirds of the votes is required). The same procedure applies to the acquisition of property from a dominant or dependent company. Non-binding resolutions of the general meeting are not common in Poland.

5 Disproportionate voting rights

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

As a general rule, the shareholders are to be treated in the same manner where similar circumstances apply and a share carries one vote at the general meeting. However, the company may issue preference shares (ie, shares with special rights attached to them and stipulated in the articles of association). Such privileges may concern in particular the right to vote (non-public companies only), the right to dividends, or participation in the division of assets in case of liquidation of the company. With reference to vote privileges, a single privileged share may carry no more than two votes.

6 Shareholders' meetings and voting

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

The entitlement to participate in the general meeting is regulated differently with regard to non-public and public companies. As regards non-public companies, shareholders have the right to participate in the general meeting of a company if they were registered in the share register at least one week prior to the holding of a general meeting. In the case of public companies, only persons who have been shareholders in the company 16 days prior to the date of the general meeting have the right to participate.

The list of shareholders entitled to participation in the general meeting, signed by the management board, with the surnames and first names or business names of those entitled, their residence (seat), the number, class and serial numbers of shares and the number of votes to which they are entitled, is to be displayed in the premises of the management board for three weekdays prior to the holding of the general meeting.

In addition, resolutions may be adopted, despite the general meeting not having been formally convened, if the entire share capital is represented and none of those present has opposed the holding of the general meeting or the inclusion of particular matters on the agenda.

Providing that it is allowed in the statute of the company, members of the management and supervisory boards may meet and adopt resolutions by way of teleconference or videoconference. Shareholders may also participate in meetings by way of teleconference or videoconference if so provided by the company statute. In such a case, participation may be subject to only such limitations as are necessary for the shareholders to be identified and for security of the electronic communication to be ensured.

7 Shareholders and the board

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

As a matter of principle, general meetings are convened by the management board of the company. The supervisory board may convene the ordinary general meeting where the management board fails to convene it within the time stipulated in statutory law or in the articles of association, as well as an extraordinary general meeting, should it deem its convocation desirable. Further, the articles of association may authorise other persons to convene a general meeting and shareholders representing at least half of the share capital or half of the total number of votes in the company may also convene an extraordinary general meeting.

Further, the statutory law grants to the shareholder or shareholders representing at least 5 per cent of the share capital the right to request a convocation of an extraordinary general meeting, as well as placing certain matters, including director nominations, on the agenda of such meeting by the management board (the request regarding new matters is to be submitted to the management board of a non-public company not later than 14 days prior to the scheduled date of the meeting and 21 days in case of a public company). The articles of association may authorise shareholders representing less than 5 per cent of the share capital to request the convocation of an extraordinary general meeting.

There are no rules to force the management board to circulate dissident statements by shareholders to resolutions proposed by the management board.

8 Controlling shareholders' duties

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

Although it is not codified, shareholders owe a general duty of loyalty to the company and to other shareholders. It means that a shareholder, mainly in relation to voting rights, may not cause harm to the company or other shareholders.

A resolution of the general meeting that contravenes the articles of association or good practices and harms the interests of the company, or is aimed at harming a shareholder, may be challenged in an action brought against the company for annulment or for declaration of invalidity of such a resolution by:

- the management board, supervisory board and each of their members;
- a shareholder who voted against the resolution and, following its adoption, requested that his or her objection be recorded in the minutes;
- a shareholder who was not allowed to participate in the general meeting without any valid reason; or
- a shareholder who was not present at the general meeting, only if the general meeting was wrongly convened or if the resolution concerned a matter not included on the agenda.

9 Shareholder responsibility

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

Shareholders must provide only the performances stipulated in the articles of association and are not liable for the obligations of the company. However, there are certain exceptions to this rule regarding the situation of joint-stock companies prior to registration: a shareholder of a joint-stock company in organisation is jointly and severally liable with the company and the persons who acted in its name for the obligations of the company in organisation as well as for the obligations of the company up to the unpaid value of subscribed shares.

Similarly, if a joint-stock company in organisation has no management board and no attorney was appointed, its shareholders are liable for the company's tax arrears.

Corporate control

10 Anti-takeover devices

Are anti-takeover devices permitted?

Anti-takeover devices are generally not explicitly regulated in Polish law. The management board may, however, use a number of defence measures to protect the company against a hostile takeover bid. As long as actions undertaken by the management board comply with the provisions of law, it is possible to use both the reactive and preventive means of protection.

Before receiving a notice of a hostile takeover, the preventive measures may include:

- agreements on high severance payments for the management members dismissed from their positions;
- agreements with the major shareholders under which the shareholders undertake not to sell shares with the exception of to persons that are signatories to the agreement. However, according to the statutory law, such agreements may be concluded only for a defined period of time, not exceeding five years from the date of their execution;
- limitations in the articles of association of the voting rights of the shareholders controlling more than one-tenth of the total number of the votes. However, the limitation may apply only to the exercise of the voting rights on shares above the limit of the votes as stipulated in the articles of association; and
- conferring upon an individual shareholder specific rights, in particular, the authorisation to appoint or remove members of the management board or the supervisory board.

Upon receiving information about a hostile takeover, the management board may decide to:

- increase the share capital by issuing new shares to increase the cost of acquisition. The discouraging effect may be reinforced if new shares are issued at a preferential price with pre-emptive rights for existing shareholders, as the acquiring company may not take advantage of such privilege;
- sell valuable items of the company in order to decrease the company's value;
- purchase shares in the acquiring company in a number granting the right to adopt a resolution on suspension of the further acquisition of the company's shares;
- acquire shares of companies in the acquiring company's sector to create antitrust law obstacles; or
- acquire and redeem the company's own shares. Redemption raises the price of the remaining shares and the price proposed to the shareholders of the company becomes less favourable.

Apart from the above, a public company listed on a regulated market such as the WSE is partially protected against hostile takeover bids by the provisions of the Act on Public Offering. When a shareholder exceeds the thresholds of 33 or 66 per cent of the total vote of a company, a requirement to make a mandatory offer applies, namely:

- an acquisition resulting in a shareholder exceeding 33 per cent of the total vote in a public company requires announcement of a tender offer for the company's shares, giving 66 per cent of the total vote; and
- an acquisition resulting in a shareholder exceeding 66 per cent of the total vote in a public company requires announcement of a tender offer for all of the remaining shares in the company.

Practice shows that with the low attendance rates of minority shareholders holding 33 per cent of the voting rights is sufficient to have a decisive influence over a company's operations. While Polish law does not distinguish between hostile or friendly takeovers, new legislation aimed at protecting strategic Polish companies from hostile takeovers was passed by the Parliament on 10 July 2015. The need for such regulations was recognised in 2012, after the Russian company Acron bid for the Polish chemicals conglomerate, Grupa Azoty. This act obliges investors to notify Poland's Minister of Energy or Prime Minister of their intention to buy shares in strategic Polish companies. The relevant authority then has 90 days to either allow or block the deal. The list of strategic companies has been determined by the Council of Ministers with the ordinance dated 8 December 2016 and includes seven Polish companies in energy, oil, gas, fuels and chemicals.

11 Issuance of new shares

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

The articles of association may authorise the management board to increase share capital by issuing new shares without a shareholders' resolution. A resolution of the general meeting on the amendment to the articles granting such authorisation must be adopted by a 75 per cent majority, in the presence of the shareholders representing at least half of the share capital (for a public company it should be at least one-third of the share capital). The authorisation for increasing share capital must not exceed a time limit of three years. Within this time frame the management board of the company may exercise the authority by making one or more consecutive share capital increases. The amount of authorised capital may not be larger than three-quarters of the share capital as at the date on which the authorisation to the management board is granted. The management board may issue shares for cash contributions only, unless the authorisation to increase the share capital states otherwise. Preference shares or shares granted with personal rights may not be issued in the case of a share capital increase contemplated in the articles of association.

Generally, shareholders have a statutory right of priority in taking up new shares in proportion to the number of shares they already hold. The exclusion of the pre-emptive right applicable to an increase of the share capital made within the limits of the authorised capital requires a resolution of a majority of four-fifths of votes at the general meeting. However, it is possible for the articles of association to authorise the management board to deprive the shareholders of the pre-emptive right with the consent of the supervisory board.

12 Restrictions on the transfer of fully paid shares

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

Restrictions on the transfer of fully paid shares are permitted only with regard to registered shares. The articles of association may either require the consent of the company for the transfer of registered shares or limit the transferability of registered shares in another way. Unless the articles stipulate otherwise, the consent for the transfer of registered shares must be given by the management board in writing. If the restriction on the transferability of shares is stipulated in an agreement concluded between the company and a shareholder, it may not be stipulated for more than five years from the date of such agreement. Moreover, in order to be recognised as a shareholder in relation to the company, any transfer of registered shares must be registered in the company's share register.

Further, shares subscribed for in-kind contributions have to remain registered and cannot be transferred or pledged until the date of approval at the earliest ordinary general meeting which considers the financial report for the financial year in which such shares have been paid for. During this time, such shares are retained by the company as a security for claims for damages for non-performance or improper performance of the obligation to make in-kind contributions. However, this restriction does not apply to the shares subscribed for as a part of an increase of the share capital conducted by the company in order to be admitted to trading on a regulated market and to become a public company.

13 Compulsory repurchase rules

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

In non-public companies a forced buyout is allowed only under clearly defined circumstances and by the authority of a resolution adopted in a general meeting. Minority shareholders holding not more than 5 per cent of the share capital can be required to sell their holdings to a majority group of not more than five shareholders holding not less than 95 per cent of the share capital. The adopted resolution must identify the shares to be bought out, the shareholders who are undertaking to buy out the shares, and the shares designated for particular purchasers.

In public companies a shareholder who has acquired over 90 per cent of the total votes can demand that other shareholders sell all their shares in the company. However, it is possible only for three months after 90 per cent of the total votes is reached or exceeded. The price offered must be not less than the price that would apply to a tender offer when exceeding the 66 per cent threshold.

On the other hand, each minority shareholder has the right to require another shareholder who has reached or exceeded the 90 per cent threshold to make a reverse squeeze-out. In this case, the request should also be made within three months of reaching the 90 per cent threshold. Minority shareholders have the right to receive a price for a squeeze-out or reverse squeeze-out not lower than the price proposed in the tender offer for all outstanding shares if the threshold was reached in such offer.

The squeeze-out obligation applies to both the shareholder concerned and members of its group. They are obliged to squeeze-out minority shareholders in 30 calendar days from receipt of such request from any minority shareholder.

14 Dissenters' rights

Do shareholders have appraisal rights?

Shareholders have appraisal rights under clearly specified circumstances, including a minority shareholder squeeze-out. If the minority shareholders subject to a squeeze-out do not agree with the provided purchase price, they may apply to the registry court for the appointment of an auditor who will determine the market price of the shares or, where there is no market price, a fair purchase price. Any shareholder may challenge the purchase price estimated under the appraisal procedure by submitting to the registry court a motion for reconsideration. If the court deems it necessary, it may appoint another auditor.

In public companies, at the request of a minority of shareholders holding at least 5 per cent of the share capital, the general meeting may adopt a resolution on appointment of an independent auditor who will examine a specific issue related to the formation or management of the company.

The responsibilities of the board (supervisory)

15 Board structure

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

Polish law divides the decision-making and supervisory powers in a company between two separate bodies. Instead of the unitary board of directors, the corporate governance system in Poland consists of a management board and a supervisory board. Despite this separation, a purely ornamental function of the supervisory board is often the case in Polish joint-stock companies.

16 Board's legal responsibilities

What are the board's primary legal responsibilities?

The management board is responsible for managing the affairs of and representing the company. It is responsible for those issues that have not been reserved either for the supervisory board or for the shareholders' meetings. The members of the management board are appointed and dismissed by the supervisory board, unless the articles of association provide for a different mechanism.

The supervisory board is responsible for supervision of all aspects of the company's activities, including those of the management board. In particular, the supervisory board oversees the company's annual financial statements. It is prohibited for the supervisory board to instruct members of the management board. However, the company's articles of association may state that the management board needs to obtain the consent of the supervisory board before taking specified major decisions.

17 Board obligees

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

The management and supervisory board are liable to the company for any harm caused by their actions which are against the law or the company's articles of association. As a result, they primarily owe their legal duties to the company. However, the shareholders may seek a redress for violation of their rights through the courts by initiating a derivative action in the name of the company or a legal action for invalidation of the company resolutions in their own name.

18 Enforcement action against directors

Can an enforcement action against directors be brought by, or on behalf of, those to whom duties are owed?

The members of the management board and the supervisory board are jointly and severally liable for damage caused to the company by their acts or omissions. If the company does not bring an action for a redress of a damage caused to it, shareholders can initiate, within one year, a derivative legal action and seek a redress of the damage in the name of company. However, if the action proves to be unfounded and the shareholder acted in bad faith when bringing the action, the shareholder is obliged to redress the damage caused to the defendant. However, shareholders rarely bring such actions, as the litigation costs are reimbursed to the company and not to the shareholder. As a result, if the company fails to reimburse the litigation costs, the shareholder needs to file another suit.

Further, shareholders may demand a nullification of the resolution if it is in contravention of the statutory laws or the articles of association of the company. It is also possible to press for annulment resolutions that contravene the statutes or good practices and harm the interests of the company or are aimed at harming a shareholder (see question 8).

19 Care and prudence

Do the board's duties include a care or prudence element?

The members of both the management and supervisory boards are obliged to exercise diligence characteristic of the professional nature of their activity in the course of performing their duties. Moreover, members of the management and supervisory board cannot, without the consent of the company, be involved in any business entity that is competitive towards the company and are obliged to avoid conflicts of interest.

20 Board member duties

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

It is possible to set out in the company's internal corporate documents (eg, in the rulebook) the detailed rules concerning the duties of individual members of the management board (eg, in accordance with their skills and professional experience). In this way the responsibilities related to managing the company affairs may be assigned based on the specific expertise of a manager. It is certainly an important way of streamlining the work of members of the management board, however, it may not be deemed as a complete exclusion of the principle of the management board's collective responsibility.

It has been confirmed by court rulings that the board should not be treated as a group of autonomous individuals, especially if it comes to decisions that are of crucial importance for the company's development and have a significant impact on its current and future financial condition. Moreover, the internal regulations are solely binding between the company and the members of the management board. This means that the internal regulations on the division of duties are not enforceable towards third parties.

As a result, the internal division of duties does not allow for a complete division of responsibility between the members of the management board for their individual acts and omissions. They are responsible for the creation of an organisational framework and securing a free flow of information between them, all of which ensures appropriate checks and balances within the management board.

21 Delegation of board responsibilities

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

Although it is standard practice of internal corporate governance to delegate responsibilities of the management board to individual members (it is rather unusual to form committees within the management board), this does not eliminate the principle of collective responsibility (see question 20). Crucial decisions regarding the company should be taken by adoption of resolution of the entire board. With respect to particular competences, the collective decision-making (in the form of a resolution) may not be excluded by the delegation of responsibilities. These competences include convening of the general meeting, issuing shares within the authorisation stipulated in the articles of association (see question 11), and considering and approving of the management board report on the operations of the company.

The principle of collective responsibility of the supervisory board is eased by the possibility of creating the committees within the supervisory board in order to streamline its work in a particular area. However, there are some responsibilities reserved for the supervisory board that may not be delegated to the committees. In public companies there is a statutory obligation to appoint an audit committee with certain supervisory competences. According to the Auditors and Auditors' Self-Governing Bodies Act, the audit committee should consist of at least three persons, of which at least one is required to have qualifications in accounting or auditing. The members of the audit committee are appointed among the members of the supervisory board. As a result, companies planning to be listed on a regulated market must take into account this requirement while composing the supervisory board in order to appoint a person that meets the aforementioned criteria.

22 Non-executive and independent directors

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

The two-tier system of corporate governance in Poland consists of a management board, responsible for decision-making, and a supervisory board, responsible for overseeing the latter. For this reason, the institution of the non-executive and executive directors is not explicitly regulated in the statutory law, with a notable exception of an audit committee in public companies (see question 21) where at least one member is required to be independent and to prove some particular competences in accounting or auditing.

23 Board size and composition

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

Only a natural person enjoying full legal capacity may serve as a member of the management board or the supervisory board. Further, a person who has been convicted of certain crimes, such as fraud, embezzlement, money laundering and misappropriation of funds, may not serve as a member of the management board, supervisory board or on the audit committee. Also excluded from membership of the supervisory board and audit committee is a person who is already a member of the management board, a holder of a commercial power of attorney, a liquidator, a manager of a branch or factory, or is employed in the company as the chief accountant, legal adviser or advocate. It should also be noted that dependent or affiliated companies cannot share the same individuals in any of these positions.

The management board may include one or more members, with the number of board members determined by the articles of association. Board members are appointed by the supervisory board, unless there is a different mechanism stipulated in the articles of association. In general, the vacancies at the management board are filled by the resolution of the supervisory board.

Every joint-stock company must have a supervisory board. Supervisory boards must have at least three, and in public companies, at least five members who are appointed and dismissed by the shareholders' general meeting (unless the articles of association state otherwise).

There is no maximum number of seats prescribed by the law for the management board or the supervisory board of a joint-stock company.

24 Board leadership

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

Polish statutory law does not cover the position of a CEO. The management board of a joint-stock company may include one or more members. If the management board comprises several members, all of them are obliged and entitled to jointly manage the affairs of the company, unless the articles of association provide otherwise.

The articles of association may state that in case of an equal number of votes, the president of the management board shall have the deciding vote. The articles of association can also grant him or her certain powers in the management of the operations of the management board. If the articles of association do not grant the supervisory board or the general meeting the right to adopt or approve regulations of the management board, the management board may adopt its own regulations.

25 Board committees

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

According to Polish regulations, there is no obligation to create mandatory committees of the management or supervisory board. Nonetheless, the management board may adopt its own regulations (see question 24), which might include the establishment of certain committees.

26 Board meetings

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

The number of management board meetings is not determined by law or regulation in Poland. The supervisory board must be convened as the need arises, but must meet at least three times in a financial year. The supervisory board must exercise its duties collectively; it may also delegate its members to individually perform certain acts of supervision without the convocation of the entire body.

27 Board practices

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

Disclosure of management board practices is generally not required by law. However, companies applying for admission to trade on a regulated market, or who are already subject to a regulated market, are obliged to comply with certain information obligations. Such entities are required to provide shareholders and future investors with access to current information about the company and current and periodic reports. Such companies are not authorised to carry out a selective information policy, omitting important events for market participants.

The information obligations of companies whose securities are admitted to trading on the regulated market of the WSE do not differ significantly from the requirements in other developed capital markets in the European Union.

28 Remuneration of directors

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

The remuneration of members of the management board employed under an employment contract or another contract is generally determined by the supervisory board; however, the articles of association might state otherwise. The general meeting may also authorise the supervisory board to decide that the remuneration of members of the management board may include the right to a specified share in the annual profit of the company that is designated for distribution among the shareholders.

The resolution establishing the remuneration or a compensatory arrangement for a member of the management board may determine the amount of remuneration for the exercise of duties or set conditions for its calculation.

The term of office of a member of the management board may not be longer than five years. Reappointments of the same person are allowed for terms of office of a maximum of five years each and the appointment may not be made earlier than one year before the end of the current term. A mandate of a member of the management board expires at the latest on the date of the general meeting approving the financial report for the last full financial year of service of such a member.

29 Remuneration of senior management

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

There are no specific rules on senior management remuneration; however, there are certain restrictions on granting loans to the members of the management board or on other transactions between the company and its managers. With respect to the conclusion of credit, loan, surety or any other similar agreements by a capital company with a member of its management board, supervisory board, a commercial proxy or a liquidator or for the benefit of any such person, the consent of the general meeting is required for their validity (see question 4).

30 D&O liability insurance

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

Directors' and officers' liability insurance for managers of the company as well as for the supervisory board members, commercial proxies, liquidators and others is accepted under Polish law and available on the insurance market. The company is usually responsible for the premium payments.

31 Indemnification of directors and officers

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

The members of the management board, supervisory board or liquidators are liable to the company for damage caused by acts or omissions in breach of the statutory law or the provisions of the articles of association, unless they are not at fault. Unlike in the case of limited liability companies, board members of a joint-stock company generally do not incur personal liability to third parties.

32 Exculpation of directors and officers

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

The liability of the management and supervisory board members, as well as the liability of liquidators towards the company for the damage caused by their acts or omissions in breach of the statutory law, or the provisions of the articles of association, is of statutory nature. It means that the articles of association cannot specify solutions excluding or limiting it and, therefore, a liable person cannot be exempted from such liability in advance.

However, the above-mentioned persons are liable to the company for damage caused, unless they are not at fault. Essentially, there is no fault if such person exercised diligence characteristic of the professional nature in the course of performing his or her duties.

33 Employees

What role do employees play in corporate governance?

The participation of employees in corporate governance is not obligatory. Nonetheless, owing to the implementation of Directive 2005/56/EC, the participation of employees in the company resulting from a cross-border merger is regulated in the Act on the Participation of the Employees in a Company Established due to a Trans-Border Merger of Companies (the Act).

As a matter of principle in the case of a cross-border merger, the regime on employee participation of the country applies, in which the acquiring or the newly formed company is going to have its registered seat (provided that such rules exist in that country). The law applicable to the acquiring or to the newly formed company must have at least the same level of participation that existed before the merger or the same rights of the employees of the acquiring, or of the newly formed company working abroad that the employees in the country of registration of the company possess. The Act determines the employees' rights to the following forms of participation: the right to choose or appoint a certain number of members to the supervisory board; the right to recommend members of the supervisory board; and the right to oppose the appointment of some or all members of the supervisory board.

34 Board and director evaluations

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

Polish statutory law has relatively limited descriptions of the duties and liabilities of management and supervisory boards. In the performance of their duties, the board members must 'exercise due diligence proper for the professional nature of their actions'. The only formal evaluation of board members is the shareholder approval of the report of the management board on the operations of the company and of the performance of duties by the members of the company's governing bodies. Being an obligatory item of the ordinary general meeting's agenda, the granting of such approval simply means that the shareholders accept the actions of the members of the company's governing bodies in a given financial year. However, it should be noted that despite granting the approval of the report of the management board on the operations of the company, the shareholders at the general meeting may still refuse to grant approval of the performance of the duties to all or some management or supervisory board members. Failure to obtain such approval by all or selected members of the company's governing bodies is an expression of the shareholders' non-acceptance of their overall performance. However, obtaining such approval does not automatically result in the waiver of any of the company's legal claims for damages against members of the governing bodies and does not exempt them from potential liability towards the company itself.

In addition, if the shareholders have lost confidence in a member of the management board, they may adopt a resolution on the dismissal or suspension of that board member at the general meeting. The right of the shareholders' general meeting to dismiss or suspend a board member from his or her activities is irrevocable. Shareholders representing at least one-twentieth of the share capital may request that an extraordinary general meeting be convened and place on the agenda the adoption of a resolution on the dismissal or suspension of a board member. The articles of association may confer the right to request holding an extraordinary general meeting upon shareholders representing less that one-twentieth of the share capital.

Disclosure and transparency

35 Corporate charter and by-laws

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

The articles of association are publicly available at the register of entrepreneurs of the National Court Register in which the company has been entered. Each company is entered in the register of the district court where it has its registered office. As the National Court Register was established to provide the public with information concerning the legal situation of the registered entities, everyone has access to the registered entities' corporate files and can obtain legalised extracts concerning data entered in the register. It is also possible to find information on the entity entered in National Court Register online and download electronic extracts. The legal status of a print-out extract has the same legal force as a sealed document obtained at the National Court Register.

36 Company information

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

Each company has its corporate files kept in the National Court Register of the district court where the company has its registered office. The information to be disclosed includes business name, address, scope of activity, amount of the share capital and length of incorporation (if limited). The company is obliged to file any changes in this information to the National Court Register within seven days of the change being made.

Moreover, the management board is required to prepare and file with the National Court Register an annual financial statement along with a management board report on the operations of the company. The annual financial statement should be prepared no later than three months following the end of the company's financial year and be approved by the shareholders at the ordinary general meeting no later than six months following the end of the financial year. As opposed to a limited liability company, all resolutions adopted at the general meeting of a joint-stock company must be recorded by a notary in order to be valid.

Investors assess the development prospects and financial condition of a company based on information provided by the participants of the regulated market, therefore listed companies have some additional reporting obligations. In general, public companies must publish information on all events that significantly influence the company's net worth, financial condition and results of operations that may affect the price or value of its shares. The reporting obligations of the WSE listed companies include:

- reports on events concerning the WSE listed company or its subsidiary such as acquisition and sale of shares;
- reports on transactions of persons performing specific functions in the company;
- quarterly reports containing unaudited short versions of quarterly financial statements;
- semi-annual reports containing audited short versions of semi-annual financial statements; and
- annual reports containing audited annual financial statements prepared in accordance with binding accounting principles.

Furthermore, on 3 July 2016 the new EU Market Abuse Regulation took direct effect in all EU member states. The Market Abuse Regulation introduced a material change with regard to the disclosure requirements of public companies, which now themselves have to determine whether a particular event should be regarded as inside information and disclosed to the market.

Update and trends

Compared to 2015, 2016 brought a slowdown to the Polish capital market. Nevertheless, the country's strong underperformance in foreign fund portfolios and relatively cheap currency made Warsaw's market more attractive, and it seems that much of the weakness of the WSE has already passed. According to forecasts, in 2017 blue chip companies will continue to be the leaders on the Polish stock market. Such a strong position of listed companies requires a higher level of transparency from them. Although observance of corporate governance in Poland is still not the same as in more highly developed markets, it has made significant progress in recent years. According to the report 'Supervisory Boards 2017: Trends and Directions of Change' provided by the WSE, only 22 per cent of 487 companies listed on the WSE have not fulfilled the information obligation contemplated in the 'Best Practices of WSE Listed Companies', a code of corporate governance. The report states that companies mostly struggle with complying with the rules regarding the organisation and broadcasting of the electronic general meetings, remuneration policies, diversity policies, conflicts of interest and the independence of the members of the supervisory board.

The implementation of the Market Abuse Regulation (MAR), which took effect from 3 July 2016 throughout the entire European Union and replaced the previous Polish market abuse regimes, did not make the corporate governance for WSE listed companies any easier. As the Polish legal system has not yet been adjusted to MAR, companies are forced to apply its provisions directly. Issuers struggle in particular with the definition of 'inside information' and the related disclosure requirements. With local provisions non-existent, it is unclear which information and to what extent must be disclosed. Thus, companies listed on the WSE currently tend to disclose more than necessary or to disclose information based on previously applicable provisions of the Public Offering Act.

Hot topics

37 Say-on-pay

Do shareholders have an advisory or other vote regarding executive remuneration? How frequently may they vote?

Shareholders do not have a binding say-on-pay on remuneration policy. The remuneration of the members of the management board is determined by the supervisory board. The general meeting may authorise the supervisory board to decide that the remuneration will also include the right to a specified share in the annual profit of the company designated for distribution among the shareholders. The supervisory board has full discretion in deciding on the remuneration of the board members unless it is not against the law (eg, in companies owned by the state treasury there is a cap on remuneration) or the company's articles of association. Nonetheless, granting excessive remuneration may trigger an action for damages caused to the company against members of the supervisory board. The articles of association may vest the right to determine the remuneration of board members to the general meeting; however, it is rather unusual in practice.

In April 2014, the European Commission has made a proposal to revise the existing Shareholders' Rights Directive (Directive 2007/36/EC) that would introduce a binding say-on-pay on remuneration policy for listed companies with their registered offices in EU member states. The draft Directive would require companies to put on a vote of their shareholders a remuneration policy that would include a maximum amount of remuneration. In Poland, where a two-tier system stipulates the supervisory board with the responsibility for the remuneration of the board members, it would still be the supervisory board that would develop the remuneration policy to be submitted to shareholders for confirmation. What is more, it would still be for the supervisory board, on the basis of the policy, to decide on the actual remuneration to be paid.

Finally, the framework for restrictions on the amount of remuneration for credit institutions and investment firms has been proposed in Directive 2013/36/EU. The Directive has introduced a maximum ratio of 1:1 between the fixed and variable component of total remuneration, with some flexibility provided for shareholders to approve a higher ratio up to 1:2. This Directive has been implemented into Polish law, by way of an amendment to the Polish Banking Act with the Act on macroprudential supervision over the financial system and crisis management of 5 August 2015. In March 2017 the European Parliament voted on its report on the revised Shareholders' Rights Directive. Its adoption will follow in 2017 and its entry into force will occur two years after its publication in the official journal. Under the revised Shareholders' Rights Directive, shareholders will be granted information and will be able to influence the company's directors' salaries by voting twice: firstly on the framework within which remuneration will be awarded and secondly ex post on the remuneration granted in the past financial year. The revised Shareholders' Rights Directive should guarantee a stronger link between pay and performance, but it is yet to be seen how and to what extend the new provisions will be implemented in Poland.

38 Shareholder-nominated directors

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

The shareholders nominate the members of the supervisory board at the general meeting. Afterwards, members of the management board are nominated by the supervisory board. However, the articles of association may confer this right upon the general meeting or a particular shareholder. In such a case, a shareholder or shareholders representing at least one-twentieth of the share capital (or less if so provided under the relevant provisions of the articles of association) may demand an extraordinary general meeting to be convened and certain issues to be put on the general meeting's agenda. If convened, the extraordinary general meeting should adopt a resolution determining whether the costs of convening and holding the general meeting should be borne by the company. The shareholders at whose request the meeting has been convened may address the registry court to be released from the obligation to bear the costs imposed under the resolution of the general meeting. Moreover, shareholders representing at least half of the share capital or at least half of the total number of the votes in the company may convene an extraordinary general meeting. However, Polish statutory law is silent on whether, in such case, the costs should be borne by the convoking shareholders, or the company. It seems that in this case, there should also be an obligation to adopt a resolution determining whether the costs of convening and holding the general meeting should be borne by the company, but it is unclear who should bear the cost if the general meeting fails to adopt a resolution in this regard.

39 Shareholder engagement

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

Ownership and control of companies are separated. The shareholders entrust their management with capital and delegate the right to manage and dispose of it in their interest. The basis for this transfer of rights to dispose of capital is an implicit contract between shareholders and managers.

Although the Commercial Companies Code does not use the term 'supervision' in relation to the engagement of the shareholders, their actions still fit within that concept as it includes the ability to investigate and evaluate the performance of the company's management as well as the authority to interfere with it in order to ensure the correct operation of the company. Such supervision, in its institutionalised form, is performed during the general shareholders' meetings, during which the 'economic owners' of the company periodically control the actions of its management and are entitled to decide on their organisational and civil responsibility. An important principle of modern corporate governance is the requirement of corporate loyalty while the shareholders exercise their statutory rights. Shareholders performing corporate supervision must ensure to carry it out in a loyal manner,

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meaning in good faith and with due regard to the legitimate purposes and interests of the company and other shareholders.

Shareholders have the right to control the management of the company directly by exercising voting rights at the annual meeting to grant discharge to the members of the governing bodies of the company (management board and the supervisory board). Shareholders may also require access to company documentation prepared for the annual meeting, primarily the annual financial statements of the company (balance sheet, profit and loss account, and cash-flow statement) and other documents if justified for the assessment of matters included in the agenda. Shareholders also have the right to ask questions at the annual meeting to the management board and the supervisory board.

Further regulations in order to encourage long-term shareholder engagement will be introduced into the Polish legal system probably with the implementation of the revised Shareholders' Rights Directive (described in question 38), which should enter into force in 2019.

Romania

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Sources of corporate governance rules and practices

1 Primary sources of law, regulation and practice

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

The law (referring here to the broad sense of the word and thus including laws, decrees, regulations, government decisions, etc) is the sole available option for regulating a specific matter in Romania. As opposed to common law jurisdictions, the Romanian legal system does not recognise precedents as a source of law. As such, the main legal framework covering corporate governance is provided by Companies Law No. 31/1990 (the Companies Law) and Trade Registry Law No. 26/1990.

In addition, there are special regulations applicable to listed companies and to state-owned enterprises.

Listed companies are subject to special corporate governance rules provided by Capital Markets Law No. 297/2004 and to the regulations issued by the specific regulatory authority in this field, namely the Financial Supervisory Authority (FSA). Among such specific regulations, FSA Regulation No. 1/2006 regarding issuers and securities operations (FSA Regulation No. 1/2006) and FSA Regulation No. 6/2009 regarding the exercise of certain shareholders' rights in connection to companies' general shareholders' meetings are the most important.

Moreover, the Bucharest Stock Exchange has issued a Corporate Governance Code, which establishes principles of corporate governance and provides recommendations. Even though the Code is not mandatory, listed companies are under the obligation to disclose, in their annual reports, whether the company complies with the provisions of the Code and, if not, the reasons for such non-compliance (the Corporate Governance Compliance Statement – the 'comply-or-explain' statement).

State-owned enterprises are subject to Corporate Governance Emergency Ordinance No. 109/2011 (GEO No. 109/2011).

2 Responsible entities

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

Under the Romanian Constitution, the Parliament, following parliamentary or government initiative, is the primary authority in charge of the enactment of binding laws and regulations, including those regarding corporate governance. Also, the Romanian government may issue legislative acts such as decisions and emergency ordinances.

In addition, other authorities (the National Bank of Romania (NBR) and the FSA) are empowered to issue secondary norms and regulations enforceable in their supervisory field.

Regarding the proxy advisory firms, the tumultuous discussions on the EU context will not lead, at least in the short term, to significant changes in Romania, taking into consideration that, in our market, there are no proxy advisory firms.

The rights and equitable treatment of shareholders

3 Shareholder powers

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

As a matter of principle, shareholders enjoy exclusive competence to appoint and remove directors in all types of companies, by means of a secret ballot. There are two ways to appoint directors: through the statutory documents (particularly as regards the composition of the first board of directors) and by the shareholders' meetings.

The above is particularly true with regard to joint-stock companies. Directors under the one-tier system (board of directors) are appointed by the resolution of an ordinary shareholders' meeting, voting by simple majority, except for the first directors, who are appointed through the statutory documents of the company. Shareholders are entitled, by resolution of the shareholders' meeting, to remove the directors at any time, by means of resolution of an ordinary shareholders' meeting, voting by simple majority. Directors are not permitted to challenge the removal decision, but they may seek damages if the removal is made without proper cause.

As an exception to the general rule, in the two-tier system (directorate and supervisory board), the members of the directorate (who oversee the management of the company in a way that is similar to the executive officers in the one-tier system) are appointed and removed by the supervisory board (with the latter being appointed and revoked by the shareholders), the shareholders only being in charge of the appointment and removal of the members of the supervisory board. The constitutive act of one company can provide that the members of the directorate be revoked also by the ordinary shareholders' meeting.

Deriving from its subordination to the shareholders' meeting, the board must take all required action to implement the decisions of the shareholders' meeting.

In listed companies and in state-owned enterprises, shareholders may appoint the members of the board of directors (under the one-tier system) and members of the supervisory board (under the two-tier system) based on the cumulative voting rights system. According to this method, a shareholder is entitled to assign its cumulative votes (ie, votes resulting from multiplying the votes held by it in the company's share capital with the number of directors composing the company's board) to one or more persons nominated for a board position. The existing members of the board of directors or the members of the supervisory board are automatically recorded as candidates for election in the new board of directors and, if they are not re-elected, they are considered revoked.

Upon the request of a significant shareholder (holding at least 10 per cent of the share capital), appointment by this method is mandatory.

4 Shareholder decisions

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

The shareholders' meeting decides on all major issues concerning the company such as:

- discussion, approval or amendment of the annual financial statements, including dividend distribution;
- appointment and revocation of directors, members of the supervisory board and auditors and establishment of their remuneration;
- the company budget and the business plan for the following financial year;
- change of the company's legal form;
- change of the headquarters of the company;
- change of the company's main business scope of activity;
- increase or decrease of the registered capital;
- setting up or dissolution of potential secondary offices;
- extension of the duration of the company's existence;
- approval of the voluntary dissolution of the company;
- merger or spin-off of the company;
- conversion of shares from one category to another (eg, nominative to bearer shares);
- conversion of bonds from one category to another or to shares; and
- issuance of bonds.

By means of statutory documents or decision of the extraordinary general meeting of the shareholders, certain powers may be delegated to the board of directors or directorate such as: change of the headquarters of the company; change of the business activities (except for the main business activity); and an increase of the share capital. According to the Companies Law, there are no matters subject to a non-binding (consultative) vote of the shareholders.

Any shareholder who did not participate in the shareholders' meeting or voted against is entitled to challenge the decisions that are contrary to the law or to the constitutive act of the company by filing a contestation action within 15 days as of the publication of the decisions in the Official Gazette of Romania.

5 Disproportionate voting rights

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

The main rule is 'one share, one vote'. However, joint-stock companies may issue preferred shares without voting rights, entitling the shareholders to a preferential distribution of dividends. Such shares are subject to specific limitations, for instance, they cannot exceed a quarter of the company's share capital and shall have the same nominal value as the ordinary shares. Also, members of the board, executive officers, members of the directorate or of the supervisory board cannot hold such preferred shares. Although the holders of preferred shares may participate in the shareholders' meetings, they do not have voting rights. If the company delays the paying of dividends, within specific conditions, preferred shares acquire voting rights. The extraordinary meeting of shareholders might decide on the conversion of preferred shares into ordinary shares or vice versa.

Other exceptions are allowed through the statutory documents in respect of shareholders holding more than one share. There are no specific rules on the limits of such exceptions, to the extent where they do not amount to a disproportionate distribution of dividends. Typically, such exceptions take the form of extraordinary veto rights on specific matters and other specific mechanisms such as quorum conditions, supermajorities, limitation of the voting rights for shareholders exceeding a specific share stake.

6 Shareholders' meetings and voting

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

Shareholders may only vote within their general meetings; the shareholders registered as such at the reference date mentioned in the convening notice are entitled to attend the meeting and vote. Shareholders' meetings are convened by the board of directors or by the directorate, whenever necessary, the meeting being held no sooner than 30 days as of the publication of the convening notice in the Official Gazette and in a highly circulated newspaper.

Shareholders may participate in general meetings either personally or via a representative holding a power of attorney in this respect. There are limitations concerning the possibility of representing the shareholders, more precisely, the directors, members of the directorate or of the supervisory board or the employees of the company cannot represent the shareholders, the sanction being the nullity of the decision of the general meeting of the shareholders if, without their votes, it would not have been possible to achieve the required majority.

Shareholders holding 100 per cent of the share capital of a company can decide to waive any and all formalities or procedural conditions with respect to the summoning, convening and holding of the general meeting of shareholders.

In the case of joint-stock companies, the powers of attorney must be submitted with the company at least 48 hours before the shareholders' meeting (or in another such term provided by the company's bylaws), under the sanction of losing the voting rights for that respective meeting. Shareholders holding preferred shares are not allowed to vote in general meetings; however, they are allowed to vote in the special meetings of such holders. Holders of bearer shares are allowed to vote only if they deposit such shares at the places provided by the statutory documents or by the convening notice at least five days before the general meeting. Voting rights in respect of unpaid shares are suspended until the full payment of such shares.

When a conflict of interest between the company and one of the shareholders arises, the latter is required to refrain from voting, otherwise such shareholder will be responsible for the damages caused to the company if a majority was not able to meet without him or her. The Companies Law also prohibits the shareholders who are directors, members of the directorate or of the supervisory board from voting with respect to their annual management discharge or, generally speaking, related to any other issue regarding their management.

The shareholders cannot generally act by written consent without a meeting; however, acting by written consent is usually practised in cases of non-listed companies, if the constitutive act provides this possibility and the written consent is signed by all shareholders.

Virtual meetings are expressly allowed for listed companies; they are possible for non-listed companies if the constitutive act expressly provides for it and with shareholders' consent.

7 Shareholders and the board

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

In this respect there is a rather official procedure, which joint-stock companies (at least) must observe. As such, the main rule is that convening notices must be published both in the Official Gazette and in a highly circulated newspaper in the city where the company has its main seat at least 30 days prior to the meeting.

Although meetings are generally convened by the board, in the case of joint-stock companies, shareholders owning a certain number of shares (at least 5 per cent of the share capital, but possibly less if so stipulated in the company's statutory documents) may require the board of directors, respectively the directorate, to convene the shareholders' meeting or to amend its agenda. Such meeting must be convened within a maximum of 30 days and held within a maximum of 60 days as of the shareholders' request. However, the convening procedures cannot be carried out directly by the shareholders.

Should the board of directors or directorate fail to comply with such request, the shareholders are entitled to request authorisation to convene a general meeting in court. Through the same court judgment, the court will set the agenda, the reference date, the day when the general meeting shall take place and the shareholder who will chair the meeting.

Also, shareholders owning at least 5 per cent of the share capital may request the board to include new items on the agenda within a maximum of 15 days as of the publication of the convening notice. The supplemented agenda completed with the requested items shall be published at least 10 days prior the day of the shareholders' meeting.

In limited liability companies, the board must convene the shareholders' meeting at the request of the shareholders representing at least a quarter of the share capital of the company.

Dissenting shareholders can request that their opinion be included in the minutes of the shareholders' meeting – minutes to which any of the shareholders may have access upon request.

8 Controlling shareholders' duties

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

Controlling shareholders do not owe specific duties to the company or to the non-controlling shareholders, apart from the general obligation to exercise their rights in good faith and by avoiding majority abuses, respecting the rights and the legitimate interests of the company and of the other shareholders. Controlling shareholders, like any other shareholders, are also obliged to avoid voting in situations where there is conflict of interest. If, despite this rule, they use their vote to force a decision in the shareholders' meeting, they may be held liable for the damages caused to the company as a result of such decision, as the case may be.

With regard to majority abuses, Romanian case law has frequently been confronted with situations in which majority shareholders exercised their voting right in discretionary ways, aiming to satisfy their individual interests, in a way that harmed the company's interest or that of the minority shareholders. Generally, majority abuses, especially if the majority shareholder is acting in bad faith, trigger the annulment of the general meetings' decisions.

In theory, a non-controlling shareholder may also check the validity of an apparently legal decision taken by the controlling shareholder on grounds of majority abuse. Such legal actions must usually be filed within a term of 15 days from the publication of the shareholders' resolution in the Official Gazette.

9 Shareholder responsibility

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

Shareholders in joint-stock and in limited liability companies (which are by far the most common forms of companies used in practice) may be held liable for the company's obligations only to the extent of their contribution to the registered capital, unless the shareholders expressly agreed otherwise.

Nevertheless, there are specific situations where shareholders' liability might be extended. As such, the founding shareholders are jointly and severally liable for the complete subscription and payment of the share capital or for providing true and complete data during the incorporation process.

Secondly, in the event of the company's insolvency, shareholders' liability may be extended if it is proven that the insolvency was caused by the shareholders, by way of activities such as using the assets or credit of the company in their own or a third-party's interest, performing commercial operations for their personal interest under the protection of the company or continuing an activity that obviously led to the cessation of payments.

In the case of dissolution or liquidation of the company, shareholders that have fraudulently abused the limited nature of their liability might be held liable for the unpaid debts of the company.

Corporate control

10 Anti-takeover devices

Are anti-takeover devices permitted?

There are no specific anti-takeover devices under the Companies Law, despite the fact that anti-takeover defences are not prohibited in Romanian law. Moreover, Romania did not transpose the prohibition from article 11 of the EU Directive on Takeover Bids preventing companies from using various devices in order to defend themselves from takeover bids. Yet, Romanian companies seem to still be reluctant to implement such clauses in their statutory documents.

However, Romania strengthened board neutrality through measures such as, for example, prohibiting the board of the company subject to takeover (after the receipt of the preliminary notice) from concluding any act or taking any measures that may affect its assets or the objectives of the takeover, except for current administrative acts (from the perspective of the Capital Markets Law, operations that are considered to affect the company's assets include, without limitation, share capital increases or securities issues granting the right to subscribe or convert into shares and encumbrance or transfer of certain assets representing at least one-third of the net asset according to the company's latest annual balance sheet). As an exception to this rule, only operations deriving from obligations assumed prior to the publication of the takeover notice and those operations expressly approved by the extraordinary general meeting called for that purpose after the preliminary notice may be performed.

In listed companies, the intention of an investor to take control over a company by acquiring more than 33 per cent of its voting rights is specifically conditioned. The investor has to submit a preliminary takeover announcement to FSA, whose approval is required. Subsequent to FSA approval, the announcement has to be submitted to the company, to the regulated market on which such securities shall be traded and shall be published in at least one central and one local newspaper within the administrative and territorial area of the issuer. The board of directors then has five days to inform FSA and the offeror about its opinion with respect to the takeover. The board may then convene a shareholders' meeting in order to inform the shareholders about the board's opinion with respect to the takeover. The convening of the shareholders' meeting is mandatory for the board if it is requested by shareholders holding at least 10 per cent of the share capital, the convening notice being published within five days as of the request and the shareholders' meeting being held within five days as of the publication of the convening notice in a national newspaper. From the date of the receipt of the preliminary notice and until the closing of the offer, the board of directors shall inform FSA and the regulated market of all operations performed by the members of the board of administration and of the executive management regarding such securities. The specific regulations are in line with the EU Directive on Takeover Bids, the sell-out and squeeze-out procedures being regulated even before the transposition of the Directive.

11 Issuance of new shares

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

Authorising the board of directors or the directorate to increase the share capital is an exception from the rule according to which the decision to increase the share capital belongs to the extraordinary general meeting of shareholders. The board of directors or the directorate may be entitled by the statutory documents or by a resolution of the shareholders to increase the share capital up to a determined nominal value (authorised capital) by issuance of new shares. Such authorisation is limited to a certain period of time (which cannot exceed five years from the date of the company's registration or from the shareholders' resolution) and to a value that cannot exceed half of the subscribed share capital.

In the case of listed companies, the board of directors may be entitled to increase the share capital within one year; this period of time can be renewed for subsequent periods of one year each time. Such decisions of the board of directors can be challenged by any shareholder under the same conditions as those for the decisions of the general meetings of shareholders.

As a rule, newly issued shares have to be offered first to the existing shareholders, proportionally to the number of shares held in the share capital of the company, or to the number of pre-emptive rights held, in the case of listed companies in which the share capital increase is preceded by transfer of such rights. The term for exercising the pre-emptive right is at least one month from the publication in the Official Gazette of the shareholders' meeting resolution approving the share capital increase. For justified reasons, which the board of directors has to explain to the shareholders through a written report, the pre-emptive right may be limited or denied through a resolution of the extraordinary general meeting of shareholders, taken with the majority of the votes of the present shareholders (the Companies Law demands that the shareholders representing three-quarters of the subscribed share capital to be present for the validity of such resolutions).

12 Restrictions on the transfer of fully paid shares

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

In non-listed joint-stock companies, restrictions on the transfer of fully paid shares are permitted through the company's statutory documents, meaning that the only available restrictions for Romanian companies are conventional restrictions and not legal mechanisms. Most commonly used restrictions are provided in the statutory documents and include drag-along and tag-along rights, as well as the right of first refusal. These may be combined with specific lock-up periods (usually up to three to five years).

In limited liability companies, share transfers to third parties require the approval of the shareholders representing at least three-quarters of the share capital. The statutory documents may require higher majorities.

In listed joint-stock companies, no such restrictions are possible.

13 Compulsory repurchase rules

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

Under the Companies Law, compulsory repurchase is stipulated with respect to dissenting shareholders who decide to withdraw from the company because they do not agree with the decisions of the shareholders' meetings changing the main business scope or the legal form of the company, relocating the registered offices abroad, or deciding on the merger or spin-off. In this case, the dissenting shareholders must exert their withdrawal right within 30 days from the publication of the corporate decision with the Official Gazette in all cases, except for that of a merger or spin-off, when the term elapses from the moment when the merger or spin-off operation is approved. The price that shall be paid by the company to the shareholder exercising his or her right to withdraw from the company in these conditions is computed by an independent authorised expert, the evaluation costs also being paid by the company.

In listed companies, the shareholder who, pursuant to carrying out a public offering addressed to all shareholders and for all their holdings holds shares representing at least 95 per cent of the total number of shares in the share capital granting the right to vote and at least 95 per cent of the voting rights that can actually be exercised; or has acquired, during the public offering, shares representing at least 90 per cent of the total number of shares in the share capital granting the right to vote and at least 90 per cent of the voting rights envisaged during the offering, is entitled, no later than three months from the public offer, to request shareholders who have not subscribed to the offering, to sell those shares at a fair price. Once this procedure is finalised, the company is delisted. The Capital Market Law also provides for a 'sell-out' mechanism for the minority shareholders, allowing them the right to request the majority shareholder that finds itself in any of the above-mentioned situations to acquire their shares.

Also, in listed companies, the shareholders who did not agree with the resolutions of the general meeting in connection to mergers or divisions (which implies the distribution of shares that are not admitted to trading on a regulated market) are entitled to withdraw from the company and to obtain payment from the latter for their shares.

There is an additional repurchase allowed, applicable only to limited liability companies: the shareholder who does not obtain the unanimous agreement of the rest of the shareholders is entitled to ask the court to issue a withdrawal judgment, provided that there are legitimate reasons justifying such request.

14 Dissenters' rights

Do shareholders have appraisal rights?

Dissenting shareholders (see question 13) have the right to sell their shares at a price computed by an independent authorised expert.

The responsibilities of the board (supervisory)

15 Board structure

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

The majority of the companies prefer the one-tier system, the management powers being usually delegated by the board to a general director.

16 Board's legal responsibilities

What are the board's primary legal responsibilities?

In the case of joint-stock companies, the board has the following main responsibilities that cannot be delegated to directors:

- to decide on the company's long-term or periodic business plan;
- to establish the accounting and financial control systems and to approve the annual financial planning;
- to appoint and remove the executive officers and establish their remuneration;
- to ensure the control of the executive officer's activity;
- to draft the annual financial statements, convene the shareholders' meeting and implement its resolutions; and
- to submit the request for opening the insolvency procedure.

The board of directors cannot delegate to the directors those responsibilities that have been delegated from the extraordinary shareholders' general meeting to the board of directors.

17 Board obligees

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

The board represents the company and not the shareholders, and owes legal duties to the company itself and not to the shareholders.

18 Enforcement action against directors

Can an enforcement action against directors be brought by, or on behalf of, those to whom duties are owed?

Enforcement actions can be brought against directors, members of the directorate and of the supervisory board who are in breach of their duties towards the company for the damages caused to the company.

The prerogative to decide on the initiation of legal action belongs to the ordinary shareholders' meeting. When taking such a decision, the shareholders' meeting shall also appoint the person representing the company in court against the director. When deciding on the annual financial statement, the ordinary shareholders' meeting may decide on the directors' responsibility even though this matter is not on the agenda. In the one-tier system, the mandate of the board members, and in the two-tier system, the mandate of the directorate, ceases automatically when the shareholders' meeting takes such a decision. As a result, the ordinary shareholders' meeting, respectively the supervisory board, will proceed with their replacement. If the action is held against the directors, their mandate is suspended until the judgment becomes irrevocable.

The ordinary shareholders' meeting can also decide to exercise the legal action against the supervisory board, their mandate ceasing automatically, furthermore the shareholders deciding on their replacement.

If the shareholders' meeting fails to make a decision, the shareholders representing, jointly or individually, at least 5 per cent of the company's share capital are entitled to bring legal action against the directors in breach, in their own name, but on behalf of the company.

19 Care and prudence

Do the board's duties include a care or prudence element?

The members of the board have to fulfil their duties with the prudence and diligence of a good manager. They also owe to the company a duty of loyalty, and their actions must be in the company's interest. The board will not be in breach of its duties if in taking the relevant decision and based on the available information, it could have reasonably believed that it was acting in the interests of the company ('the business judgement rule').

20 Board member duties

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

There are no specific regulations in this respect, all board members have the same duties towards the company and act as a collegial body. It will be the board's internal decision to give specific duties to individual members by considering their experience and skills, but the decisions of the board will still be taken as a collective body and the responsibility will belong as such to the board members, regardless of the nature of the matter decided on.

Where the board elects to delegate its management responsibilities to executive officers, the latter may be entrusted with different operational attributions according to their experience or skills.

If the board sets up various board committees with consultative roles (as described in question 25), such as remuneration or audit committee, its members shall have the duties indicated by the board of directors.

21 Delegation of board responsibilities

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

Under the one-tier system, the board may delegate the management of the company to one or several executive officers from inside or outside the board. However, if such management powers are delegated, then the majority of the board must be composed of non-executive officers. As an exception, certain powers cannot be delegated to executives, such as those listed in question 16, along with those delegated to the board by the extraordinary general meeting of shareholders (eg, change of the company's headquarters, increase of the registered capital). Such delegation is mandatory for a joint-stock company whose financial statements are subject to compulsory financial audit obligations.

In the two-tier system, the management is entrusted to the directorate, while the supervisory board strictly controls the way the directorate manages the company.

For specific operations, the board may also narrowly delegate some of its attributions to other persons, on a case-by-case basis.

22 Non-executive and independent directors

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

Where the management of the company is delegated by the board to executive officers (because it is required by the shareholders or by law) members of the board may also be appointed as executives. However, in such case, the majority of the board must be represented by non-executive directors. As regards their responsibilities, the executives may hold representation powers, while the non-executives hold only supervisory powers. By 'non-executive' directors, the Companies Law simply understands this to be those members of the board of directors who do not have day-to-day management and representation responsibilities.

Moreover, based on the statutory documents or on the resolution of the shareholders' meeting, one or more members of the board of directors may be independent directors. In assessing directors' independence, the shareholders' meeting may consider, inter alia, the following criteria:

- he or she should neither be nor have been a director of the company or of one of its subsidiaries during the past five years;
- should not have maintained an employment relationship with the company or its subsidiaries during the past five years;
- must not be a significant shareholder of the company;
- should neither be nor have been an auditor of the company or of a subsidiary during the past three years; and
- there should be no potential conflict of interest.

The independent directors have the same legal duties towards the company as the rest of the members of the board, but they play a significant role in aspects such as developing the company's strategy from an external perspective, monitoring the management, solving the conflicts of interest.

Under the Corporate Governance Code (applicable only to those listed companies that voluntarily adopted it), there is the recommendation that an adequate number of non-executive directors be independent, in the sense that they do not maintain, nor have they recently maintained, directly or indirectly, any business relationship with the listed company or persons linked to the listed company of such a significance as to influence their autonomous judgement. Renunciation to a term, by an independent director, shall be accompanied by an extensive, detailed statement regarding the reasons for such action.

23 Board size and composition

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

Generally speaking, there are no criteria related to age, nationality, diversity, expertise, insolvency or similar criteria, except for the cases mentioned below.

A person cannot be appointed as director if previously sentenced for any of the following criminal offences: fraudulent management, breach of trust, embezzlement, forgery, perjury, bribery, tax evasion, crimes relating to money laundering and terrorist acts. However, in the case of specialised entities, such as credit institutions, insurance companies and investment firms, the directors must have adequate experience in their corresponding field of activity (eg, banking, insurance, investments). In the case of insurance companies, at least one of the board members must speak Romanian.

There are no disclosure requirements relating to board composition, except for certain identification data of the directors that need to be included in the statutory documents and, as such, are subject to public disclosure by registration with the Trade Registry (eg, full name, citizenship, date and place of birth).

In the case of the one-tier system in joint-stock companies, the board is composed of an odd number of directors, determined by the shareholders' meeting. In the two-tier system, the directorate board is composed of an odd number of directors and the number of the members of the supervisory board is established by the constitutive act, and cannot be lower than three and higher than 11. If the financial statements of the company are audited, the board of directors (the directorate) will have at least three members. In the case of limited liability companies, there are no limits, the company being managed by one or more directors, as determined by the shareholders' meeting.

State-owned enterprises are managed by a board of directors composed of five to nine members who have to meet the following requirements:

- relevant experience within the management of a profitable state-owned enterprise engaged within the business scope of the company in question; and
- at least one of the board of directors should have undertaken economic studies and have five years' experience within the economic, accountancy or audit fields.

In the case of a vacancy of one or more director positions, unless otherwise provided by the company's by-laws, the board shall appoint temporary directors until the ordinary shareholders' meeting is held. If the vacancy causes a decrease in the number of directors below the minimum legal number, the remaining directors shall promptly convene the ordinary shareholders' meeting. Should the board of directors fail to comply with such request, the shareholders are entitled to request the court to appoint the person entitled to convene an ordinary shareholders' meeting that will elect the members of the board of directors.

24 Board leadership

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

The Companies Law expressly allows the board chairman to function as CEO, but ultimately it is up to the shareholders or the board to decide how to deal with this issue. The common practice is to join the two functions, so that the chairman also acts as CEO. This is generally seen as best practice in one-tier structures, particularly where the chairman's role is not merely decorative.

When the same person is both board chairman and CEO, the Corporate Governance Code provides for the listed companies that there should be a clear separation between the responsibilities of the two positions.

In the case of state-owned enterprises, the board chairman cannot also be appointed as CEO.

25 Board committees

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

The general framework provided by the Companies Law does not impose the obligation to establish specific committees. However, the board can set up consultative committees of at least two members of the board. The responsibilities of such committees include investigations and recommendation for the board with respect to different key areas of interest, such as financial audit, remuneration of directors, executive officers and employees or candidacy for different management positions. At least one of the members of such committees must be a non-executive independent director.

Furthermore, the audit and remuneration committees must only be composed of non-executive directors. The committees are compelled to regularly submit reports to the board concerning their activities. Similarly to the board of directors, in the two-tier system, the supervisory board may also establish consultative committees in order to carry out investigations and make recommendations to the directorate with respect to its activities.

In the case of specific entities, there is, however, the obligation to establish certain committees. For example, credit institutions have the obligation to establish an audit or remuneration committee, or both, as per NBR Regulation No. 18/2009; state-owned enterprises should establish a remuneration and nomination committee and an audit committee, as per GEO No. 109/2011.

The Corporate Governance Code (applicable only to those listed companies that voluntarily adopted it) makes the recommendation for the listed companies to create a nominalisation committee, a remuneration committee and an audit committee.

26 Board meetings

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

In the one-tier system, the board of directors is required to organise board meetings at least once every three months. The board meetings are convened by the chairman, but can also be convened upon the justified request of at least two members of the board or the CEO. The convening notice shall be sent in due time; however, a specific term to be observed can be set by the board. In the two-tier system, the supervisory board is required to organise meetings at least once every three months; the directorate has a duty to present written reports regarding the company's management to the supervisory board every three months.

27 Board practices

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

Disclosure of board practices is not expressly required. Nevertheless, information regarding the members of the board of directors and the executives holding representation powers has to be made available at the Trade Registry for any interested person.

28 Remuneration of directors

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

As a general comment, the board members and the executive officers of joint-stock companies cannot perform their duties based on employment contracts, but only based on service or mandate contracts. In the case that such persons are appointed from among the company's employees, then their respective employment contracts shall be suspended for the duration of the mandate.

The basic (as well as any additional) remuneration of the board of directors and of the supervisory board is established by the statutory documents or by the shareholders' meeting. The remuneration of the executive officers and of the members of the directorate is established by the board of directors and the supervisory board, respectively. The remuneration package should normally be justified by the specific functions of the members and by the status of the company, but otherwise there are no specific legal limitations as to the value of the remuneration.

Compensatory arrangements are not widely used in Romania. While they are not illegal per se, it should be thoroughly investigated if such payment would not ultimately determine the directors to breach their obligations of independence and loyalty towards the company, and not towards specific shareholders.

In joint-stock companies, the length of a director's mandate is stipulated in the statutory documents and it cannot exceed four years, with the possibility of being renewed. However, the duration of the mandate of the first members of the board is limited to two years. In limited liability companies the mandate of the director can be established for any duration, even for an indefinite period of time.

The company is not allowed:

- to grant loans to its directors;
- to grant financial advantages to the directors following the execution of agreements between the company and the directors for the sale or purchase of goods or for the execution of works or services;
- to guarantee, fully or partially, any loans granted to its directors;
- to guarantee, fully or partially, the execution by its directors of any obligations undertaken by the directors towards a third party; or
- to acquire a receivable, having as its subject matter a loan granted to its directors by a third party.

The prohibitions listed are also applicable to operations involving the spouses or relatives of the directors up to the fourth degree, as well as to those operations involving companies where the directors or the persons indicated above have at least 20 per cent of the share capital. Nevertheless, these limitations shall not be applicable if the value of the operation does not exceed €5,000, or the operation is part of the company's regular business activities and is concluded on an arm's-length basis.

29 Remuneration of senior management

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

There is no specific law or regulation with respect to senior management remuneration. The rules presented in question 28 are applicable to the senior management as well.

30 D&O liability insurance

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

In joint-stock companies, taking out professional liability insurance for the directors, the members of the directorate and the supervisory board is mandatory. The premiums are usually paid by the companies.

31 Indemnification of directors and officers

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

The matter of whether directors and officers may be indemnified by the company in this respect is not covered specifically in the Companies Law. Generally, since the board members are liable only towards the company, and not to third parties, any indemnity from the company is practically excluded. There is also the possibility that the members of the board are liable towards third parties, but this would be an exceptional situation as it is not common for companies to indemnify such directors.

32 Exculpation of directors and officers

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

There are no specific regulations as regards the possibility of companies or shareholders precluding or limiting the liability of directors and officers. As a matter of principle, there can be decisions of the shareholders or even provisions in the charter containing such limitations in various degrees and forms. Such exonerations are, however, debatable in the event of fraudulent or wilful conduct of directors.

33 Employees

What role do employees play in corporate governance?

Employees do not play a formal role in corporate governance, but they may enjoy various degrees of leverage through trade unions or employees' representatives with regard to their position and involvement in the decision-making process of the company; however, this is not a regulated legal matter.

34 Board and director evaluations

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

There is no legal provision regulating the evaluation of the board of directors.

Disclosure and transparency

35 Corporate charter and by-laws

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

Corporate charters and by-laws are registered with the Trade Registry Office and are publicly available. In addition, most listed companies publish these documents on their website, along with other corporate documents.

36 Company information

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

As a general rule, companies are compelled to submit to the Trade Registry all amendments brought to their corporate charter and by-laws. However, in the case of joint-stock companies, there are certain exceptions where such registrations are not mandatory, for example, when changes are made in the shareholding structure. Also, the submission of updated by-laws is not required when board members are replaced (in opposition to limited liability companies where the submission of the updated by-laws in this case is mandatory).

Listed companies have much broader disclosure obligations towards investors, FSA and stock exchange markets. According to FSA Regulation No. 1/2006, the following report categories have to be drafted and submitted by the companies:

- quarterly, biannual and annual reports, including, among others, accounting documents, certain economic and financial indicators, auditors' and board's reports;
- disclosure of privileged information – a listed company must disclose any privileged information concerning the company's activity that can influence the price of shares. Such disclosure must be made in a term of maximum 24 hours, and may refer to aspects such as:
  - board of directors' resolutions regarding the convening of shareholders' meetings or board meetings (in this case when the subject matter of the meeting refers to any of the powers delegated by the extraordinary meeting of shareholders to the board);
  - shareholders' resolutions or board resolutions (in this case when the subject matter of the meeting refers to any of the powers delegated by the extraordinary meeting of shareholders to the board);
  - changes in the direct or indirect control over the company;
  - changes in the management of the company;
  - change of the company's auditor, along with the reasons triggering this change;
  - termination or decrease of the company's contractual relations that generated at least 10 per cent of the company's turnover of the previous financial year;
  - publication of the merger or spin-off project with the Official Gazette;

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- changes of the characteristics or rights of the shares;
- litigations involving the company;
- suspension and resuming of activity;
- initiation and closing of dissolution, judicial reorganisation or bankruptcy procedures; and
- reports regarding the payment of dividends, regarding dividend value and payment term and arrangements.

State-owned enterprises are required to post the following information on their website:

- resolutions of the general meeting of shareholders;
- annual financial statements;
- quarterly accounting reports;
- an annual audit report;
- membership of the company's management bodies, directors' and executive officers' CVs or, as the case may be, CVs of members of the directorate and supervisory board; and
- reports of the board of directors or of the supervisory board.

Hot topics

37 Say-on-pay

Do shareholders have an advisory or other vote regarding executive remuneration? How frequently may they vote?

In a one-tier board structure, the shareholders' meeting establishes the remuneration of the board members. If the management is delegated to executive officers, their remuneration is established by the board. For the two-tier board structure, the remuneration of the members of the directorate is established by the supervisory board. Nevertheless, the shareholders' general meeting is entitled to set the general limits of all remuneration or financial advantages, including those regarding the company's executives. As regards the frequency under which the shareholders decide upon the remuneration of the board members, the law does not impose any specific frequency.

38 Shareholder-nominated directors

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

Any shareholder has the ability to nominate directors within 15 days as of the publication of the convening notice in the Official Gazette and, further, to have their nominations included in the updated shareholder meeting materials. The final decision regarding the appointment belongs to the general meeting of shareholders.

39 Shareholder engagement

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

Romanian companies do not usually engage with shareholders outside the annual meeting season.

Russia

Maria Miroshnikova and Yuri Arkhipov

Ivanyan & Partners

Sources of corporate governance rules and practices

1 Primary sources of law, regulation and practice

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

The Civil Code is the principle source of civil law and its regulation is in most cases superior to other civil laws and enactments. General corporate governance rules are established in chapter 4 of the Civil Code that regulate matters related to legal entities. Provisions of the code that govern commercial enterprises are further developed in the two primary corporate laws – the Law on Joint Stock Companies and the Law on Limited Liability Companies. Both laws were substantially modified within the last 20 years and encountered together up to 100 amendments. It is relevant to note that certain provisions of both laws remain outdated and contradict with the Civil Code regulation, which sometimes makes construction of the law complicated. The harmonisation of the laws and the Civil Code is ongoing and some amendment drafts are currently under consideration of the government and the Parliament.

The issuance of securities by joint-stock companies is governed by the Law on the Securities Market.

Public companies are subject to regulation enacted by the Russian Central Bank that is a unified regulator of corporate governance matters. Listed companies are also required to comply with the listing rules issued by stock exchange and such requirements are generally mandatory.

Another source of corporate governance practice may be found in a non-binding Code of Corporate Governance approved by the Central Bank which contains principles and mechanisms recommended by the Central Bank to listed companies. Compliance with it may be considered as a best practice for major corporations in Russia.

The law leaves a lot of issues related to corporate governance of private companies at the discretion of shareholders and the articles of association of the company become an important source of corporate governance rules.

2 Responsible entities

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

Until 2014 the functions of control over the securities market, issuers, professional participants of the securities market and stock exchanges were performed by the Federal Commission on Financial Markets. In 2014 these powers were consolidated with the insurance authority and passed to the Russian Central Bank. Since 2014, the Russian Central Bank has been the unified authority in the sphere of securities regulation and corporate governance compliance, and performs control over issuers and effectuates registration of issues of securities, prospectus of issue and issue reports.

Proxy services and other shareholder-related services are rarely provided in Russia in the form of a stand-alone business. They may constitute a part of legal or general consulting services but are not common and there is no recognised leadership in this narrow sphere.

The rights and equitable treatment of shareholders

3 Shareholder powers

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

The board of directors of a joint-stock company is appointed by the general meeting of shareholders by a cumulative voting procedure which provides that the number of votes of each shareholder is multiplied by the number of board members and the resulting total number of votes may be distributed by the shareholder among any number of nominees in any proportion. The nominees that gain the highest number of votes are considered appointed as board members. Private companies may opt for a different nomination procedure by introducing it in the articles of association. Such amendment shall be approved unanimously by the shareholders.

The term of service of the board members is limited until the next annual general meeting of the shareholders. If it so happens that the annual general meeting does not take place, the authority of the board members is deemed terminated except for the powers required to organise, convene and conduct the annual general meeting.

Upon nomination, the shareholder is unable to require the board or any of its members to pursue a particular course of action and the board members are required to act not in the interest of any particular shareholders but in the interest of the company.

The shareholders may only dismiss the whole board in the aggregate without any option to dismiss any particular member. The decision to dismiss the board shall be approved by a simple majority of votes present at the general meeting (which threshold may be increased in private joint-stock companies).

As for limited liability companies, the law provides that the board of directors is an optional government body whose creation may be agreed by the members of the company in the articles. In the latter case the articles shall regulate the matters of board formation, working procedures, dismissal of its members and its competence. The law provides for a minimum of procedural limitations which makes the board of directors in a limited liability company much more flexible when compared to the board of a public company.

4 Shareholder decisions

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

The Law on Joint Stock Companies provides that the following issues are exclusively reserved to the shareholders of the company (unless otherwise indicated below):

- amendment and approval of the company's articles of association;
- reorganisation of the company;
- liquidation of the company, nomination of the liquidation commission and approval of interim and final liquidation balance;

- decisions on the number of board members, appointment and dismissal of board members;
- decisions on the number of issued shares, their nominal value, class and shareholder rights granted by such shares;
- increase of the share capital by way of increase of the nominal value of shares or by issuing additional shares unless this issue is delegated by law to the board of directors;
- decrease of the share capital by decrease of the nominal value of shares, by redemption of shares by the company or by cancelling shares that were redeemed;
- formation of the executive body of the company and early termination of its authority unless this matter is delegated to the board by the company's articles;
- appointment and dismissal of the members of the internal audit commission;
- appointment of the company's auditor;
- payment of quarter and annual dividends and other distribution of profit;
- approval of the annual report and annual financial statements, unless it is delegated to the board of directors by the articles;
- approval of procedures of the general meeting of the company;
- appointment and dismissal of the counting commission;
- splitting and consolidation of shares;
- approval of major transactions and interested-party transactions (some transactions may be delegated to the board);
- shares redemption and buyout in cases provided by law;
- participation in a group of companies, association or other unity of commercial legal entities;
- adoption of internal documents of the company;
- listing of shares unless this matter is delegated to the board by the articles of association;
- delisting of shares; and
- other matters as prescribed by law.

For limited liability companies, the list of reserved matters is shorter but is generally similar.

In public companies, the listed matters are reserved for shareholders (unless provided otherwise as described above) and this list may be neither widened nor shortened. Private companies and limited liability companies are free to expand the authority of the general meeting of shareholders (company members) or to delegate particular matters to the board of director (limited liability companies may also delegate some matters to executive bodies) with certain exceptions indicated by law.

Any amendments to the list of matters reserved to the shareholders shall be included in the company's articles of association and require unanimous decision of the shareholders. Limited liability companies may amend the list of reserved matters by at least two-thirds of the total number of votes of all members of the company (some amendments have a higher threshold).

5 Disproportionate voting rights

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

The Law on Joint Stock Companies is clear in stating that each share provides its holder with similar rights. However, the shareholders are free to regulate the voting matters and limits in the shareholders' agreement, which gives much more flexibility. The shareholders may undertake to perform their rights in any particular way, to refrain from such performance or waive such rights. The shareholders' agreement may provide for an obligation of a party to vote in any particular way or to coordinate the voting with other shareholders. It is relevant to note that any breach of such undertaking will not invalidate the voting but will be treated as a breach of civil law obligations and will entitle other parties to claim damages or to exercise other remedies that may be provided in the agreement (such as liquidated damages).

The shareholders of public joint-stock companies are required to notify the company if they obtain a right to control the voting procedure based on the shareholders' agreement. This notice shall be served every time they exceed the following voting control thresholds together with their affiliates: 5, 10, 15, 20, 25, 30, 50 and 75 per cent of votes. Before this notice is served, they may only vote with the number of votes that they had before obtaining such control.

The regulation on the limited liability companies is much more flexible and it states that the articles may provide for a different way of calculation of the number of votes. Inclusion of such regulation in the articles must be approved by all the members of the company.

6 Shareholders' meetings and voting

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

All ordinary shareholders of the company have a right to attend and vote at its general meetings. The holders of preference shares are entitled to vote on limited matters, such as reorganisation and liquidation of the company, re-registration of the public company as a private company and filing an application to be released from disclosure duties.

The notice of the general meeting of shareholders must be served at least 20 days before the meeting, unless the law requires a longer notification period for particular matters of the agenda (30 days if the reorganisation matter is being considered and 50 days for the board election). As for limited liability companies, the notice shall be sent to the members of the company at least 30 days before the meeting (which term may be extended or shortened by the articles of association).

To participate in the general meeting, the shareholder is required to be included in the list of shareholders entitled to participate in the meeting. Such list enumerates the shareholders on a specific date which may not be less than 10 days following the date of the decision to convene the meeting and more than 25 days before the meeting. For some specific matters of the agenda these limits are different.

All the attendees are required to be registered. The shareholders may be present at the meeting in person or by proxy. The powers of the representative shall be certified by the power of attorney to be composed and executed in accordance with requirements of corporate law. In certain cases, such powers may be certified by law or official act.

The shareholders may decide on most of the matters by voting by ballots with a few exceptions identified by law: election of the board and internal audit committee, nomination of the company's auditor, and approval of the financial statements and annual report shall be reviewed at a meeting at which the shareholders must be present. For limited liability companies, the list of exceptions only includes approval of annual reports and financial statements.

Decisions of general meetings of shareholders shall be certified by the registrar of the company (for both public and private companies) or by a notary (only for private companies). If the company has only one shareholder, certification is not required. Decisions of general meetings of members of limited liability companies shall be notarised unless the members unanimously decide otherwise.

7 Shareholders and the board

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

Shareholders that together hold at least 10 per cent of the shares are entitled to request the board to convene an extraordinary meeting of shareholders. If the meeting is already convened, the shareholders that together hold at least 2 per cent of the shares are entitled to include new items in the agenda. There are certain matters that may only be submitted to the general meeting for approval if proposed by the board (unless the articles provide otherwise). Such matters include:

- reorganisation of the company;
- increase and decrease of the share capital;
- establishing the date for dividend calculation for each shareholder;
- split and consolidation of shares;
- approval of interested-party transactions and major transactions;
- redemption of shares;
- participation in a group of companies, associations and other units of legal entities; and
- approval of primary internal documents of the company.

The board may also control any distribution of profit by the general meeting by refusing to recommend such distribution to the meeting or by limiting its amount. In these circumstances shareholders may not decide on any distribution that is in excess of the amount recommended by the board.

If the board refuses to convene the meeting at the request of the shareholders or if it fails to convene it within five days, the shareholders that requested the board to convene such meeting may request the court to obligate the company to convene the meeting.

Any proposal of nominees does not require approval of the board and is described in question 23 in more detail. The law does not regulate the circulation of any documents by the board except for documents that shall be provided to the shareholders in accordance with the legislation requirements.

8 Controlling shareholders' duties

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

The establishment of fiduciary duties of shareholders to the company is not duly elaborated in Russian law and there exist a number of doctrinal disputes on the scope and grounds for such duties. The courts' practice is controversial and there are decisions both supporting and denying such duties in particular cases. Generally, the courts tend to admit that in addition to common duties attributable to any shareholder, controlling shareholders are required to act reasonably and in good faith towards the company. Such approach may be based on the provisions of article 53.1 of the Civil Code, which stipulates that persons who may determine the actions of the company are required to act reasonably and in good faith and are liable for damages of the company caused because of its fault.

Failure to act in such a way may be considered as a material breach of shareholders' obligation. If the company is a private joint-stock company or a limited liability company, this will entitle other shareholders (company members) to submit a claim to court with a request to exclude such shareholder (company member) from the company if such breach resulted in material damage to the company or if it obstructed the normal activity of the company.

If failure to act reasonably and in good faith caused damages to the company, the company may claim such damages from the shareholder. Other shareholders are entitled to submit the same claim in the name of the company based on article 65.2 of the Civil Code.

9 Shareholder responsibility

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

The general principle of corporate law is that the corporation is a legal entity distinct from its members, and the liability of the shareholders of the joint-stock company and of the members of the limited liability company is limited by the value of their shares or participating interest. Other than that, shareholders and members generally are not liable for a company's debts. However, this rule has an exception in cases of subsidiaries being under control of the parent company. Under the Russian Civil Code a company is considered a subsidiary of the parent company if the parent company is entitled to determine decisions of the subsidiary on the grounds of a prevailing participation in the charter capital, pursuant to an agreement or on other grounds. In this case, the parent company is jointly liable with the subsidiary under transactions executed by the subsidiary further to a direction or approval of the parent company except for approval of the transaction by the general meeting of shareholders (company members) of the subsidiary or its approval by government bodies of the parent company. Further, in case of insolvency (bankruptcy) of the subsidiary caused by fault of the parent company, the parent company can be held liable for the subsidiary's obligations in case of property insufficiency.

In most cases, Russian courts are reluctant to attach liability to the parent company for acts or omissions of its subsidiary except for bankruptcy cases, which have a higher chance of imposing liability on the controlling company.

Corporate control

10 Anti-takeover devices

Are anti-takeover devices permitted?

The law does not contain any special anti-takeover devices and was not designed to facilitate their creation. However, shareholders may structure some mechanisms to make takeover actions complicated. The shareholders of a private company have more flexibility in this matter due to an option to increase the number of votes required to make decisions on the general meeting of shareholders and by the governing bodies of the company.

11 Issuance of new shares

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

As a general rule, the increase of the share capital of the company is within the competence of the general meeting of the company. However, the company's articles of association may provide that the issuance of new shares within the total limit of authorised shares indicated in the articles may be delegated to the board of directors of the joint-stock company. In this case, the issue shall be approved by a unanimous decision of board members.

In private joint-stock companies, the shareholders generally have pre-emptive rights to acquire newly issued shares. However, the pre-emptive right may be excluded in the company's articles of association or in a unanimous decision of the general meeting approving the issue of shares.

12 Restrictions on the transfer of fully paid shares

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

Restrictions on the transfer of fully paid shares may only be agreed by the shareholders in the shareholders' agreement. If the shareholders so agree, any further transfer of shares in breach of the obligations under the shareholders' agreement may be contested only if the claimant proves that the transferee knew or should have known of the restrictions established by the shareholders' agreement.

The instrument of shareholders' agreements was introduced in Russian corporate law not long ago and any conclusions on its effectiveness with respect to the restrictions on the transfer of shares would be premature.

13 Compulsory repurchase rules

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

The company is not entitled to require its shareholders to sell their shares back to the company.

However, in certain cases the controlling shareholder of the company may squeeze out other shareholders by requesting them to sell their shares to such shareholder. In order to do so, three requirements shall be met.

First, the controlling shareholder shall become the owner of more than 95 per cent of shares of the company as a result of voluntary or mandatory offers. The voluntary offer is an offer that may be served to all the shareholders by the shareholder that intends to acquire more than 30 per cent of the company shares. The mandatory offer is an offer that shall be served by the shareholder that has already acquired 30, 50 or 75 per cent of the company shares.

Second, at least 10 per cent of the company shares must have been acquired as a result of a voluntary or mandatory offer.

Third, the request for squeeze-out may only be served within six months of the expiry of such voluntary or mandatory offer.

Another option to squeeze out the minority shareholders is triggered in a situation of reorganisation of the company in a form of merger or aquisition. If the sole shareholder of the company being reorganised becomes individually or together with its affiliates an owner of more than 95 per cent of shares of the new public company, it may file an offer to acquire the remaining shares of the new company within five years following the reorganisation. If as a result of this offer the shareholder acquired more than 50 per cent of the remaining shares, it is entitled to squeeze out the remaining shareholders by serving a request to sell the remaining shares. Such request shall be served within six months following the end of the term of the initial offer.

The Law on Limited Liability Companies provides the members of the company with another option to put a particular member aside. If the member materially breaches its corporate obligations or if its acts or omissions obstruct the activity of the company, other members that hold at least 10 per cent of the company's capital may initiate court proceedings to expel such member from the company. If the motion to expel is granted, the company shall pay to the expelled member an actual cost of its participating interest based on the financial statements for the last accounting period.

14 Dissenters' rights

Do shareholders have appraisal rights?

Shareholders of the company may request the company to acquire their shares in whole or in part in certain cases specified by law. The holders of ordinary shares may file such request if first the general meeting of shareholders decides in favour of reorganisation of the company or approves a major transaction for the amount exceeding 50 per cent of the balance value of the company's assets or approves any amendments to the charter reducing the rights of such shareholders or decides to convert a public company into a private entity or to delist the shares of the company, and secondly if such shareholder was not present at the meeting or voted against such decision.

The company is required to notify its shareholders when they become entitled to sell their stock to the company and shall indicate the price and procedure to be followed if they decide in its favour. The price of the shares for these purposes shall be established by the board of directors but may not be less than the market value to be determined by an independent appraiser. If the company is listed, the price may not be less than the weighted average price of shares as quoted on the stock exchange for a six-month period prior to the decision of the general meeting that triggered the right to sell the shares. If the shareholder is personally registered in the register of shareholders, the request for buyout shall be filed to the registrar. Otherwise it shall be served with the entity that is recording the rights of the particular shareholder. Such request shall be filed within 45 days following the date of the general meeting of shareholders, it shall identify the shareholder and indicate the number of shares to be acquired by the company. As soon as the shareholder serves the buyout notice, he or she is no longer entitled to dispose of or to encumber such shares.

The maximum amount that may be utilised by the company for the purpose of a buyout shall not exceed 10 per cent of the net assets of the company. If the total amount of requests served by the shareholders exceeds such limit, the company shall only acquire such shares in part pro rata to the number of shares indicated in shareholders' requests.

The buyout regulation in limited liability companies is partially different from joint-stock companies. A member of a limited liability company has similar rights to request the company to acquire his or her participating interest if the member voted against the decision to increase the charter capital or to approve any major transaction or was not present at the meeting.

In addition to such rights, the member of a limited liability company may request the company to acquire its participating interest if the articles of the company restrict any sale of the participating interest to third parties other than the members of the company and if the members refuse to acquire such participating interest or if they did not approve the transfer of the participating interest to any third party. Further, articles of a limited liability company may provide its members with a right to request a buyout without any cause, in which case any member may serve such request at any time.

In all cases described above, the limited liability company shall pay to its member an actual value of its participating interest to be calculated based on the last financial statements.

The responsibilities of the board (supervisory)

15 Board structure

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

The board structure of all joint-stock companies including the listed ones may be described as two-tier. The leading role is played by the board of directors (which is also named a supervisory board) that holds all the management and operational duties. The supervisory functions over financial activity of the company are performed by the internal audit committee that shall be created in a public joint-stock company. Private companies and limited liability companies having more than 15 members are generally subject to similar requirements unless they decide not to create an internal audit commission by introducing such provision in the articles of association. For other limited liability companies, the foundation of the internal audit commission is optional and this matter may be regulated by the articles.

The internal audit committee may request any documents and explanations from the company's officials or employees. It is responsible for review of annual reports and balance sheets before they are submitted to the general meeting for approval. Members of the internal audit committee may not be members of the board or hold other positions in the governement bodies of the company (they may, however, be employed by the company).

16 Board's legal responsibilities

What are the board's primary legal responsibilities?

The board of directors is responsible for general management of the company except for matters being within the exclusive competence of the general meeting (as described in question 4). The Law on Joint Stock Companies provides that the board of directors shall:

- set up the priority activities of the company;
- convene the regular and extraordinary general meetings with few exceptions;
- approve the agenda of the general meeting;
- decide on the date to be used for creating a list of shareholders entitled to participate in the meeting and other matters related to convening and organising the meeting;
- decide on conversion of preference shares into ordinary shares without increase of the share capital;
- issue bonds and other securities (other than ordinary shares);
- appraise assets and decide on the emission price and shares buyout price for various cases provided by law;
- decide on buyout of shares;
- recommend on the remuneration of the auditor and members of the supervisory commission;
- recommend on the amount of dividends and on dividend payment procedure;
- decide on application of assets of the reserve fund and other funds of the company;
- approve internal documents of the company other than documents to be approved by the general meeting of shareholders or executive bodies of the company;
- decide on the foundation of the company's branches and representative offices unless this matter is delegated to executive bodies of the company;
- approve certain major transactions and interested-party transactions;
- approve the registrar of the company; and
- decide on participation and exit from other entities unless this matter is delegated to executive bodies and excluding matters within the competence of the general meeting.

The articles of association may also delegate the following matters to the board:

- increase of the share capital by issuance of additional shares within the total number of authorised shares;

- appointment of the CEO and its dismissal;
- approval of the annual report and financial statements; and
- listing of the company's shares.

The Civil Code gives an option to private companies to amend the competence of the board of directors by introducing other regulation in the articles of association. Such amendments shall be approved by the shareholders unanimously.

The Law on Limited Liability Companies provides more flexibility and allows the members of the company to delegate to the board of directors any or all matters that are not within the exclusive competence of the general meeting or executive bodies of the company. Examples indicated in the law are mostly similar to the competence of the board of directors of a joint-stock company.

17 Board obligees

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

Under Russian law, board members owe their duties to the company and not to individual shareholders and therefore they do not represent any of the shareholders. The non-binding Code of Corporate Governance approved by the Central Bank indicates that the members of the board shall make decisions taking an equal attitude to all shareholders. It is relevant to note that the legal obligations of board members that represent the state are different and such members are required to vote and act in accordance with the directions of the state.

18 Enforcement action against directors

Can an enforcement action against directors be brought by, or on behalf of, those to whom duties are owed?

The liability of board members to the company is based on article 53.1 of the Civil Code, which provides that the board members are liable in the same way as the executive director, who is required to compensate damages caused to the company as a result of his or her fault if so requested by the company or by its shareholders. The Civil Code provides that shareholders are only entitled to submit such claims in the name of the company and not in their personal capacity. In certain cases, damages claims against board members can also be brought by an external governor to be nominated in case of the company's bankruptcy that shall act on the name of the company.

The court practice on indirect claims against the members of the board has changed. Before 2013, court rulings against board members were very uncommon. The trend has changed after the Decree of the Supreme Arbitration Court No. 62 of 30 July 2013 'On certain matters of damages compensation by members of governing bodies of legal entities' was passed, providing official guidance on certain matters of liability of the board members and executives. The Supreme Arbitration Court facilitated the bringing of a claim against board members and executives by providing criteria required to find a director liable, illustrating the switch of the burden of proof from the company to the director and giving examples of breach of duties of care and duties of loyalty. Following the decree, claims for damages against the directors for breach of duties became a more common practice.

19 Care and prudence

Do the board's duties include a care or prudence element?

Care and loyalty are two elements specifically indicated by the Civil Code, the Law on Limited Liability Companies and the Law on Joint Stock Companies as duties of the board members. The Supreme Arbitration Court illustrated these duties by giving examples of breach of such duties in its Decree No. 62 of 30 July 2013. The Decree provides that the duty of care shall be considered broken in the following cases:

- if the board member has taken a decision without considering any information within his or her knowledge that was relevant for such decision; or
- before making a decision he or she failed to undertake such measures to get any relevant information considered by business practice as common in similar circumstances. Any failure to postpone the transaction until getting relevant information shall also be considered as a breach of duty of care if a reasonable board member would have postponed it in similar circumstances.

The duty of loyalty shall be considered broken in the following cases:

- if there is any conflict of interest between the interest of the director or his or her affiliates and the interest of the company unless the information on the conflict of interest was disclosed in due course; or
- if the board member knew or should have known that his or her actions were not in the interest of the company when they were committed.

As a general rule, the company searching for damages as a result of a breach of duty of care or duty of loyalty by the board member shall show the circumstances evidencing the same. After that the director shall be allowed to give explanations and show reasons for his or her actions. If the board member fails to give such explanations, the burden of proof shall switch to the board member and after that he or she is required to prove that his or her duty of care and loyalty were performed in due course.

20 Board member duties

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

The duties of individual members of the board of Russian companies are similar. The matter of individual approach to directors which would take into consideration their individual skills and experience in analysing a potential breach of a duty of care has not been duly researched in Russian doctrine and has not been reviewed by Russian courts to give grounds for any conclusions or trends.

21 Delegation of board responsibilities

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

The Law on Joint Stock Companies and the Law on Limited Liability Companies both provide that the members of the board of directors may not delegate their votes to any third persons including any other members of the board. Therefore, the decision-making responsibilities may not be delegated and the board members shall perform them personally.

Any committees of the board of directors that may be organised by the board do not perform the functions of the board itself but rather assist the board in making decisions. Any decisions of the committees are advisory in their nature. Following the decision of the committee, the board of directors is still required to make its own decision, which may derogate from the decision of the committee.

22 Non-executive and independent directors

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

The law does not require the companies to have any number of independent directors and does not provide for a definition of the independent director. Moscow Exchange listing requirements indicate that the total number of independent directors shall be not less than three, and they shall constitute at least one-fifth of the total number of the board members. The listing rules identify the independent director as a person that is independent enough to have his or her own position and is able to make considered and impartial judgements that are not influenced by executive bodies of the issuer, any groups of shareholders or dependent entities and has enough experience, competence and skills. A member of the board may not be considered independent if he or she is connected with the company or its shareholder or major counterparty or the state or municipal body. The non-binding Code of Corporate Governance approved by the Central Bank recommends public companies to ensure that independent directors constitute at least one-third of the total number of board members.

23 Board size and composition

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

The size of the board shall be indicated in a company's articles of association or shall be approved by the general meeting of shareholders. As a general rule, it may not be less than five directors. If the number of ordinary shareholders exceeds 1,000, the number of directors shall be not less than seven. If it exceeds 10,000, there shall be at least nine members of the board. Private companies may have a smaller board if it is set forth in the articles of the company. The maximum number of directors is not limited.

Any shareholder having individually or together with other shareholders at least 2 per cent of the ordinary shares of the company is entitled to propose nominees to the board. The directors are appointed on an annual basis by a general meeting through a cumulative voting procedure, which is described in more detail in question 3.

There are no mandatory criteria to be met by individual directors. The non-binding Code of Corporate Governance generally recommends to appoint as board members those nominees who have an irreproachable personal and business reputation and have skills, experience and competence required to make decisions delegated to the board and to perform its functions.

The Regulation of Russian Central Bank No. 454-P provides for an obligation of public companies whose shares are publicly traded and private companies whose bonds are publicly traded to disclose in their quarterly reports information on the composition of the board of directors that shall include broad information on each member including information on education, position in the management bodies of the company and other companies, participation in the share capital of the company and its subsidiaries, participation in the committees of the board of directors, status as independent director and the amount of remuneration of each director.

24 Board leadership

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

The Law on Joint Stock Companies and the Law on Limited Liability Companies both require that the functions of board chairman and CEO are separated. Further, they provide that the chairman of the board shall be nominated from among its members by the board members by a simple majority vote unless a higher vote is required under the company's articles. The non-binding Code of Corporate Governance indicates that the best practice is to nominate the chairman of the board from among its independent directors.

25 Board committees

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

The law provides for a possibility to create board committees but does not require any committee to be created. The listing rules of the Moscow Exchange indicate that the issuers of shares listed in the first tier shall organise at least three committees of the board of directors:

- the audit committee, led by an independent director, which shall effectuate control over the financial statements of the issuer, over risk management systems and shall procure independence of internal and external audit;
- the remuneration committee, which shall elaborate the remuneration policy for members of the board of directors, management board members and CEO; shall perform preliminary annual evaluation of CEO and management board members; shall elaborate the terms of early termination of duties of CEO and management board members including any payoff; and shall provide recommendations on remuneration of the corporate secretary; and
- the nomination committee, which shall effectuate annual evaluation of the board of directors and members of its committees; shall communicate with the shareholders to give guidance to shareholders with respect to nomination of members of the board of directors; and shall plan staffing and nomination matters to ensure continuity of duties.

Most or all the members of each of the above committees shall be independent. The members of the management board and the CEO may not become members of such committees.

26 Board meetings

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

The law does not provide for any particular number of meetings of the board of directors that shall be arranged within a year. The company is free to include such provisions in its internal regulations.

27 Board practices

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

The Regulation of Russian Central Bank No. 454-P provides that public companies whose shares are publicly traded and private companies whose bonds are publicly traded shall disclose information on material facts as described in question 36. Such information includes information on convocation and meetings of the board, agenda and certain decisions taken by the board. The company is not required to indicate the voting of particular board members and shall only disclose general information on voting results.

28 Remuneration of directors

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

The board members are appointed on an annual basis and their duties last until the next annual general meeting. Within this term, the board members may be remunerated. The matters of directors' remuneration and reimbursement of expenses associated with their services are within the competence of the general meeting of shareholders and may be decided by a simple majority vote. In the absence of such decision, the company has no obligation to pay remuneration to the board members.

The law neither requires nor prohibits any contracts between the company and the board member. If the company chooses to enter into a contract with the board member, such contract may be in the form of a civil law contract or a labour contract (which is not a common practice). Any civil transactions between the director and the company for the amount exceeding 0.1 per cent of the balance sheet asset value of the company (or other limits to be established by the Russian Central Bank) including loan agreements are considered as interested-party transactions and shall be approved in accordance with a special procedure (generally it shall be approved by a majority of non-interested board members unless it is equal or exceeds 10 per cent of the balance value of assets of the company, in which case it will be subject to general meeting approval). If such arrangement may be considered as a form of remuneration, it shall be approved by the general meeting.

Listing requirements of the Moscow Exchange provide that the remuneration policy with respect to the board members shall be elaborated by the remuneration committee of the board. Any further decision on the amount of remuneration shall be taken by the general meeting of shareholders.

29 Remuneration of senior management

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

The relations between the company and its senior management (CEO, management board members, etc), unlike relations with the board members, are regulated by labour legislation. The amount of remuneration shall be established in their labour contracts or other auxiliary agreements (such as option agreements) and generally it is not limited or regulated by law. In state-owned enterprises, the remuneration of the senior management is subject to special regulation and shall be limited by a special ratio calculated based on the remuneration of other employees.

Listing requirements of the Moscow Exchange provide that the remuneration policy with respect to members of the board of directors, members of the management board and CEO shall be elaborated by the remuneration committee of the board. Any further decisions on this matter are not subject to listing regulation.

30 D&O liability insurance

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

D&O insurance under Russian law has existed for more than 10 years but remains a rare practice due to several factors. Mostly this is caused by partially outdated insurance regulation of the Civil Code. Article 932 of the Civil Code contains a general prohibition on contractual liability insurance unless such insurance is specifically provided by law. The law does not contain any references to directors' liability insurance and therefore any contractual liability of directors may not be insured on the face of it.

D&O insurance is not the only sphere where provisions of article 932 create a critical impediment to both insurance companies and insured persons, and this regulation has been reviewed by the courts in a number of cases. In certain cases (one of the milestone cases was reviewed by the Supreme Arbitration Court following a claim from Ugoria insurance company) courts acknowledged that the limitations of this article may be overruled and there is a certain trend to uphold the insurance contracts when insurers try to invalidate the insurance contracts with a reference to any conflict with article 932. Yet, the risk of invalidation of the insurance contract remains high.

One more impediment to this type of insurance is caused by article 963 of the Civil Code, which exempts the insurance company from any obligation to make payment if the insurance accident was caused as a result of wilful misconduct. When dealing with D&O liability it is common for the courts to rule against the director only if the actions of the director are considered as wilful misconduct, which automatically disables any insurance compensation.

The reluctance of companies to take advantage of the D&O insurance is also caused by another provision of article 932 of the Civil Code, which states that the contractual liability insurance contract may only insure the liability of the party to the contract. Any contract that provides for insurance of third-party liability is void. In these circumstances the companies are unable to enter into D&O insurance agreement covering the liability of directors and do not have an option to pay the premium directly.

All these reasons taken together make D&O insurance a rare practice in Russia.

31 Indemnification of directors and officers

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

The mechanism of indemnity was only introduced in Russian law in mid-2015. It provides that a party (indemnitor) may only undertake to compensate losses of the other party (indemnitee) that were caused by circumstances that were not connected with a violation of the indemnitor's obligation, which is not the case when talking about directors' liability, which is almost always connected with a breach of legal duty by the board member. Further, the law provides that the indemnity mechanism may only be applied in 'business to business' relations, which generally precludes the parties from applying it in directors' engagement. Therefore, as of today Russian law indemnity may not be implemented in corporate law to address the directors' liability issues. Sometimes the parties choose to apply indemnity provisions under English law if any foreign element is present in a particular case (which is required for the application of foreign law provisions).

32 Exculpation of directors and officers

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

Private companies may only discharge and limit directors and officers of liability that was caused by a breach of the duty of care by entering into agreement with the director. Other limitations of liability of directors including those caused by breach of duty of loyalty for private companies or caused by breach of any duty by the director for public companies, including any actions in bad faith, are specifically identified by the Civil Code as void. Other ways to release directors of liability such as shareholders' approvals of directors' actions have been rejected by recent court practice. The Superior Arbitration Court in its official comments provided that the approval of the actions of directors by the shareholders or other governing bodies or any further actions of directors in pursuit of such approval or decision shall not discharge the director from liability. This approach is based on the principle that the duties of care and loyalty of the director are independent from any third parties.

33 Employees

What role do employees play in corporate governance?

Employees have no influence on corporate governance matters and are not represented on any management level of the company.

34 Board and director evaluations

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

Russian law does not have any regulation that would require evaluation of the board, its committees or directors. Any such evaluation is commonly performed due to listing requirements or in order to comply with a non-obligatory Code of Corporate Governance. The Code provides that the board of directors shall carry out an annual evaluation of the board members and committees. The listing rules of the Moscow Exchange indicate that the issuers of shares listed in the first tier shall organise a nomination committee of the board of directors that shall effectuate an annual evaluation of the board of directors and members of its committees.

There is no special disclosure procedure with respect to the evaluation of the board members. Some companies choose to disclose the information on evaluation of directors in their annual reports, but they are not required to mention it or to disclose any evaluation results. Any such disclosure is performed as a way to follow best corporate governance practice.

Disclosure and transparency

35 Corporate charter and by-laws

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

The Regulation of Russian Central Bank No. 454-P provides for an obligation of a public company to disclose its articles of association and internal documents that regulate procedural issues of the governing bodies of the company. As a common practice, such documents are disclosed on company's website. Non-public companies and limited liability companies are not required to do so. To obtain their articles of association, one should file a written application to a local tax authority

Update and trends

One of the key developments in corporate governance matters in 2016 is a reform of the major transactions and interested-party transactions. The new rules became effective as of 1 January 2017.

A major transaction is now defined as a transaction beyond the scope of normal business activity of the company, which involves assets with a transaction price or balance sheet value of at least 25 per cent of the balance sheet assets value on the last accounting date. For these purposes the law introduced a definition of transactions within the normal scope of business. It covers transactions that are normally executed by the company or other companies engaged in similar activities, regardless of whether the company executed such transactions before, provided that it does not result in termination of the company's operations, or a change in the nature of the business, or a change in the scale of the business of the company. The role of the board of directors in the approval of major transactions has increased: if the transaction is required to be approved as a major transaction, the board of directors (or the CEO, if the company has no board) shall issue a report indicating potential consequences of the transaction.

The procedure of contesting a major transaction has changed. Following the reform, it is only available to shareholders (members) holding at least 1 per cent of voting capital, to individual board members and to the company itself. The claimant is now free to contest all transactions and is not limited to transactions where his or her voting could influence the approval. Further, he or she does not need to show that the contested transaction resulted in losses or negative consequences for the claimant. On the other hand, the claimant is now required to prove that the company's counterparty knew or should have known that the transaction was a major transaction for the company and that it was not duly approved.

The regulation on interested-party transactions has also changed. First, the definition of an interested-party transaction now covers transactions with an interest of a member of the governing body of the company or with an interest of the 'controlling person' (a person controlling directly or indirectly over 50 per cent of votes or able to appoint over 50 per cent of the board of directors or another collegial body, or able to appoint the sole executive body of the company). Initially it was linked to an 'affiliation test' which provided for 20 per cent participation.

Second, the law introduced an exemption for transactions 'within the scope of normal business activity'. It is different from the same term used for major transactions and covers similar transactions executed by the company several times within an extended period which did not qualify as an interested-party transaction.

Third, interested-party transactions are now limited to transactions involving assets with a transaction price or balance sheet value equal to or exceeding 0.1 per cent of the balance sheet asset value of the company as of the last reporting date (provided that the transaction price does not exceed other limits to be established by the Russian Central Bank). Further, the approval of transactions between 2 per cent and 10 per cent of the balance sheet asset value of the company has now passed to the board of directors.

Another new option permits the company to ratify an interested-party transaction after its execution unless preliminary approval is required by a general director, a member of a management or supervisory board or a shareholder (member) holding at least 1 per cent of the voting share capital of the company.

Starting from 1 January 2017, all private companies are free to exclude the approval requirement for interested-party transactions, or to amend the approval procedure set out in the law.

Finally, the calculation of the number of votes required for approval of interested-party transactions was amended to take into account only shareholders present at the meeting instead of all shareholders of the company.

whose address may be found in the extract from the state registrar. Such extracts are now issued in electronic form on the official website of the Russian Tax Authority (egrul.nalog.ru). The information is only available in Russian.

36 Company information

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

Disclosure obligations are established by the Law on Joint Stock Companies. The law provides that public companies and private companies having more than 50 shareholders are required to disclose annual reports and annual financial statements. Public companies shall also disclose securities prospectus, notices on convocation of general meetings of shareholders and other information as required by the Russian Central Bank. Such requirements were detailed in the Regulation of the Russian Central Bank No. 454-P dated 30 December 2014. It provides that public companies whose shares are publicly traded and private companies whose bonds are publicly traded shall disclose information on:

- issuance of shares and bonds;
- registration of issue prospectus;
- quarterly reports; and
- information on material facts that may influence the quotations and the price of the shares or bonds when disclosed.

The list of information to be disclosed is very broad and includes among other things the following:

- information that the general meeting of shareholders or a meeting of the board of directors are convened or have taken place and information on all decisions taken by the general meeting and certain decisions taken by the board;
- information on interested-party transactions, major transactions and transactions exceeding 10 per cent of the balance value of company's assets;
- information on the filing of an application on the reorganisation or liquidation of the issuer;
- information on new material subsidiaries being under the control of the issuer;
- information on corporate disputes of the issuer; and
- other information indicated in Regulation No. 454-P.

The disclosure of material facts shall be notified on a news feed within one day and on the website of the company within two days. Official news feeds are www.disclosure.ru, e-disclosure.azipi.ru, www.e-disclosure.ru, disclosure.1prime.ru and disclosure.skrin.ru.

It is relevant to note that the general meeting of the company may agree to file an application to be discharged from disclosure obligations. Such decision may be taken by 95 per cent of all votes of a public company or by three-quarters of the votes present at the general meeting of other companies.

Hot topics

37 Say-on-pay

Do shareholders have an advisory or other vote regarding executive remuneration? How frequently may they vote?

As a general rule, the general meeting of shareholders may only vote on the remuneration of the members of the board of directors and the law does not list remuneration of other executives as a matter within its competence. Public companies may not amend the scope of the general meeting unless specifically provided by law, therefore shareholders of public companies do not have an option to decide on the executive remuneration. Private companies and limited liability companies are free to expand the authority of the general meeting of shareholders (company members) and may amend the articles to refer these matters to shareholders. Further, the shareholders (members) of private companies and limited liability companies will be entitled to vote on the remuneration of the CEO and on other terms of the contract with the CEO if there is no board of directors in the company (which is a standard scenario for limited liability companies and an option for joint-stock companies having fewer than 50 shareholders).

38 Shareholder-nominated directors

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

Any shareholder having individually or together with other shareholders at least 2 per cent of the ordinary shares of a company is entitled to propose nominees to be included in voting and appointment procedure on a regular general meeting of shareholders. The appointment is performed through a cumulative voting procedure as described in question 3. There are no alternative procedures for shareholders to nominate members of the board of directors.

39 Shareholder engagement

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

Most of the listed public companies engage with investors and shareholders on an ongoing basis. The communication channels may differ and in most cases such interaction is limited to the disclosure of significant facts as described in question 36. In some cases, the companies hold investor conferences and meetings with individual shareholders. In most cases, such conferences are organised before the annual general meeting or in connection with the quarterly or annual financial statements.

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Sources of corporate governance rules and practices

1 Primary sources of law, regulation and practice

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

Rules on corporate governance for all types of legal entities that may be established in Serbia are primarily provided in the Company Law.

Certain corporate governance rules, as well as those that may ultimately have an impact on corporate governance within joint-stock companies, are further provided in the Capital Markets Law and its by-laws. Rules applying to joint-stock companies whose shares are traded on the stock exchange market or a multilateral trading facility (public companies) are additionally contained in the Takeover Law, regulations of the Securities Exchange Commission (SEC) and the Central Securities Depository and Clearing House (CRS), as well as in the Rules and Procedures of the Belgrade Stock Exchange (Belex). Public joint-stock companies whose shares are traded on the stock exchange are obliged to comply with the applicable listing rules. Companies for management of investment funds are subject to regulation under the Law on Investment Funds.

Corporate governance practice in Serbia for joint-stock companies, especially public companies, is also established and developed by the SEC, which supervises, monitors and consequently influences the corporate governance practice of these entities.

Rules on corporate governance in financial institutions are primarily contained in the Banking Law (ie, for banks) and the Insurance Law (ie, for insurance companies), with subordinate application of the Company Law. Rules on corporate governance in public enterprises (ie, companies performing activities of general interest, which are established by Serbia, its autonomous province or local-self governments) are contained in the Law on Public Enterprises.

2 Responsible entities

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

Laws in Serbia, including those governing corporate governance, are enacted by Parliament. Certain legislative acts, which provide further regulation on implementation of the laws, are enacted by the government (ie, ministries).

Corporate governance and operation of public companies are under the supervision of the SEC, CRS and Belex, which are in charge of enacting sub-regulations that regulate such companies' operations, including their reporting obligations, notification and publication requirements.

There are no shareholder activist groups or proxy advisory firms that set precedents in interpretation or regulation of corporate governance rules. However, some guidelines on corporate governance in joint-stock companies are provided by the Serbian Chamber of Commerce through draft codes on corporate governance which may be enacted within such companies.

Even though court practice is not a statutory or formal source of law, with its precedents it greatly affects the overall application and enforcement of laws, including those related to corporate governance.

The rights and equitable treatment of shareholders

3 Shareholder powers

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

Directors may be appointed either by the shareholders' assembly or the supervisory board, depending on the type of corporate governance established within a company. The Company Law in Serbia recognises two types of corporate governance system: a one-tier corporate governance system, in which management authorities are vested in one or more directors (ie, a board) and two-tier corporate governance system in which management authorities are vested in the supervisory board and one or more directors (ie, a board), which, in joint-stock companies, must be executive directors.

In general, in joint-stock companies operating under a one-tier corporate governance system, directors are appointed and removed by the shareholders' assembly, by a simple majority of votes of shareholders who are entitled to vote, unless a greater majority is provided in the companies' articles of association. In public companies, directors are appointed by cumulative vote, if so provided in their articles of association.

In joint-stock companies operating under a two-tier corporate governance system, directors are appointed and removed by the supervisory board by a simple majority of votes of the present supervisory board members, unless a greater majority is provided in the companies' articles of association or the applicable rules of procedure, if any.

A similar corporate governance system in terms of appointment and removal of directors exists in limited liability companies.

In joint-stock companies operating under a one-tier corporate governance system, directors may elect, from among the executive directors, the general manager. In joint-stock companies operating under a two-tier corporate governance system, such appointment is within the authority of the supervisory board. The general manager is in charge of representing the company.

Shareholders may not require the board to pursue a particular course of action. However, owing to the shareholders' assembly's authority to supervise and remove directors and members of the supervisory board, such authority may sometimes be influential on the management's operations.

4 Shareholder decisions

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

Pursuant to the Company Law, the following decisions are reserved to the shareholders (ie, the shareholders' assembly) in joint-stock companies:

- amendments to the company's articles of association;

- increase or reduction in share capital, and each issuance of securities;
- decision on the number of authorised shares;
- changes in the rights or privileges pertaining to any class of shares;
- restructurings and changes in legal form;
- acquisition and disposal of property with great value;
- profit distribution and coverage of losses;
- adoption of financial statements and auditor's reports, provided that financial statements are subject to auditing;
- adoption of reports by the board of directors or the supervisory board, if the company has a two-tier corporate governance system;
- decision on remuneration paid to directors or members of the supervisory board, if the company has a two-tier corporate governance system, or the decision on the rules for determining such remuneration, including the remuneration paid in shares and other securities of the company;
- appointment and recall of directors;
- appointment and recall of members of the supervisory board, if the company has a two-tier corporate governance system;
- instigation of liquidation proceedings, or filing for insolvency;
- selecting auditors and remuneration for their work;
- other issues that are included in the agenda of the shareholders' assembly in accordance with the Company Law; and
- other issues in accordance with the Company Law and the company's articles of association (eg, certain competences of the board of directors and supervisory board may be delegated to the shareholders' assembly by the articles of association).

The shareholders' assembly generally decides by a simple majority of votes of present shareholders with voting rights on a specific issue, unless a greater majority is provided in the articles of association or the Company Law (eg, a three-quarters majority of votes of present shareholders with voting rights is required for decisions on disposal of property with great value or for decisions on exclusion of pre-emption rights).

The Company Law does not provide for non-binding shareholder votes.

5 Disproportionate voting rights

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

Pursuant to the Company Law, each common share provides one vote. However, there are circumstances in which shareholders may be deprived of their voting rights, or their voting rights may be limited; for example, a shareholder and its related persons are deprived from voting on: their release of liabilities towards the company or reduction of such liabilities; instigation or cancellation of proceedings against such shareholder; or approval of transactions in which such shareholder has personal interest. Moreover, shareholders may be deprived from voting rights as a consequence of an imposed sanction; for example, shares acquired in banks without the necessary regulatory approvals, or shares acquired in the course of a takeover contrary to the mandatory takeover rules, do not provide any voting rights.

Articles of association may subject personal participation of a shareholder at the shareholders' assembly meeting to a minimum number of shares that must be owned by each shareholder (ie, the 'census', which cannot be higher than 0.1 per cent of the total number shares), which requirement may indirectly limit the ability of some minority shareholders to vote.

Contrary to common shares, preferred shares and treasury shares generally do not provide any voting rights.

As an exception to the above rule, holders of preferred shares have one vote per share at the shareholders' assembly, deciding on: an increase or decrease in the number of the classes of preferred shares; alteration of preferential rights; a stock split, a reverse stock split and stock swaps; and new issuance of preferred shares. Voting rights under preferred shares may also be provided under a joint-stock company's articles of association; for example, it may be provided that shareholders with preferred shares that may be converted into common shares are entitled to vote together with shareholders with common shares on all or on specific issues, provided that the number of votes under such preferred shares is equal to the number of votes under the common shares into which they can be converted. Moreover, it may be provided that shareholders with preferred shares have a right to vote together with holders of common shares if they have not received dividends to which they are entitled under the shareholders' assembly decision, until such dividends are paid and in proportion to the participation of such preferred shares in the company's share capital.

6 Shareholders' meetings and voting

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

Each shareholder with a common share is entitled, but is not obligated, to participate and vote at the shareholders' assembly meeting. Such rights are exceptionally provided to holders of preferred shares. The right to participate at the meeting, as explained in question 5, may be subject to a census provided under the articles of association. The record date is relevant for determination of shareholders with voting rights.

Even though the Company Law does not specifically refer to 'virtual' (ie, online shareholders' assembly meetings), it provides that a shareholders' meeting may be held by use of conference or other audiovisual equipment, which enables all participants to communicate with each other. Shareholders may vote via electronic devices if so provided under the applicable articles of association. Moreover, they may vote in writing, without attending the shareholders' assembly meeting, via notarised ballots, unless such notarisation requirement is waived under the company's articles of association. Finally, shareholders may vote via proxies. A company may stipulate terms and conditions that proxies must meet or may limit their overall number.

In addition, extraordinary shareholders' meetings in non-public joint-stock companies may be held even without convocation, if attended by all shareholders with voting rights on all items of the agenda and if not opposed by any of shareholders, unless otherwise provided in the articles of association or the applicable rules of procedure.

Agreements through which shareholders undertake to vote in line with instructions of the company, directors, or the supervisory board members, as well as voting agreements through which shareholders undertake to vote in a specific manner or to refrain from voting in exchange for benefits to be provided to them by the company, directors or supervisory board members, are void.

7 Shareholders and the board

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

Shareholders are entitled to request convocation of both regular and extraordinary shareholders' assembly meetings under the conditions prescribed below.

If the regular shareholders' assembly meeting does not take place within the statutory deadlines, each shareholder who is entitled to participate at the meeting, a director (in one-tier corporate governance system) or a member of the supervisory board (in two-tier corporate governance system) may, within three months from the expiry of the term for convocation of the shareholders' assembly meeting, request a court to order that such meeting takes place.

Shareholders holding at least 5 per cent of the company's capital or voting shares on a specific topic (or a lesser amount of capital or shares if so provided in the company's articles of association) may request convocation of an extraordinary shareholders' assembly meeting, provided that they acquired a shareholding status at least three months before the date of the request and continued to be shareholders until their request was decided upon. If the board of directors (in a one-tier corporate governance system) or the supervisory board (in a two-tier corporate governance system) fails to decide on the request of shareholders for convocation of the extraordinary shareholders' assembly meeting within eight days from the date of receipt of such request, or if within the same deadline it rejects such request and fails to notify shareholders thereof, as well as if the extraordinary shareholders' assembly meeting does not take place within 30 days from the date of the receipt of the request, each shareholder applicant may request a court to order that such meeting takes place within a further 30 days.

Shareholders holding or representing at least 5 per cent of the voting shares may propose to the board of directors (in a one-tier corporate governance system) or the supervisory board (in a two-tier corporate governance system) inclusion of additional topics for discussion or decision-making to the agenda for the shareholders' assembly meeting. Such written request, containing (when necessary) draft decisions to be adopted by the shareholders' meeting, shall be filed with the company 20 days before the date of the regular shareholders' meeting and 10 days before the date of the extraordinary shareholders' meeting. If the board of directors (in the one-tier corporate governance system) or the supervisory board (in the two-tier corporate governance system) fail to approve the filed request by the minority shareholders within three days from its receipt, the minority shareholders may request from the court, within further three days, to order the company to include such additional topics to the shareholders' meeting agenda.

Moreover, each shareholder who is entitled to participate at the shareholders' assembly meeting is entitled to raise questions with directors or members of the supervisory board in relation to the agenda, as well as other questions concerning the company, provided that the answers to such questions are necessary for the right evaluation of questions in relation to the agenda topics. Questions may also involve related companies when consolidated financial statements are discussed within the mother-company. If a decision was made at the shareholders' meeting on a topic in relation to which a question was posed, but not answered, the shareholders who posed such unanswered question may, within eight days of the shareholders' meeting, request a court to order the company to provide the shareholder with the answer to the question posed within eight days. This right pertains to each shareholder who objected to the fact that the posed question was not answered and such objection was recorded in the minutes of the meeting.

Director nominations may be made by any director or the board of directors, the appointment committee (if any) and shareholders who are entitled to propose the agenda for the shareholders' assembly meeting.

Within three days of the expiry of the statutory eight-day deadline for producing the minutes, the chairman of the shareholders' assembly or the secretary of the company is obligated to deliver the signed minutes from the shareholders' assembly meeting to all shareholders or to publish the minutes on the company's web page or the commercial registry's web page and keep the publication active for 30 days.

8 Controlling shareholders' duties

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

Controlling shareholders, as well as those with a significant shareholding in a company (ie, shareholders who solely or by acting in concert hold more that 25 per cent of votes in a company) owe the following fiduciary duties to the company:
- duty of care;
- duty of reporting related-party transactions;
- duty of loyalty (duty to prevent conflicts of interest);
- duty of confidentiality; and
- duty arising out of competition prohibition.

In case of breach of the above fiduciary duties by the controlling shareholder or other persons with such duties (supervisory board members, directors, liquidation administrators, etc), the company may file a claim for damages, and, depending on the specific duty that has been breached, may also file a claim for:
- annulment of the transaction arising out of the breach of fiduciary duties (eg, in case of breach of the duty of reporting related-party transactions);
- transfer of benefits acquired by the party in breach to the company (eg, in case of breach of duty of loyalty and breach of duties arising out of prohibition of competition);
- termination of the shareholding status; and
- termination of employment, if applicable (eg, in case of breach of duty of confidentiality and breach of duties arising out of prohibition of competition).

In addition, each shareholder is entitled to file a claim for damages in his, her or its name against the controlling shareholder, as well as other persons with fiduciary duties towards the company, in the event of a breach by such persons.

Moreover, as a result of a breach of the above fiduciary duties, shareholders are entitled to file a derivative suit against the controlling shareholder or other persons with such duties. The claim is filed in the name of the claimants but for the account of the company, provided that the claimants represent at least 5 per cent of the company's registered capital; and have previously requested instigation of the lawsuit by the company, which request was rejected or was not pursued within 30 days of its filing.

9 Shareholder responsibility

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

Shareholders are generally not liable for the company's obligations. However, such liability may be established and the corporate veil may be lifted in cases that could qualify as misuse of the limited liability principle by shareholders, which include:
- use of the company for prohibited goals;
- use or disposal of the company's assets as if they were the shareholders' personal property;
- use of the company or its assets for the purpose of damaging creditors; or
- deterioration of the company's property for the purpose of acquiring personal profit or profit for third parties, despite the knowledge that the company shall consequently not be able to fulfil its obligations.

In the above cases, creditors of the company are entitled to file claims against the responsible shareholders within six months from the moment of learning about the abuse, but no later than five years from the date of the abuse by the shareholder.

Additionally, shareholders of a liquidated company are jointly and severally liable for such company's obligations up to the amount of the liquidation surplus they received.

Corporate control

10 Anti-takeover devices

Are anti-takeover devices permitted?

Pursuant to the Takeover Law, from the moment of publication of the Notification of Takeover Intent until the completion of the takeover bid process, the board of directors, supervisory board and bank's executive and management board respectively, of the target public company may not:
- increase the target company's share capital;
- undertake extraordinary actions or enter into agreements that would alter significantly the status of the target company's property or liabilities (ie, may only exercise its regular activities that are related to the target company's operations);
- decide on acquisition or sale of treasury shares; or
- publish a takeover bid for another company.

However, the company's management may execute the above actions with the consent of the shareholders' assembly, which decides on these matters by a simple majority of votes.

Within the same period of time, the target public company must not amend its articles of incorporation so as to limit the number of votes carried by its voting shares, but may cancel the existing limitations, if any, by a simple majority of shareholders' votes.

For the duration of a takeover process, the board of directors, supervisory board and bank's executive and management board respectively, of the public target company is entitled to seek a counter takeover bid.

The board of directors, supervisory board and bank's executive and management board respectively of a public target company is obligated, within 10 days following the bid's publication, to publish its opinion with respect to the takeover bid, and state the factors that support such opinion, in the same manner in which the takeover bid was published. Aside from said opinion, the board of the target public company is not entitled to pass any decision within the scope of its competency that would unlawfully prevent or impede takeover or would have detrimental effect to the company's operations for a longer period of time. Employees are also entitled, under certain circumstances, to provide their opinion on the takeover.

The Company Law additionally provides certain anti-squeeze-out rules. Namely, the squeeze-out procedure may be initiated by a shareholder who holds at least 90 per cent of the share capital in a joint-stock company and votes arising out of all common shares, unless the squeeze-out is prohibited under the company's articles of association or a greater majority is required for the squeeze-out thereunder.

11 Issuance of new shares

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

While a decision on share issuance is generally passed by the shareholders' assembly, the Company Law provides a possibility for the board of directors or the supervisory board (depending on the corporate governance system applicable in the company) to decide on the share issuance when the same relates to the authorised shares, the issuance of which was envisaged in the company's articles of association (noting that the overall number of authorised shares must be less than half of the issued common shares).

Each shareholder in a joint-stock company generally has a pre-emption right with respect to acquisition of shares of new share issuance in proportion to his, her or its fully paid-in shareholding. This right may be limited or excluded in case of private share issuance (ie, without prospectus) on the basis of the shareholders' assembly decision or a board's or supervisory board's decision, in case of issuance of authorised shares, passed by a three-quarters majority of votes of present shareholders.

In addition, articles of association may provide for a pre-emption right with respect to issuance of shares of a different type and class (as compared to those held by shareholders exercising such right), provided that other shareholders eligible to acquire such newly issued shares have already exercised their pre-emption rights.

12 Restrictions on the transfer of fully paid shares

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

In general, shares are freely transferable, unless the company's articles of association restrict their transfer by pre-emption right of other shareholders or by prior approval of the company. However, transfer of shares and rights arising out of the shares issued by public companies may not be restricted.

While transfer of shares issued by non-public joint-stock companies is executed via notarised agreements, transfer of shares issued by public companies is executed in accordance with the Capital Markets Law.

The rights attached to a share, except for the voting right, are freely transferable, unless such transfer is restricted or excluded through the underlying articles of association or a decision on share issuance.

13 Compulsory repurchase rules

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

Pursuant to the Company Law, the shareholders' assembly may provide, in its decision on issuance of preferred shares, the company's right or obligation to redeem such shares under terms and conditions provided in the underlying decision on share issuance, provided that such issuance and terms and conditions for a subsequent redemption of shares are provided in the company's articles of association.

A joint-stock company may redeem such preferred shares provided that: such shares are fully paid-in; payment of the purchase price for such shares is made from the reserves established specifically for that purpose; and the net assets of the company are not less than the paid-in capital, increased by the reserves that are to be maintained by the company under the law and the applicable articles of association, if such reserves exist, excluding reserves designated for acquisition of treasury shares.

14 Dissenters' rights

Do shareholders have appraisal rights?

Every shareholder may request the company buy out his, her or its shares, if the shareholder votes against or refrains from voting on:

- amendments to the articles of association of the company that affect (ie, reduce) his, her or its rights;
- restructuring, change of the company's organisational form, change of the term for which the company was established, or a business transaction having a significant value;
- any other decision that changes the shareholders' rights, provided that the company's articles of association provide that shareholders have a right to dissent to such decisions and to request payment of the market value for their shares; or
- withdrawal of one or more shares from the regulated market or a multilateral trading facility.

The above rights also pertain to shareholders who were not present at the shareholders' meeting at which one of the above decisions was passed.

If one of the above-listed decisions is proposed for adoption at the shareholders' meeting, the documentation related to such meeting must include information on the right of dissenting shareholders to request a buyout, as well as a form of the buyout request, together with information on the book-value, the market value and the valuation of shares as of the date of the decision on the shareholders' meeting convocation. A dissenting shareholder who intends to request the buyout of shares must serve a buyout request on the company at the shareholders' meeting at which one of the above-listed decisions is passed or within 15 days of the date of such meeting. The company is obligated to perform the buyout of shares within 60 days from the expiry of the above-mentioned 15-day term under the highest of the possible prices (ie, the book value, the market value or the valuation of the shares as of the date of the shareholders' meeting convocation).

A shareholder dissenting restructuring may request buyout of his or her shares by the company where the purchase price will be the price determined in the decision on restructuring. If a shareholder deems that the share price determined in the decision on restructuring does not correspond to the market value, or if the company does not pay him or her the price, the shareholder may file a claim with a court, within 30 days from the date of payment or from the expiry of the term for payment if the latter was not performed, requesting thereby:

- payment of the remainder of the full value of shares determined in line with the criteria set out in the Company Law (the highest of the book value, the market value or the value determined through the valuation of shares as of the date of the shareholders' meeting convocation) if he, she or it deems that the company paid him, her or it less than the full value of shares because the value was determined incorrectly or because the company made a partial payment;
- payment of the full value of shares determined in line with the above-mentioned statutory criteria, if the company failed to make any payment to the shareholder, despite the filed request for the buyout.

Shares bought out by the company as a consequence of exercise of dissenting shareholders' rights related to restructuring become treasury shares.

The final and enforceable judgment through which a company is obligated to make a payment to a dissenting shareholder has the erga omnes effect towards all dissenting shareholders, including those who did not file the claim to this end. A failure of a company to make payment to all dissenting shareholders triggers the right of the latter to file a claim with a court requesting such payment.

The responsibilities of the board (supervisory)

15 Board structure

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

Public companies in practice tend to opt for the two-tier corporate governance structure.

16 Board's legal responsibilities

What are the board's primary legal responsibilities?

Primary responsibilities of the board are:
- determination of the company's business strategy and business goals;
- internal control of the company's affairs;
- creating accounting and risk management policies;
- activities related to financial statements and their filing with the shareholders' assembly;
- convocation of the shareholders' meeting and determination of draft agenda;
- granting and revoking of proxy (*prokura*);
- deciding on distribution of interim dividends if so provided under articles of association or a shareholder decision;
- issuance of authorised shares, if applicable, and deciding on acquisition of treasury shares in line with the law;
- determination of price for issuance of shares and other securities, and market value of shares; and
- proposing policy for remuneration of director and executive directors, as applicable, unless such policy is provided in the articles of association, and proposing engagement of and employment contracts for directors and executive directors, as applicable, etc.

17 Board obligees

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

Directors are appointed by the shareholders' assembly or the supervisory board. All executive directors are generally representatives of the company, unless such representation powers are vested in a limited number of executive directors through the articles of association.

Directors and supervisory board members are fiduciaries of the company, with specific duties towards the company: duty of care; duty of reporting related-party transactions; duty of loyalty (duty to prevent conflicts of interest); duty of confidentiality; and duties arising out of competition prohibition (see question 8).

18 Enforcement action against directors

Can an enforcement action against directors be brought by, or on behalf of, those to whom duties are owed?

Yes, an enforcement action may be filed against a director or supervisory board member because of breach of his or her fiduciary duties, under the terms and conditions applicable to the action for breach of fiduciary duties against a controlling shareholder (see question 8).

19 Care and prudence

Do the board's duties include a care or prudence element?

Yes. Directors and supervisory board members are bound by duty of care and prudence (see question 8).

20 Board member duties

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

Pursuant to the Company Law, executive directors generally manage operations of the company and act as the company's legal representatives, while non-executive directors supervise the work of executive directors, propose a business strategy for the company and supervise its implementation, and provide consent for business transactions involving personal interests of executive directors.

Skills and overall experience, however, may play a role in practice (or may even be provided as a requirement under the articles of association) in the process of selection of candidates for directors of a joint-stock company. In terms of members of the auditing committee, the Company Law specifically requires that at least one member must be a certified auditor or a professional with experience in the financial or accounting sector.

21 Delegation of board responsibilities

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

The competence of the board of directors and supervisory board may not be delegated to executive directors of the company, but may be delegated to the shareholders' meeting of the company, unless otherwise provided in the company's articles of association.

22 Non-executive and independent directors

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

Under the Company Law, requirements related to 'non-executive' or 'independent' directors apply only to public companies.

In public companies operating under a one-tier corporate governance system, the overall number of non-executive directors must be greater than the number of executive directors and at least one non-executive director must also qualify as independent. In public companies operating under a two-tier corporate governance system, a member of the supervisory board can neither be an executive director nor a *prokura* holder. At least one member of the supervisory board must be an independent director.

In general, executive directors manage the company's operations and act as its legal representatives, unless such authorities are vested to a specific executive director through the articles of association or limited thereunder. In joint-stock companies operating under a two-tier corporate governance system, certain actions by the executive directors require prior approval by the supervisory board. Directors in a one tier-corporate governance system may appoint one of the executive directors as a general manager. Such appointment in joint-stock companies operating under two-tier corporate governance systems is made by the supervisory board. Specific authorities are provided for the board of directors and the executive board.

Non-executive members generally supervise the work of executive directors, propose a business strategy for the company and supervise its implementation and approve business transactions involving personal interest of the executive directors.

For eligibility criteria applicable to executive and non-executive directors, see question 23.

23 Board size and composition

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

Individual directors, board and supervisory board members must have 'business capacity'. An eligible candidate for a director (board or supervisory board member) cannot be:
- a director or a member of the supervisory board in more than five companies;
- a person who has been convicted of a commercial crime during the period of five years as of the date the underlying judgment became final (excluding any sentence time); or
- a person bound by a prohibition of performance of the company's prevailing business activity, for the time of such prohibition.

Additional requirements may be imposed on candidates for directors and board and supervisory board members through the company's articles of association.

Non-executive directors and members of the supervisory board cannot be employees of the company. Moreover, members of the supervisory board cannot act as executive directors or *prokura* holders of the same company.

In public companies, at least one executive director and at least one supervisory board member must act as the independent director (ie, independent from the company).

In order to qualify as an independent director, a person must not be related to other directors and must not have been, in the previous two years:

- an executive director or an employee in the company or a related entity;
- an owner of more than 20 per cent of the share capital in a company, such company's employee or a person hired by such company in another manner if such company generated more than 20 per cent of its annual revenues from the company in which the candidate is to become a director;
- the recipient from or the claimant against the company or its related parties of payments exceeding 20 per cent of the company's annual revenues in that period;
- an owner of more than 20 per cent of the share capital of the company's related party; or
- engaged in auditing of the company's financial statements.

If an independent board member becomes ineligible for performance of his or her tasks based on the above criteria, he or she will continue operating as an executive director, provided that he or she meets the relevant requirements; otherwise his or her appointment shall terminate. If a position of an independent director becomes vacant in a public company for the above reasons, the remaining directors must appoint a new director by co-optation or, where they fail to do so, must convene an extraordinary meeting for that purpose within 30 days from the date they found out the reason for termination of the previous independent director's mandate. The new independent director in the public company must be appointed within 60 days from the date when the remaining directors found out the reasons for termination of appointment of the previous independent director.

Directors, as well as board and supervisory board members must be registered with the Serbian Business Registers Agency, and information on them is publicly available on the register's web page. Specific disclosure requirements are provided for directors of financial institutions.

The minimum number of seats on any board within a joint-stock company is three. The exact number of board members and their mandate is determined in the articles of association. The number of supervisory board members must, additionally, be odd.

While non-public joint-stock companies operating under a one-tier corporate governance system are not required to have a board of directors (but may, instead, have less than three directors), public companies operating under the same corporate governance system are required to have a board of directors.

In non-public joint-stock companies operating under a two-tier corporate governance system, three or more directors form the executive board – a body that is required in public companies.

In a one-tier corporate governance system, directors are appointed by the shareholders' assembly upon nomination by a director or the board of directors, the appointment committee or shareholders with the right to propose the agenda for the shareholders' meeting. In public companies operating under a one-tier corporate governance system, candidates may only be nominated by the appointment committee or by shareholders with the right to propose the agenda for the shareholders' assembly. If so provided in the articles of association, directors in public companies are appointed by cumulative vote. The maximum mandate of each director is four years, with the right to reappointment. The law also provides for a right of co-optation among directors for the purpose of filling vacancies on the board.

In a two-tier corporate governance system, executive directors are appointed by the supervisory board, upon nomination by the appointment committee or any supervisory board member, if no appointment committee has been established. Members of the supervisory board are appointed by the shareholders' assembly upon nomination by the supervisory board, the appointment committee or shareholders with the right to propose the agenda for the shareholders' meeting. The law also provides for a right of co-optation among members of the supervisory board for the purpose of filling vacancies on the board.

24 Board leadership

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

There is no mandatory requirement to separate functions of the board chairman and CEO.

In practice, the chairman of the board of directors often acts as the CEO of the company.

25 Board committees

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

The board in a joint-stock company (ie, the board of directors or the supervisory board, depending on the applicable corporate governance system) may establish committees to assist the board in its work (eg, in preparation of draft decisions; supervision of implementation of certain decisions; and performance of specific expert duties).

The committees must have at least three members and may include directors and other natural persons having adequate knowledge and work experience. The committees cannot decide on matters falling within the scope of competence of the board.

The board of a public company must establish an audit committee and may establish appointment, remuneration and other committees, in line with its articles of association.

At least one member in each committee in a public company must be an independent director. The majority of members must be non-executive directors. An audit committee within a public company must have at least one member who is a qualified auditor, or has relevant knowledge and work experience in the financial and accounting industry, and who is independent from the company; and a chairman who is an independent director. An employee, or person otherwise engaged within a legal entity responsible for audit of the company's financial statements may not be a member of the audit committee.

26 Board meetings

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

The minimum number of board and supervisory board meetings in public companies is four meetings a year. If a chairman of a board does not convene a board meeting upon a written request by any director, so that such meeting takes place within 30 days of the date of such request, the meeting may be convened by the director, subject to providing reasons for convocation of the meeting and draft agenda.

27 Board practices

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

The board of directors, in joint-stock companies operating under a one-tier corporate governance system, and the supervisory board, in joint-stock companies operating under a two-tier corporate governance system, are obligated to submit to the shareholders' assembly, at the annual meeting, reports on: the applicable accounting and financial reporting practices, if any; compliance of the company's operations with the law and other regulations; qualifications and independence of auditors, provided that financial reports are audited; and agreements involving personal interests of directors.

Moreover, each public company is generally obligated to publish and register its annual operating report, a part of which is a statement on application of a specific corporate governance code, with details on corporate governance practice within the company.

Public companies, being under scrutiny of the SEC and Belex, are obligated to publish information about their corporate governance practices, including but not limited to reports on the shareholders' meetings, decisions passed, etc.

Specific disclosure regimes apply to financial institutions; for example, banks are obligated to publish on information on their management of executive board members, including but not limited to the names of the members and their position.

28 Remuneration of directors

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

Directors are entitled to remuneration for their work. In addition, a director may receive an incentive consisting of stocks or warrants of the company or of an affiliated company. The remuneration and incentives are determined by the articles of association, a decision of the shareholders' assembly or by a decision of the supervisory board (in a two-tier corporate governance system), and those may vary depending on the business results of the company. Remuneration in the form of profit participation is, however, expressly prohibited by the Company Law. Remuneration is always provided in the employment agreement concluded with the director, but could also be provided in the management agreement concluded with a director if he or she is not an employee of the company.

The directors' remunerations and incentives in a public company must be disclosed separately in the company's annual financial statements and, to the extent that incentives are provided in shares, the statements must contain a note on the type, class, number and nominal value of the shares (or accounting value if the shares do not have nominal value) that the director acquired, or was entitled to acquire, on that basis.

The directors are appointed by the shareholders' assembly in a one-tier structure or by the supervisory board in a two-tier structure, for a term defined in the articles of association, but in any case for a maximum period of four years. Re-election is possible without constraints. The shareholders' assembly or supervisory board (in a two-tier corporate governance system) may remove directors before expiry of the term of their appointment, without stating the reasoning thereof.

The director is obliged to notify the board on the existence of a personal interest (or an interest of a director's related party) in any transaction entered into or any action taken by the company. Where a company has a sole director, the said notification must be made to the shareholders' assembly (or the supervisory board in a two-tier corporate governance system). It must be deemed that personal interest exists when a director enters into any transaction with a company.

The transactions involving personal interest of a director must be approved by a simple majority of votes (if a different majority is not provided in the articles of association or articles of incorporation) of all directors having no personal interests or by the supervisory board (in a two-tier corporate governance system), and if the supervisory board member has a personal interest, by a simple majority of votes of all supervisory board members that have no personal interest. If there is no voting quorum, or a decision cannot be reached because of a tied vote of board members, the transaction concerned shall be approved by the shareholders' assembly by a simple majority of votes of present shareholders having no personal interest in said transaction. However, it may be provided by the articles of association or articles of incorporation that it is within the competency of shareholders' assembly to approve transactions involving personal interest of directors.

Update and trends

There have been no significant changes to Serbian corporate governance legislation since 2011. The Serbian Ministry of Economy has announced amendments to the Insolvency Law, the draft of which was published in October 2016. However, no information has been made publicly available as to when the announced amendments to the Insolvency Law will be adopted.

29 Remuneration of senior management

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

There are no particular provisions regulating remuneration of senior management. The above rules on remuneration of directors also apply to senior management (whereby a management agreement can be concluded only with a director and not with senior management) (see question 28).

30 D&O liability insurance

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

D&O liability insurance is offered by insurance companies as part of general liability insurance. However, D&O liability insurance is still not a common practice in Serbia.

31 Indemnification of directors and officers

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

In general, pursuant to the Law on Obligations, a company is liable to third parties for damages caused by its employees or corporate bodies in performance of their duties, but is entitled to reimbursement of the paid amounts from the parties in default if they caused damages intentionally or by gross negligence.

However, third parties may claim damages directly from employees, if such damages were caused intentionally.

Even though this question is not specifically regulated under the Company Law, or other applicable regulations, it may be argued that the company should indemnify a director who acted in obedience of his or her duties, in the best interest of the company (see questions 8 and 17) or if he or she acted on the basis of a shareholders' assembly decision (see question 32), provided that such actions do not qualify as criminal acts.

32 Exculpation of directors and officers

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

A director is liable to the company for damages caused thereto by violation of the Company Law, articles of association or decisions of the shareholders' assembly. A director is, however, not liable for damages arising out of his or her actions based on a shareholders' assembly decision. If damages arise out of a decision of the board of directors, all such board members who voted for the decision or refrained from voting are liable for damages. The same applies to directors who were not present at the board's meeting, but failed to notify the board in writing on their disagreement with such decision within specific deadlines.

The above liability for damages becomes time-barred upon expiry of three years from the date of damages.

In general, the company may not waive its request for damages, except if such waiver is granted by the shareholders' assembly, with a three-quarters majority of votes of present shareholders, provided that minority shareholders holding or representing at least 10 per cent of the company's share capital do not object to such waiver.

33 Employees

What role do employees play in corporate governance?

Employees do not generally play any important role in corporate governance. However, they can participate in corporate governance as shareholders as well as executive directors.

In addition, employees may affect everyday operations of the company through work councils and unions.

Pursuant to the Labour Law, work councils may be established in companies with more than 50 employees, with the aim of providing opinions and participating in decision-making concerning economic and social rights of employees in line with the Labour Law and the applicable employment-related general acts. Given that the role of work councils is not further regulated in the Labour Law, the above participation of work councils in corporate governance may be regulated through internal acts of a company (which is generally not the practice).

Aside from work councils, employees may establish work unions, which must be registered with the Labour Ministry. The unions have the right to be informed by the employer company (and consulted, depending on the case) on economic and labour-related issues that are important for employees or union members.

Furthermore, an employee may have a certain role in takeovers (see question 10).

34 Board and director evaluations

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

Apart from the specific obligation and competences of the board, its committees or individual directors, the applicable regulations do not prescribe specific obligations with respect to the conduct of evaluations or the manner or time frame of such evaluations. Therefore, the issue of evaluations of the board, its committees or directors should be regulated by the company's internal rules. In practice, large companies tend to implement various evaluations of its employees, including the board, its committees and directors.

Disclosure and transparency

35 Corporate charter and by-laws

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

As of 1 February 2012, articles of association and articles of incorporation, as well as amendments thereto, have to be filed and registered with the Serbian Business Registers Agency and published on its web page.

Moreover, all documents filed for registration purposes with said agency (eg, corporate governance decisions) are publicly available and may be inspected and copied upon request, subject to payment of applicable fees.

36 Company information

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

In general, legal entities in Serbia are obligated to disclose and register with the Serbian Business Registers Agency all corporate governance actions and the underlying documents (eg, documents on establishment of legal entities; shareholder structure; management; changes to the shareholder structure) and such documents are publicly available (see question 35).

Joint-stock companies, however, have additional disclosure obligations, which relate to their corporate governance, including but not limited to information on the shareholders' meetings, shareholders' decisions, etc.

Public companies, which are under scrutiny of the SEC and Belex, are obligated to provide a large amount of information to the SEC and Belex, including but not limited to: annual, semi-annual and quarterly financial statement-related reports, which also need to be disclosed to the public in line with the applicable regulations; changes to articles of incorporation and articles of association; changes to the rights arising out of proprietary shares; information on acquisitions of significant shareholdings within a company; prospectuses, etc.

Hot topics

37 Say-on-pay

Do shareholders have an advisory or other vote regarding executive remuneration? How frequently may they vote?

The shareholders' assembly is exclusively in charge of deciding the remunerations paid to directors or members of the supervisory board, if the company has a two-tier corporate governance system, and on the rules for determining such remunerations, including remunerations paid in shares and other securities of the company.

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38 Shareholder-nominated directors

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

Yes, shareholders with the right to propose the agenda for the shareholders' meeting (ie, shareholders holding at least 5 per cent of voting shares) are entitled to nominate directors (see question 23).

39 Shareholder engagement

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

Traditional ways in which companies engage with shareholders are through participation of the managing directors at shareholder assembly meetings (participation is mandatory in the case of annual meetings) and reporting by the managing directors at annual shareholder assembly meetings about:
- the accounting and financial reporting practices of the company and its affiliated companies, if any;
- compliance of the company's operations with the law and other regulations;
- company auditor's qualification and independence from the company, if the financial statements of the company were subject to an audit; and
- contracts concluded between the company and directors, as well as their affiliated persons.

Apart from in the traditional ways, companies are generally free to agree on other ways in which they can engage with shareholders.

Singapore

Leon Yee

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Sources of corporate governance rules and practices

1 Primary sources of law, regulation and practice

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

The corporate governance regime in Singapore focuses primarily on companies listed on the Singapore Exchange Securities Trading Limited (SGX-ST) and consists of laws, rules and recommended practices.

Company law

The Companies Act (chapter 50) of Singapore (CA) is the principal statute governing corporate governance matters in Singapore. The CA expressly provides that the board shall be responsible for the overall management of the company and may exercise all the powers of the company except any power that is required to be exercised by the company in general meetings under its constitution or the CA. The CA imposes specific duties on the board (see question 16).

The CA also codifies certain fiduciary duties of directors that existed at common law, for example, by providing that a director shall act honestly and use reasonable diligence in the discharge of his or her office and shall not make improper use of any information acquired by virtue of his or her position. These directors' duties are not exhaustive, but exist in addition to any other rule of law relating to the duty of directors or officers (including directors' duties under the common law, as set out below).

Under the CA, a director has the duty to disclose:

- his or her interests in transactions or proposed transactions with the company or any potential conflict arising from his or her holding other offices or possessing any property;
- particulars necessary for the company to maintain its register of directors' shareholdings and register of directors; and
- if he or she is a director of a public company, the date when he or she has or will have attained the age of 70 years.

Under the common law, a director owes the company the following fiduciary duties (which overlap with the statutory duties imposed by the CA):

- to act bona fide in the interests of the company;
- to exercise skill, care and diligence;
- not to place him or herself in a position of conflict with the company;
- not to make a secret profit from the company;
- to act within the powers conferred by the company's constitution and to exercise such powers for proper purposes; and
- not to fetter his or her discretion.

Listing regime

The Securities and Futures Act (chapter 289) of Singapore (SFA) and the Listing Manual of the SGX-ST (the Rules) play an important role in regulating the governance of Singapore-listed companies.

The SFA, which is the primary legislation regulating the securities and futures industry in Singapore, governs the offer of securities and regulates market conduct by providing for offences such as insider trading, false trading and market manipulation, dissemination of false information and the employment of manipulative and deceptive devices. Officers (including directors and senior management) of a listed company are required not to deal in its securities while in possession of material price-sensitive information and during the blackout period (ie, the period surrounding the announcement of the company's financial results); as such dealings could give rise to civil and criminal liability for insider trading under the SFA.

The Rules, which seek to secure and maintain confidence in the market, set out the requirements that a company must meet to qualify for admission to the Official List of the SGX-ST and the listing of its equity securities, as well as the continuing requirements that a listed company is required to observe. It should be noted that despite the non-statutory nature of the Rules, a company is obliged to comply with them once it lists on the SGX-ST. The SGX-ST has discretion in respect to the interpretation and application of the rules and may apply to the court to enforce them pursuant to sections 25, 203 and 325 of the SFA. Additionally (or in the alternative), the SGX-ST may punish non-compliance in other ways (eg, by reprimanding a company, halting or suspending its trading, or even delisting it).

Under the Rules, listed companies are also required to disclose their corporate governance practices with specific reference to the principles of the Code of Corporate Governance 2012 (the Code) and disclose and explain any deviation from any guideline of the Code in their annual reports. The Code recommends that listed companies make a positive confirmation at the start of the corporate governance section of their annual report that they have adhered to the principles and guidelines of the Code, or specify the areas of non-compliance, if any. The SGX-ST, on 29 January 2015, provided further guidance on compliance with the Code by way of an additional disclosure guide whereby listed companies are encouraged to answer and enclose such answers in their annual reports.

Code of Corporate Governance 2012

The Code was first issued by the Corporate Governance Committee on 21 March 2001, with the objective of encouraging Singapore-listed companies to enhance shareholder value through good corporate governance, and was effective from and applied to annual general meetings held from 1 January 2003 onwards. Following a review of the Code by the Council on Corporate Disclosure and Governance, a revised Code was issued on 14 July 2005, and has been effective from and applies to annual general meetings held on or after 1 January 2007.

In February 2010, the Monetary Authority of Singapore (MAS) announced the composition of a newly established Corporate Governance Council (the CG Council), which will play an advisory role to MAS, the Accounting and Corporate Regulatory Authority (ACRA) and the SGX-ST on matters relating to corporate governance and review the Code in light of the financial crisis. Members of the CG Council are drawn from the business community and stakeholder groups. As part of the efforts to enhance the corporate governance landscape in Singapore, the CG Council conducted a comprehensive review of the Code, which was last reviewed in 2005. The CG Council consulted the public extensively on proposed revisions to the Code, and submitted its recommendations to MAS on 22 November 2011 for consideration. On 2 May 2012, MAS incorporated all the recommendations made by the CG Council and issued a revised Code. The key changes to the Code are focused on the areas of director independence, board composition, director training, multiple directorships, alternate directors, remuneration practices and disclosures, risk management, as well as shareholder rights and roles. The revisions apply to annual reports relating to financial years commencing from 1 November 2012. Notwithstanding the above, as MAS recognises that sufficient time should be given for companies to make board composition changes, a longer transition period will be provided for necessary board composition changes to comply with the requirement for independent directors to make up at least half of the boards in specified circumstances (Guideline 2.2). These changes should be made at the annual general meetings following the end of financial years commencing on or after 1 May 2016.

The Singapore Code on Takeovers and Mergers

In Singapore, takeover offers are regulated under the SFA. The Singapore Code on Takeovers and Mergers (the Takeover Code), which was issued by MAS under the SFA, governs the takeover or merger of a company or business trust with a primary listing on the SGX-ST, or an unlisted public company or unlisted registered business trust with more than 50 shareholders or unit holders (as the case may be) and net tangible assets of S$5 million or more (target company). In a takeover situation, the board of a target company is required to observe both the spirit and provisions of the Takeover Code.

MAS, on the advice of the Securities Industry Council (SIC) issued a revised Takeover Code on 23 March 2012. The revised Takeover Code incorporated the feedback received from the public consultation conducted by the SIC on or around October 2011 and is consistent with international best practices. The amendments to the Takeover Code took effect on 9 April 2012.

The key changes to the Takeover Code were as follows:

- codify existing practices:
  - clarify that the SIC may take further actions against a person who breaches the Takeover Code in addition to depriving him or her of his or her ability to enjoy the facilities of the securities market in flagrant cases;
  - state that advisers who breach the Takeover Code may be required to abstain from Takeover Code-related work;
  - set out the rules, which, if breached, would normally result in compensation being directed by the SIC; and
  - publicise the factors that the SIC would consider in determining whether to permit an offeree company shareholder (who is not part of management) to invest in the bid company to the exclusion of all other offeree company shareholders;
- keep pace with product innovation and market developments:
  - clarify the application of the Takeover Code to real estate investment trusts and business trusts; and
  - clarify when an option or derivative transaction is subject to Rule 14 on mandatory offers, and require persons who would cross the mandatory offer thresholds as a result of such transactions to consult the SIC beforehand;
- enhance disclosure:
  - require disclosure of dealings in long options and derivatives over offeree company shares during the offer period by associates who hold 5 per cent or more in the offeree company;
  - require the offeror to disclose the number and percentage of his or her shareholdings that have been charged as security, borrowed or lent; and
  - lower the shareholding threshold for a shareholder to disclose dealings in the offeree company shares during the offer period from 10 to 5 per cent;
- provide greater flexibility:
  - provide for a class exemption to shareholders of a company from the requirement to make a mandatory offer as a result of the company buying back its shares; and
- other changes:
  - set out the circumstances where shareholders voting together on a board control-seeking resolution might be regarded as parties acting in concert.

2 Responsible entities

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

ACRA is responsible for the administration of the CA. A steering committee, chaired by the Attorney-General and supported by a joint secretariat comprising the Ministry of Finance (MOF), the Attorney-General's Chambers and ACRA, had been appointed by the Minister of Finance to review the CA and had issued its proposals for public consultation in the first half of 2010. Some of the key amendments proposed include allowing nominee companies or custodian banks to appoint more than two proxies to attend general meetings of a company, enhancing investor rights for Central Provident Fund (CPF) members who buy company shares through the CPF Investment Schemes, increasing minority shareholder protection and alternative modes of executing documents.

MAS has oversight of the securities and futures market in Singapore and has powers under the SFA to issue directions to the SGX-ST, make regulations for the due administration of the SFA, carry out civil enforcement actions in relation to market misconduct and conduct investigations in relation to matters under the SFA.

The Rules are made by the SGX-ST, subject to any requirements that may be prescribed by MAS under the SFA. If a listed company fails to comply with the Rules, MAS or the SGX-ST may apply to court to enforce the Rules, or the SGX-ST may reprimand the company, suspend the trading of the company's securities or delist the company.

The Code was brought within the purview of MAS and the SGX-ST with effect from 1 September 2007. On 4 February 2010, MAS announced the establishment of the CG Council. The purpose of the CG Council is to promote a high standard of corporate governance in companies listed in Singapore, so as to maintain investors' confidence and enhance Singapore's reputation as a leading and trusted international financial centre. The CG Council also plays an advisory role to MAS, ACRA and the SGX-ST on matters relating to corporate governance.

The Takeover Code was issued by MAS under the SFA and it is administered by the Securities Industry Council (SIC), which comprises representatives from the private sector and the public sector appointed by the Minister of Finance. SIC has powers under the SFA to investigate any dealing in securities that is connected with a takeover offer. If SIC finds a breach of the Takeover Code, it may have recourse to private reprimand or public censure or further action designed to deprive the offender of the facilities of the securities market. If SIC finds evidence that a criminal offence has taken place, it will refer the matter to the appropriate authority.

In addition, certain organisations have been established to provide guidance and promote best practices in relation to corporate governance matters, such as the Singapore Institute of Directors, which was set up to promote the professional development of directors and uphold corporate governance standards and the Audit Committee Guidance Committee, which was set up to develop practical guidance for the audit committees of listed companies.

The rights and equitable treatment of shareholders

3 Shareholder powers

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

The CA states that unless provided for otherwise by the constitution of a company, a company may appoint a director by way of ordinary resolution. In addition, the CA states that unless provided for otherwise by its constitution, private companies may also remove its directors by way of ordinary resolution (simple majority of over 50 per cent of the votes cast at the meeting). The constitution of a company will typically provide that directors are to be elected or removed by shareholders passing an ordinary resolution (ie, a resolution passed by a simple majority of members present and voting) at a general meeting.

In the case of public companies, the CA does not permit the appointment of two or more persons as directors by a single resolution, unless it is unanimously agreed to by the meeting that such a resolution may be moved. This is to allow members the opportunity to accept or reject each nominated director. Shareholders of listed companies may propose a candidate for election to the office of director by leaving at the office of the company (at least 11 clear days before the general meeting) a written notice signed by the nominee, consenting to the nomination and signifying his or her candidature for the office, or the intention of such member to propose him or her. The constitution of private companies may provide that certain shareholders have the power to appoint directors; however, such an article will not be enforceable by a person who is not a member of the company unless there is a separate contract outside the constitution embodying that right.

Shareholders of a public company may, by way of an ordinary resolution passed in a general meeting, remove a director before the expiry of his or her term of office, notwithstanding anything contained in the constitution of the public company or in any agreement between the public company and the director. By contrast, a director of a private company may only be removed from office in accordance with its constitution. If the constitution does not provide for the removal of directors, directors cannot be removed before the expiry of their term of office unless the constitution is suitably amended. The constitution of a private company may be drafted to contain provisions to entrench certain directors.

Shareholders holding at least 10 per cent of the paid-up capital of the company, pursuant to the CA, may use their power to call for or requisition an extraordinary general meeting and require resolutions to be put for the purpose of appointing or removing directors, or amending the constitution to compel the board to pursue a particular course of action.

4 Shareholder decisions

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

The following matters require shareholders' approval under the CA:

- amendments to the constitution of the company;
- alteration of share capital;
- issuance of shares;
- reduction of share capital;
- disposal of the whole or substantially the whole of the company's undertaking or property;
- provision or improvement of emoluments to directors in respect of their office; and
- appointment of auditors.

In addition, the Rules require listed companies to obtain shareholders' approval for, inter alia: transactions with interested persons (as defined in the Rules); and acquisitions and disposals that exceed certain financial thresholds.

Furthermore, pursuant to shareholder agreements or amendments to the constitution, additional matters may require shareholders' approval.

The CA does not require any matter to be subject to a non-binding shareholder vote. However, shareholders may call for or requisition an extraordinary general meeting and require resolutions to be passed (see questions 3 and 6).

5 Disproportionate voting rights

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

In the case of public companies, at a poll at any general meeting, each equity share carries one vote only (the exception being 'golden' shares issued by listed companies in certain regulated industries). Likewise, for private companies, each share carries one vote only, unless the constitution provides otherwise. The constitution may provide that a member shall not be entitled to vote unless all calls or other sums personally payable by him or her in respect of the company have been paid.

6 Shareholders' meetings and voting

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

The general rule is that every member who holds ordinary shares (excluding treasury shares) shall have a right to attend any general meeting of the company and to speak and vote on any resolution before the meeting. However, the constitution may provide that a member shall not be entitled to vote unless all calls or other sums personally payable by him or her in respect of the company have been paid. That being said, all shareholders are entitled to vote on any resolution to voluntarily wind-up the company or on any resolution that proposes to vary rights attached to a specific share. A shareholder may appoint a proxy (who need not be a shareholder) to vote on his or her behalf. Only shareholders of private companies and unlisted public companies may pass resolutions by written means; however, these must strictly comply with the requirements under sections 184B and 184F of the CA. Whether a company is able to hold a virtual meeting of shareholders depends on its constitution. Where a company's constitution provides for virtual meetings of shareholders, it should also set out the manner in which the virtual meeting of shareholders is to be conducted.

7 Shareholders and the board

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

Generally, two or more shareholders holding not less than 10 per cent of the company's issued share capital (excluding treasury shares) may call a meeting of the company.

Shareholders of the company (numbering not less than 5 per cent of the members entitled to vote or not less than 100 shareholders who hold shares on which there has been paid up an average sum of S$500 per member) can then requisition the company to circulate the proposed resolution (which may include director nominations) and a statement containing further details in respect of the proposed resolution. This must be done at the expense of the requisitionists (unless the company otherwise resolves). The copy of the requisition sent must contain signatures of all the requisitionists, must be deposited at the registered office of the company and must be followed by a sum of money reasonably sufficient to meet the company's expenses in giving effect to the resolution.

8 Controlling shareholders' duties

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

Controlling shareholders do not generally owe duties to the company or to non-controlling shareholders. However, a shareholder may apply to court for relief where the affairs of a company are being conducted in a manner that is oppressive towards him or her, disregards his or her interests, discriminates unfairly against him or her or is otherwise prejudicial to him or her under section 216 of the CA. A successful application under section 216 of the CA gives the Court the discretion to make a wide variety of orders, including but not limited to, directing or prohibiting acts and varying transactions.

Where the controlling shareholders also sit on the board of the company, they will then owe directors duties to the company. Other shareholders may then step into the shoes of a company, and bring enforcement action through either a common law derivative action or statutory derivative action (private companies only).

9 Shareholder responsibility

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

Shareholders are not generally held responsible for the acts or omissions of the company, except in exceptional circumstances. Shareholders of a company limited by shares are generally not liable for its debts except to the extent that they are liable as contributories on the winding-up of the company, such liability being limited to any unpaid amount on shares held.

Corporate control

10 Anti-takeover devices

Are anti-takeover devices permitted?

Where the board of a target company believes a takeover offer is imminent, the Takeover Code requires that the board must not take any action that could effectively result in the takeover offer being frustrated or the shareholders being denied an opportunity to decide on its merits. The board, in advising the shareholders, should have regard to the interests of the shareholders as a whole.

11 Issuance of new shares

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

The constitution usually vests the power to issue shares in directors. However, the directors must not exercise any power to issue shares without the prior approval of the company in the general meeting.

Shareholders may have pre-emptive rights to acquire newly issued shares if the constitution so provides. However, the constitution of a listed company must provide that, subject to any direction to the contrary that may be given by the company in a general meeting or except as permitted under the Rules, all new shares of listed companies shall, before issue, be offered to existing shareholders in proportion, as far as circumstances admit, to the amount of the existing shares to which they are entitled.

12 Restrictions on the transfer of fully paid shares

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

Shares are transferable in the manner provided for in the constitution. The transfer of shares in a private company must be restricted in some way, usually by giving directors discretion to refuse to register the transfer or existing shareholders' pre-emptive rights. Public companies may, but are not required to, impose restrictions on the transfer of their shares. Listed companies are not permitted to restrict the transfer of their shares, except in the case of certain regulated industries where these companies are permitted to restrict the transfer of their shares to foreigners (eg, banks and some privatised government companies).

13 Compulsory repurchase rules

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

If a company (offerer) acquires or has contracted to acquire at least 90 per cent of the shares in another company (the target company), it may compulsorily acquire the shares of the target company that are held by dissenting shareholders. Once the offerer gives a dissenting shareholder notice of its intention to acquire the shares held by the dissenting shareholder, unless the court thinks fit to order otherwise on the application of the dissenting shareholder, the offeror will be bound to acquire the shares on the same terms as those applicable to the original offer for the acquisition of 90 per cent of the shares.

14 Dissenters' rights

Do shareholders have appraisal rights?

In Singapore, shareholders do not have appraisal rights under the CA. Shareholders of private companies may have appraisal rights if these are expressly provided for in the constitution or a shareholders' agreement.

The responsibilities of the board (supervisory)

15 Board structure

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

Listed companies have a one-tier board structure.

16 Board's legal responsibilities

What are the board's primary legal responsibilities?

Under the CA, the board has a general duty to manage the company's business and is also obliged:

- to ensure that the company keeps such accounting and other records as are necessary to explain the transactions and financial position of the company;
- to present the audited accounts of the company at the annual general meeting;
- not to knowingly incur debts when there is no reasonable ground for expecting that the company will be able to pay the debts;
- not to allow payment of dividends by the company unless there are profits available for that purpose; and
- to ensure that the company complies with its statutory obligations under the CA (such as the obligations to maintain statutory books, make statutory filings with ACRA and convene general meetings annually) and other relevant laws and regulations.

The boards of listed companies have additional responsibilities under the Rules and the Takeover Code.

17 Board obligees

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

The board represents and owes fiduciary duties to the company. However, in discharging its duties, the board is entitled to consider the company's commercial interests, the collective interests of shareholders and the interests of employees. Where the company is close to insolvency, the board must place a greater emphasis on the interests of creditors.

18 Enforcement action against directors

Can an enforcement action against directors be brought by, or on behalf of, those to whom duties are owed?

Directors owe fiduciary duties to the company and the company may bring an action against its directors for the breach of these duties. Where the company has not brought an action against the defaulting director, a shareholder may seek the court's leave to bring a derivative action (ie, an action brought on behalf of the company and in respect of a cause of action vested in the company) against such director.

19 Care and prudence

Do the board's duties include a care or prudence element?

Under the CA, directors are required to act honestly at all times and to use reasonable diligence in the discharge of their duties, and shall act in the best interests of the company. Directors' fiduciary duties under the common law include the duty to exercise care, skill and diligence. The standard of care and diligence expected of a director is objective; a director is expected to exercise the same degree of care and diligence as a reasonable director in his or her position. However, this standard is not fixed but a continuum depending on various factors such as the individual's role in the company, the type of decision being made, the size and the business of the company. This standard will not be lowered to accommodate any inadequacies in the individual's knowledge or experience. The standard will, however, be raised if he or she held him or herself out to possess, or if he or she in fact possesses, some special knowledge or experience.

20 Board member duties

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

All directors are subject to the same responsibilities under the general law, although the expectations of the necessary actions to fulfil directors' duties may differ (see question 19).

21 Delegation of board responsibilities

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

In practice, the board of a listed company will delegate responsibility for the day-to-day operations of the company to management, and responsibilities for certain board matters to its audit, remuneration and nomination committees (see question 25). However, directors have a non-delegable duty of supervision that is objective (*Vita Health Laboratories Pte Ltd v Pang Seng Meng* [2004] 4 SLR 162).

22 Non-executive and independent directors

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

Listed companies are required under the Rules to have at least two non-executive directors who are independent and free of any material business or financial connection with the listed company. Further, the Code recommends that at least one-third of the board should comprise independent directors. In addition, pursuant to Guideline 2.2 of the Code, independent directors should make up at least half of the board in any of the following four scenarios:

- the chairman of the board and the chief executive officer (CEO) (or equivalent) are the same person;
- the chairman and the CEO are immediate family members;
- the chairman is part of the management team; or
- the chairman is not an independent director.

Principle 2 of the Code states that there should be a strong and independent element on the board of companies which is able to exercise objective judgement on corporate affairs independent from management and shareholders with at least 10 per cent of the total voting shares. The Code defines an 'independent' director as one who has no relationship with the company, its related companies, any shareholders with at least 10 per cent of the total voting shares or its officers that could interfere, or be reasonably perceived to interfere, with the exercise of the director's independent business judgement with a view to the best interests of the company. Guideline 2.4 of the latest Code also states that the independence of any director who has served on the board beyond nine years from the date of his or her first appointment should be subject to particularly rigorous review. The board should also explain why any such director should be considered independent.

The CA defines a 'non-executive director' as a director who is not an employee of, and does not hold any other office of profit in, the company or its related corporation in conjunction with his or her office of director and his or her membership of any audit committee. While there is no distinction drawn between the duties of independent directors and non-independent directors under the CA and the Rules and independent directors, by definition, are also non-executive directors, non-executive directors are not necessarily independent directors pursuant to Guideline 2.2 of the Code. The Code states that the role of non-executive directors is to constructively challenge and help develop proposals on strategy, to review the performance of management in meeting agreed goals and objectives, and to monitor the reporting of performance. To facilitate a more effective check on management, the Code also encourages non-executive directors to meet regularly without the presence of management.

All directors are subject to the same responsibilities under the general law, although the expectations of the necessary actions to fulfil directors' duties may differ (see question 19). Although independent directors, as non-executive directors, are not expected to give the same continuous attention to the affairs of the company as executive directors, they will be liable, just like executive directors, if it is found that they failed to properly discharge their duties at law. This is illustrated in a recent case involving the release of a misleading statement by a listed company, Airocean, where the court had imposed a fine on the other directors involved in the offence but imposed a four-month custodial sentence on the independent director as he was found to have played a major part and was the most culpable among the directors in relation to the release of the misleading statement that downplayed a bribery probe involving Airocean's former chief executive officer (*PP v Chong Keng Ban @ Johnson Chong & Ors*). However, in the independent director's appeal to the High Court, the then Chief Justice Chan SekKeong acquitted him stating that Airocean had not acted recklessly as the company had relied on legal advice from its lawyer and acted in accordance with the legal advice that has been provided (*Madhavan Peter v Public Prosecutor and other appeals*).

23 Board size and composition

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

In general, there is no legal requirement as to board size, apart from the minimum requirement under section 145 of the CA that each company is required to have at least one director who is ordinarily resident in Singapore (ie, resident in Singapore with some degree of continuity and apart from accidental or temporary absences, and is independent from citizenship). Any person may be a director as long as he or she is a natural person, of full age (ie, 21 years) and capacity. Although there is no requirement that a director must have any particular educational qualification or business experience, the CA imposes restrictions on the following categories of persons from assuming the post of a director:

- undischarged bankrupts;
- unfit directors of insolvent companies (ie, the court being satisfied that the conduct of a director of a company that went into insolvent liquidation makes him or her unfit to take part in the management of a company);
- persons who had been convicted of offences involving fraud and dishonesty, and management offences;
- persons who had been thrice convicted of failing to file returns, accounts and documents with ACRA as required under the CA; and
- directors of companies that had been wound up on grounds of national security.

With reference to the above, it should be noted that the constitution of the individual company may increase the minimum number of directors or require specific qualifications in respect of the directors. Additionally, in the case of listed companies, the Code recommends that independent directors should make up at least one-third of the board in ordinary circumstances, and one-half the board where there are relationships or circumstances that are likely to effect, or could appear to affect the director's judgement.

If the company only possesses one director and he or she vacates office, this absence will be deemed invalid as this would contravene the requirement of the company having at least one director. All subsequent and additional appointments of directors and casual vacancies are dictated by the constitution of the company. In the case of listed companies, the nominating committee of a listed company is responsible for recommending candidates to be appointed to the board of directors.

The board composition of listed companies is typically disclosed in the annual report as the Code recommends that listed companies disclose in their annual report several matters relating to a board's practices (see question 27). The nominating committee of a listed company is responsible for recommending candidates to be appointed to the board of directors. Companies are also generally required to provide information on the composition of their board and their directors to ACRA.

24 Board leadership

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

The Code recommends that there be a clear division of responsibilities at the helm of the company. Therefore, the chairman of the board (chairman) and the CEO should be separate persons, to ensure an appropriate balance of power (between the board and management), increased accountability (of management to the board) and greater capacity of the board for independent decision-making. However, it is not unusual for the chairman and CEO of listed companies to be the same person.

In addition, companies should disclose the relationship between the chairman and CEO where they are immediately related. Companies should appoint an independent non-executive director to be the lead independent director where the chairman and the CEO:
- are the same person;
- are related by close family ties;
- are both part of the executive management team; or
- the chairman is not independent.

The independent directors of a Singapore-listed company should make up at least half of its board under any of the four specific scenarios listed in question 22.

The lead independent director (if appointed) should be available to shareholders where they have concerns and for which contact through the normal channels of the chairman, CEO or chief financial officer (or equivalent) has failed to resolve or is inappropriate.

25 Board committees

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

The CA requires every listed company to establish an audit committee comprising three or more members of the board, the majority of whom must be independent directors. The chairman of the audit committee must not be an executive director or employee of the company or its related corporation.

Additionally, the Code recommends that the audit committee should comprise at least three directors, all non-executive, the majority of whom, including the audit committee chairman, should be independent. At least two members of the audit committee including the audit committee chairman should have accounting or related financial management expertise or experience. The CA, the Rules and the Code set out the role of the audit committee in reviewing audit matters, financial reporting matters, the internal control systems of the company and interested party transactions.

The Code recommends that every listed company establishes a nominating committee to make recommendations to the board on all board appointments (including the renomination of directors). The nominating committee is also responsible for determining if a director is independent, bearing in mind the circumstances set forth in Guidelines 2.3 and 2.4. The nominating committee should comprise at least three directors, a majority of whom, including the chairman, should be independent. The lead independent director, if any, should be a member of the nominating committee.

The Code also recommends that every listed company establishes a remuneration committee to make recommendations to the board on the remuneration of directors and the CEO (or executive of equivalent rank) and review the remuneration of senior management. The remuneration committee should comprise of at least three directors, all non-executive, the majority of whom, including the remuneration committee chairman, are independent.

Guideline 11 of the Code states that the board should be responsible for the governance of risk in the company, and recommends the establishment of a separate risk committee or otherwise assess appropriate means to assist it in carrying out the responsibility of overseeing the company's risk management framework and policies.

26 Board meetings

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

Neither the CA nor the Rules prescribe a minimum number of board meetings to be held each year. The Code recommends that the board meets regularly and as warranted by particular circumstances, as deemed appropriate by the board members.

27 Board practices

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

The Code recommends that listed companies disclose in their annual report, inter alia, the following matters relating to a board's practices:
- any delegation of authority by the board, to any board committee, to make decisions on certain board matters;
- the number of board and board committee meetings held in the year, and the attendance of every board member at these meetings;
- the type of material transactions that require board approval under internal guidelines;
- where the company considers a director to be independent in spite of the existence of a relationship as stated in the Code that would otherwise deem him or her as non-independent, the nature of the director's relationship and the reason for considering him or her as independent;
- where the board considers an independent director, who has served on the board for more than nine years from the date of his or her first appointment, to be independent, the reasons for considering him or her independent;
- the relationship between the chairman and CEO where they are related to each other;
- the composition of the nomination, remuneration and audit committees;
- the process for the selection and appointment of new directors to the board;
- the process for assessing the effectiveness of the board as a whole and the contribution of each individual director; and
- the maximum number of listed company board representations that its directors may hold.

On 29 January 2015 the SGX-ST provided further guidance on disclosures for compliance with the Code.

28 Remuneration of directors

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

A company cannot provide or improve emoluments for a director in respect of his or her office unless the provision is approved by a shareholders' resolution that is not related to other matters.

The Code recommends that the remuneration committee makes recommendations on remuneration policies and packages of directors and senior management to be submitted to the board for endorsement (see question 25). For listed companies, the fees payable to non-executive directors must be a fixed sum, and not by a commission on or a percentage of profits or turnover and likewise, salaries payable to executive directors may not include a commission on or a percentage of turnover. The Code recommends that executive directors' remuneration should be structured to link rewards to corporate and individual performance, and long-term incentive schemes are encouraged. Non-executive directors' remuneration should be linked to their level of contribution and responsibilities, and the remuneration committee should consider implementing schemes to encourage non-executive directors to hold shares in the company to align their interests with shareholders. The remuneration of executive directors and senior management is typically not put forward for shareholders' approval at the annual general meeting (see question 37). The Code also recommends that the

Update and trends

The MAS announced on 27 February 2017 that it had formed a new Corporate Governance Council (the New CG Council) to review the Code. The review will include an examination of how the current corporate governance regime can be made more effective. A public consultation will be carried out in respect of the New CG Council's recommendations at a later date. The New CG Council's chairman, Mr Chew Choon Seng, former Chairman of the Singapore Exchange (SGX) stated that the review of the Code will take into account changes in Singapore's corporate landscape as well as international developments.

From 1 January 2018, Singapore incorporated companies listed on the SGX-ST will need to apply a new accounting framework similar to the International Financial Reporting Standards. In addition, the revised auditing standards will include the requirement that the auditor will be required to consider whether the annual report of the company under audit (excluding the financial statements) (the 'other information') is materially inconsistent with the knowledge obtained by the auditor during the audit. The auditor will also be required to report whether the other information was received prior to the signing of the audit report. Currently, almost all listed companies in Singapore do not issue their annual reports at the time when the audit of the financial statements is signed off. This new change will significantly impact the workflow in relation to the preparing of annual reports for Singapore companies listed on SGX-ST.

We anticipate that the latest review of the Code will lead to a significant increase in disclosure and compliance requirements as set out in its guidelines as well as a corresponding update to the Rules to revise the current leeway granted to listed companies to deviate from the guidelines of the Code. During the past year, concerns on the issues of disclosure of remuneration, board diversity and board independence have been raised by not only regulators and leading experts in corporate governance, but also the Singapore government. Some of these views include the view taken by the president and chief executive of the Securities Investors Association (Singapore) urging regulators to consider requiring boards of listed companies to have formal independent reviews of long-term independent directors; the Minister for Culture, Community and Youth advocating that by 2020 at least 20 per cent of board seats are filled by women; and the chief executive of ACRA advocating the improving of current financial reporting by listed companies.

This push for improving corporate governance is to be taken in context of recent incidents in Singapore relating to corporate governance concerns. One of the most notable instances was that of a multi-billion dollar Singapore listed company failing to disclose its lead independent director's interest in certain acquisitions. The result of this failure to disclose led to a shakeup in the company's board and senior management, as well as ongoing investigations by ACRA for possible breaches of the CA. Another significant incident was the judicial management of a leading Singapore listed engineering, procurement, construction and installation (EPCI) company. In addition to leading experts having highlighted the lack of proper disclosure in said EPCI company's announcements , the company and its current and past directors are under investigation by the Commercial Affairs Department, a department of the Singapore police force, for possible breaches of the SFA.

remuneration policy, level and mix of remuneration, and the procedure for setting remuneration be disclosed in the annual report of the company, and the remuneration of each individual director and the CEO on a named basis should also be disclosed.

Listed companies typically provide in their constitutions that directors are to resign and present themselves for re-election at least every three years, as recommended by the Code. Constitutions of listed companies must also provide that, where a managing director or a person holding an equivalent position in a listed company is appointed for a fixed term, the term must not exceed five years.

Companies (other than private companies in which no corporation holds a beneficial interest and that have no more than 20 members) are prohibited from granting loans or entering into any guarantee in relation to loans made to their directors or directors of their related companies, subject to limited exceptions under the CA. Prior to listing, all debts owing to the company or the group to be listed by its directors, substantial shareholders and companies controlled by such directors and substantial shareholders should be settled.

Directors are not prohibited from dealing with the company but they must disclose to the board any interest (whether direct or indirect) that they have in any transaction with the company, unless such interest may properly be regarded as being immaterial. Under the Rules, the constitutions of listed companies must provide that a director must not vote during board deliberations in relation to any contract or proposed contract or arrangement in which he or she has, directly or indirectly, a personal material interest.

29 Remuneration of senior management

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

Executive remuneration is a matter for the board to determine. The Code recommends that the remuneration committee should recommend to the board a framework of remuneration and the specific remuneration package for the CEO or executive of equivalent rank, and review the remuneration of senior management.

30 D&O liability insurance

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

Companies are allowed but not obliged to purchase and maintain directors' and officers' liability insurance to insure directors and officers against monetary liability arising from any claims made against them in respect of their performance of duties. At present, it is not a widespread practice for unlisted companies to purchase directors' and officers' liability insurance for their directors and officers but it is increasingly common for public-listed companies to do so.

31 Indemnification of directors and officers

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

Under the CA, any provision (whether in the constitution or in any contract or otherwise) exempting an officer (including a director) from or indemnifying him or her against liability for negligence, default, breach of duty or breach of trust is void. However, a company may purchase and maintain insurance against such liability for its officers or indemnify an officer against any liability incurred by him or her: in defending any proceedings in which a judgment is given in his or her favour or in which he or she is acquitted; or where the court has exercised its power to relieve him or her from such liability.

32 Exculpation of directors and officers

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

Shareholders may agree to release a director from his or her fiduciary duties and excuse him or her for liability for breaches of duty to the company provided the director has made a full and frank disclosure of all material facts. Shareholders cannot, however, ratify an illegal act. Additionally, under the CA, the court has the power to relieve directors from the consequences of their negligence, default, breach of duty or breach of trust, but the court will only exercise such power to excuse directors who have not received the company's property in breach of trust. See also question 31.

33 Employees

What role do employees play in corporate governance?

At present, employees do not play a formal role in the corporate governance process, except to the extent that they are also shareholders, directors or officers of the corporation. However, through whistle-blowing, employees may help to uncover acts of misfeasance by the company's management. The Code recommends that the audit committees ensure that appropriate measures are put in place for employees to raise any concerns in strict confidence with regard to any act of misfeasance by the management, together with an appropriate follow-up independent investigation of the concerns raised.

34 Board and director evaluations

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

In respect of listed companies, the Code recommends a formal assessment of the effectiveness of the board as a whole and the contribution made by each director. The evaluation process should be carried out by the nominating committee, and the results of the assessment should be disclosed in the company's annual report.

The Code further recommends that the nominating committee put together objective performance criteria to measure the board against. This should allow comparison with its industry peers and address how the board has enhanced long-term shareholder's value (eg, the company's return on investment, return on equity, return on assets over a long-term period). Individual evaluation should aim to assess whether each director continues to contribute effectively and demonstrates commitment to the role.

There are no similar laws or regulations requiring private companies to do the same.

Disclosure and transparency

35 Corporate charter and by-laws

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

The constitution of a company incorporated in Singapore is publicly available from ACRA, for a fee. However, such constitution may not include any amendments to it made pursuant to resolutions. While resolutions made by the company may be separately obtained from ACRA for a fee, prior to the purchase of such resolutions an interested party will not be able to identify the contents of resolutions filed by the company.

36 Company information

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

Listed companies must observe the continuing disclosure requirements in the Rules and make timely and non-misleading disclosure of the information set out below (which is non-exhaustive):

- material information (including information necessary to avoid the establishment of a false market in its securities, information that might be price sensitive and information concerning the listed company's assets, business, financial condition and prospects, information concerning a significant change of ownership of the listed company's securities owned by insiders, a change in effective or voting control of the issuer and any developments that materially affect the present or potential rights or interests of the shareholders);
- transactions between the listed company and interested persons (and obtain shareholder approval if necessary);
- acquisitions and disposals that exceed certain financial thresholds (and obtain shareholder approval if necessary); and
- the financial statements of the company for each full financial year and for each of the first three-quarters of its financial year.

The Code sets out additional matters that listed companies are encouraged to disclose in their annual reports, such as the remuneration of directors and key executives, the policy on remuneration, details of employee share schemes and the adequacy of internal control systems.

Hot topics

37 Say-on-pay

Do shareholders have an advisory or other vote regarding executive remuneration? How frequently may they vote?

Typically, the remuneration of executive directors and senior management is not put forward for shareholders' approval at the annual general meeting. Executive directors' remuneration falls within the purview of the remuneration committee. However, where the executive directors' remuneration includes employee share options or incentive shares, separate shareholders' approval may be required prior to the grant of such share options or share awards.

38 Shareholder-nominated directors

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

Shareholders can nominate directors without the recommendation of the board (see questions 3 and 7).

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39 Shareholder engagement

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

The Rules require listed companies to make continual disclosures relating to select matters, including but not limited to any information likely to materially affect the price of a listed company's securities. Such disclosures are to be made on the SGX-ST's website, SGXNET. The Code also recommends that listed companies actively engage their shareholders and put in place an investor relations policy to promote regular, effective and fair communication with shareholders. Some of the recommended ways in which companies can engage their shareholders that are set out in the Code include disclosing information through a company website and establishing regular dialogue by way of analyst briefings or investor roadshows. The foregoing is in addition to annual meetings, which are required by all companies under the Act.

Typically, for engagement efforts outside annual meetings, representatives from listed companies are limited to management. At annual meetings, engagement efforts are usually led by the directors and senior management. However, for annual meetings and extraordinary general meetings where the listed company is seeking approval from shareholders for specific transactions or corporate actions, it is common for the relevant outside counsel to be present to answer shareholder queries.

Switzerland

Daniel Schoch, Annina Müller and Christophe Pétermann

Meyerlustenberger Lachenal

Sources of corporate governance rules and practices

1 Primary sources of law, regulation and practice

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

There are several sources of law relating to corporate governance. The primary sources of law are the provisions on stock corporations (article 620 et seq of the Swiss Federal Code of Obligations (CO) which is currently under review) and the Swiss Federal Act on Financial Market Infrastructures and Market Conduct in Securities and Derivatives Trading (Financial Market Infrastructure Act (FMIA)) which entered into force on 1 January 2016. Several provisions relating to corporate governance which were previously incorporated in the Swiss Federal Stock Exchange and Securities Trading Act (SESTA) have been transferred to the FMIA. Such provisions include regulations on market abuse and its sanctions, disclosure of shareholdings and public takeover offers relating to listed companies. The SESTA is still in force but is limited to governing the authorisation and supervision of securities brokers for the professional securities trading. These remaining provisions are expected to be transferred to the Financial Institutes Act (FinIA) which is still in the legislative process. The FMIA as well as the SESTA are both concretised by ordinances.

Furthermore, the Swiss Financial Market Supervisory Authority (FINMA) has the competence to issue directives and circulars. For the present questionnaire its circular 'Minimum standards for remuneration schemes for financial institutions' (in force since 1 January 2010) is of interest.

The Ordinance against Excessive Compensation in Listed Companies (OaEC) entered into force on 1 January 2014 and is now fully effective. It is only applicable to stock corporations governed by Swiss law whose shares are listed on a stock exchange in Switzerland or abroad.

The SIX Swiss Stock Exchange (SIX) as well as the BX Berne eXchange (BX), both currently still self-regulatory organisations under the SESTA, have submitted a new request for authorisation to FINMA and, hence, in future will be self-regulatory organisations under FMIA. They have issued listing rules that include specific reporting and disclosure requirements. The SIX 'Directive on information relating to corporate governance' (SIX Directive Corporate Governance (DCG)) is of importance, obliging the issuers to disclose certain information with regard to corporate governance in a separate section of their annual reports. While the listing rules are binding, the principle of 'comply or explain' applies under the DCG, meaning that if an issuer refrains from disclosing information prescribed in the annex of the DCG, the issuer must point out this fact in the corporate governance report and give substantial grounds for each individual case for which information is not disclosed (for further details, see question 36).

Economiesuisse, an influential association of Swiss businesses, has issued a Swiss Code of Best Practice for Corporate Governance (SCBP, issued in 2002 and amended in 2014). The SCBP sets standards in the form of non-binding recommendations. The code primarily addresses listed companies, but may also serve as guidelines for non-listed, economically significant companies or organisations. Furthermore, the 'Guidelines for institutional investors governing the exercise of shareholder rights in Swiss listed companies' aim at enhancing good corporate governance by describing best practices for the exercise of shareholders' rights by institutional investors. These self-regulating non-binding recommendations have been published by an important group of representatives of Swiss institutional investors, proxy advisers and economical associations.

2 Responsible entities

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

Besides the Swiss government itself, there are two main governmental authorities, the FINMA and the Swiss Takeover Board (TOB), which are the main regulators and enforcers.

On a non-governmental basis, the SIX issues and enforces the SIX listing rules, which first need to be approved by FINMA.

There has been considerable shareholder activism in recent years and proxy adivsers such as Ethos, Swipra, zCapital, ISS and Glass Lewis are gaining importance. They are mandated by a growing number of Swiss pension funds to represent their votes in the general meetings of shareholders of listed companies.

In 2016, the Swiss National Bank also decided to exercise the voting rights of its share portfolio in regard to corporate governance questions.

The rights and equitable treatment of shareholders

3 Shareholder powers

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

One of the fundamental and non-transferable competences of the shareholders' meeting is to vote on the appointment or removal of the members of the board. Therefore, any shareholder may vote on this in a shareholders' meeting if the agenda of such meeting provides for the appointment and removal of directors, as the case may be. The shareholders' meeting of listed companies is required by the OaEC to re-elect annually the members and the chairman of the board as well as the members of the compensation committee.

The decision is made by an absolute majority of the voting rights represented at the respective meeting, unless otherwise provided for by the articles of association.

The shareholders do not have a direct possibility to require the board to pursue a particular course of action. However, certain matters require a shareholders' decision (see question 4).

4 Shareholder decisions

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

The following decisions have to be adopted by the general meeting of shareholders:

- adoption and amendment of the articles of association;
- appointment or removal of the members of the board and the auditors;
- approval or rejection of the management report, including, if applicable, the consolidated financial statements;
- approval or rejection of the use of the balance sheet profit and, in particular, the declaration of dividends;
- discharge of the members of the board from liability; and
- matters that are by law or by the articles of association reserved to the shareholders' meeting.

Non-binding shareholders' votes are not provided for under Swiss law and the legal effects of such votes are unclear.

5 Disproportionate voting rights

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

Subject to a corresponding provision in the articles of association, companies are entitled to introduce voting shares. Such shares grant the right of one vote per share despite their par value being a fraction of the par value of the ordinary shares. The maximum ratio allowed between the par value of a voting share and an ordinary share is 1:10. Voting shares can only be issued as registered shares and must be fully paid up. Moreover, disproportionate voting rights do not apply for the following decisions of the shareholders' meeting:

- the election of the auditors;
- the appointment of experts to audit the company's business management or parts thereof;
- any resolution concerning the instigation of a special audit; and
- any resolution concerning the initiation of a liability action.

6 Shareholders' meetings and voting

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

It is each shareholder's right to participate in the shareholders' meeting and to exercise his or her voting rights. The shareholder may have his or her shares represented by a third party who, unless provided otherwise in the articles of association, does not need to be a shareholder.

Under the applicable law it is not permissible to pass a shareholders' resolution without a physical meeting. This also applies for direct electronic voting. However, listed companies are obliged to ensure that powers of attorney and instructions for the independent proxy may also be given electronically (indirect electronic voting).

7 Shareholders and the board

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

One or more shareholders representing (together) at least 10 per cent of the issued share capital may request the convention of a shareholders' meeting. Shareholders representing shares with a nominal value of 1 million francs or at least 10 per cent of the issued share capital (if such amount is lower) may demand that an item be placed on the agenda. A demand for the convention of a shareholders' meeting or the request that an item be placed on the agenda must be made in writing to the board. If the board does not comply with such request within a reasonable time frame, a judge may order the convention upon request of the relevant shareholders.

Dissident shareholders are not entitled to request the board to circulate their statements among the shareholders. However, shareholders are allowed to make statements and bring forward motions at the general meeting of shareholders. A dissident opinion may be expressed on this occasion within the agenda item concerned.

8 Controlling shareholders' duties

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

The only duty of a shareholder of a Swiss company – whether controlling or non-controlling – is to pay the issue price for the shares. However, significant shareholders may have certain disclosure obligations vis-à-vis the company and, with regard to listed companies, the SIX (see question 36). Any shareholder who directly, indirectly or in concert with other shareholders acquires equity securities representing more than one-third of the voting rights of a listed Swiss company is obliged to make a takeover offer to the remaining shareholders for all listed equity securities of the company. The articles of association of a company may provide for an 'opting up', meaning that a takeover offer must only be made by shareholders owning more than 49 per cent of the voting rights, or an 'opting out', dispensing shareholders to make a takeover offer regardless of the stake held. The disclosure obligations and the obligation to make a takeover offer can be enforced by the TOB and the FINMA.

Any person who acquires bearer shares in a company whose shares are not listed on a stock exchange must give notice of the acquisition within one month. Furthermore, any person who alone or by agreement with third parties acquires shares in a company whose shares – irrespective of whether they are bearer shares or registered shares – are not listed on a stock exchange, and thus reaches or exceeds the threshold of 25 per cent of the share capital or votes must give notice to the company of the first name, the surname and the address of the natural person for whom it is ultimately acting (the beneficial owner) within one month of the acquisition. There is an exemption from these reporting obligations if the indirect owner is a stock-listed company. If the shareholder fails to do so, the membership rights conferred by the shares in respect of which notice of acquisition must be given are suspended and the property rights lapse. If the shareholder gives notice at a later date, they may exercise the property rights arising as from that date. These reporting obligations do not apply if the bearer shares are organised as intermediated securities in accordance with the Swiss Federal Act on Intermediated Securities.

In regard to listed companies, FINMA has recently modified reporting requirements for the discretionary power to exercise the voting rights set out in the FINMA Financial Market Infrastructure Ordinance. In the case of delegated voting rights, the person deciding how voting rights are exercised is now subject to the reporting requirements. Alternatively, the reporting requirements can be met on a consolidated basis by a controlling person for the units controlled by them.

9 Shareholder responsibility

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

Without being (de jure or de facto) an organ of the company, a shareholder does not act for and is independent from the company, and therefore cannot be held responsible for acts or omissions of the company. Only in exceptional abuse-of-right situations, the corporate veil may be pierced and an individual shareholder could be held accountable.

Corporate control

10 Anti-takeover devices

Are anti-takeover devices permitted?

Certain anti-takeover devices, such as transfer restrictions on registered shares (see question 12), limits on the registration of shares in the company's share ledger, the introduction of voting shares (see questions 5 and 12) and the introduction of an increased quorum for specific decisions via a respective provision in the articles of association, are permissible. Different regimes apply to listed and non-listed companies.

11 Issuance of new shares

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

In principle, new shares cannot be issued without approval by an absolute majority of the voting rights of the shareholders represented at the shareholders' meeting. The board must carry out a capital increase resolution within three months. This is an ordinary capital increase.

Based on an amendment of the articles of association, the shareholders' meeting may, however, authorise the board to increase the share capital within a period of up to two years. Such authorised capital may not exceed one-half of the existing share capital. Within these limits, the board may carry out an authorised capital increase.

In addition, by amending the articles of association, the shareholders' meeting may resolve on a contingent capital increase. Creditors of new bonds or similar debt instruments issued by the company, as well as employees, may be granted rights to subscribe to shares to be issued (conversion or option rights).

In principle, each shareholder has a pre-emptive right to acquire new shares in proportion to its actual participation in the company to avoid dilution. Nevertheless, the shareholders' meeting can exclude such pre-emptive rights by qualified quorum of at least two-thirds of the voting rights represented in the shareholders' meeting and an absolute majority of the nominal value of shares for important reasons. In particular, the takeover of companies, equity interests and employee share ownership are deemed to be valid reasons stated by law. However, the cancellation of the pre-emptive rights must not result in any improper advantage or disadvantage to the parties involved.

12 Restrictions on the transfer of fully paid shares

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

There is an important distinction between privately held and listed companies in this respect.

The articles of association of privately held companies may require that registered shares can only be transferred with the company's approval (the board is responsible), which can be denied based on important reasons specified in the articles of association. Alternatively, the company may also offer to the seller that it acquires its registered shares for its own account, the account of other shareholders or for the account of a third party at fair market value. Lastly, the company may refuse the transfer and the registration of the transferee in the company's share ledger if the acquirer does not explicitly state that it has acquired the shares in its own name and on its own account.

A listed company may only refuse to register an acquirer in its share ledger for two reasons: either the acquirer exceeds a certain percentage of the company's voting rights, which has previously been declared in the articles of association of the company, or the acquirer fails to state that it holds the acquired shares in its own name and on its own accounts. However, in both cases, a listed company may only prevent the shareholder from exercising its voting rights in respect to the acquired shares but not the transfer of title of the acquired shares.

13 Compulsory repurchase rules

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

A company is allowed to repurchase shares up to 10 per cent of its nominal share capital (in case the repurchase is made in connection with transfer restrictions, the threshold is 20 per cent of its nominal share capital) provided that the company has sufficient freely available equity (ie, profit, profit carried forward and general reserves) on a voluntary basis. There are no compulsory share repurchase rules under Swiss law.

However, given specific circumstances, the Collective Investment Schemes Act provides for mandatory share repurchases in corporate investment schemes.

14 Dissenters' rights

Do shareholders have appraisal rights?

In general, there are no appraisal rights of shareholders under Swiss law. However, legal entities involved in a merger may provide a compensation payment of fair value to objecting shareholders if an acquirer chooses to squeeze out a minority shareholder.

The responsibilities of the board (supervisory)

15 Board structure

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

The CO provides for a one-tier board model. However, in larger and listed companies, the daily business is (except for the non-delegable and inalienable competencies of the board) often delegated from the board to the executive management, effectively leading a two-tier structure.

16 Board's legal responsibilities

What are the board's primary legal responsibilities?

The board is responsible for managing the business of the company, unless responsibility for such management has been delegated (see question 21). Generally, the board may pass resolutions on all matters that are not explicitly reserved to the shareholders' meeting by law or by the articles of association, or delegated to the executive management based on organisational regulations.

17 Board obligees

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

As the governing body, the board represents the company. It is its duty to act in the company's best interest. In line with the prevailing but not undisputed opinion, the long-term interests of the shareholders as well as those of other stakeholders have to be kept in mind in order to determine what is in the company's best interest.

18 Enforcement action against directors

Can an enforcement action against directors be brought by, or on behalf of, those to whom duties are owed?

The members of the board or persons who, despite not being appointed as directors act as such, and who have significant influence on the company's decision-making process, are jointly and severally liable for damages caused by intentional or negligent breach of their duties. Each member can be held liable with his or her entire assets.

The action may be brought by the company, its shareholders or, in the event of the company's bankruptcy only, by the company's creditors. The shareholders may sue the company directly if they suffered direct damage. If they only suffered indirect damage (eg, a loss of value of their shares resulting from damage incurred by the company) they can only ask that compensation of such loss be paid to the company.

19 Care and prudence

Do the board's duties include a care or prudence element?

The members of the board have duties of care and loyalty towards the company. These duties require the members of the board to act in the same way as a diligent and competent member would have acted in the same circumstances. The compliance with the duties is, hence, assessed by reference to an objective standard, unless a member of the board is an expert in a certain field, in which case the duty of care of such director will be assessed by reference to a diligent and competent director having the same level of expertise in the relevant field.

It is established case law that decisions of the board that are based on adequate information and a reasonable and professional decision-making process do not constitute a breach of duty, even if such decision proves to be wrong retrospectively, provided, however, that board members involved acted in an impartial and independent manner and were free of any conflict of interests when making the decision (the 'business judgement rule'). If a decision meets these standards, members of the board cannot be held liable for an unfavourable decision.

20 Board member duties

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

The duties of the members of the board are defined by objective criteria. As the same duties apply to each individual member of the board, they do not differ based on the skills or experience of the respective member of the board. Therefore, their background, in terms of professional experience, skills, etc, is irrelevant (see question 19).

21 Delegation of board responsibilities

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

The following board responsibilities are non-delegable and inalienable (article 716a of the CO):

- the overall management of the company and the issue of all necessary directives (strategic governance);
- determination of the company's fundamental organisational structure;
- the organisation of the accounting, financial control and finance planning systems as required for the management of the company;
- the appointment and dismissal of persons entrusted with managing and representing the company;
- overall supervision of the persons entrusted with managing the company, in particular, in regard to compliance with the applicable law, articles of association, operational regulations and directives;
- compilation of the annual report, preparation for the general meeting of shareholders and implementation of its resolutions;
- notification of the (bankruptcy) court when the company's liabilities are no longer covered by its assets (over-indebtedness); and
- issuing the annual compensation report on the board's and senior management's compensation and election of the compensation committee consisting of members of the board (only for listed companies according to OaEC).

Apart from the above, the board is allowed to delegate its responsibilities to third parties, individual board members or committees, or the executive management based on the company's organisational regulations.

Even with respect to non-delegable and inalienable responsibilities, the board may delegate the preparation and execution of its decisions, but never the decision-making itself.

22 Non-executive and independent directors

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

There is no requirement by law, regulation or by the listing rules specifying a minimum number of 'non-executive' or 'independent' directors.

Nonetheless, the DCG contains specific disclosure obligations for non-executive members. And the SCBP recommends that the majority of the board should consist of independent members, meaning non-executive members who have either never, or at least not for the past three years, been members of the senior management, and who have no (or comparatively minor) business relations with the company.

23 Board size and composition

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

There is no mandatory provision on the minimum or maximum number of seats on the board. The SCBP recommends that the size of the board should match the needs of the individual company and be composed by members of both genders. However, often companies set minimum or maximum sizes of their boards, or both, in their articles of association.

Potential board members do not have to meet any formal prerequisites with the exception of being a natural person and not a legal entity. In addition, the OaEC obliges listed companies to set a maximum number of permissible mandates a board member may hold in the management or administration of other companies.

In some regulated industries, like the financial markets, it is, however, required that members of the executive bodies have a proper business conduct and the required knowledge and experience ('fit and proper').

Vacancies on the board can only be filled by the appointment of a new member by the shareholders' meeting. Unless otherwise provided in the articles of association, the board may appoint a new chairman for the remaining term of office, if this position becomes vacant.

SIX-listed issuers are required to disclose detailed information on individual board members, the organisation of the board and its committees as well as its compensation. The legal basis for these disclosure obligations is found in the DCG.

Lastly, the identity of any member of the board will be disclosed in the commercial register.

24 Board leadership

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

With the exception of banks and insurance companies, there is no law that requires the separation of the functions of board and senior management (including the board chairman and CEO). The SCPB nonetheless recommends – by emphasising the importance of keeping the balance between direction and control on the senior management level – either separating the two functions or adopting other adequate control mechanisms, such as the appointment of an experienced non-executive lead director.

It is common practice in Switzerland for the CEO not to be a member of the board.

25 Board committees

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

There are no mandatory committees for non-listed companies. For listed companies the OaEC requires the establishment of a compensation committee, whose members have to be elected by the shareholders' meeting each year. For some banking entities, an internal audit committee is mandatory. Otherwise, there are no requirements or restrictions relating to board committees under Swiss law. The SCBP also recommends establishing further committees, such as a nomination committee.

26 Board meetings

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

In order to prepare the annual general meeting (AGM) of shareholders (board resolution on the agenda) at least one board meeting is required per year. However, the SCBP recommends for listed companies that at least four annual meetings should be held, depending on the specific requirements of the company. Moreover, each board member is entitled to individually request the chairman to convene an immediate meeting by stating the reasons for the request.

27 Board practices

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

In general, companies are not required to disclose any board practices. An exception is made for listed companies. The DCG asks companies to disclose a variety of information including their internal organisational structure.

28 Remuneration of directors

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

For non-listed companies, it is in the exclusive competence of the board to determine the remuneration of its members.

Under the OaEC, since 1 January 2014, Swiss companies whose shares are listed on a Swiss or foreign exchange are obliged to annually submit the board's proposal on the compensation of the board members, the senior management and the advisory board to the shareholders' meeting for a binding vote (binding say-on-pay; see question 37).

Contracts between the company and its members of the board or the senior management on which their compensation is based are limited to a maximum term of one year. Loans or other transactions specified in the OaEC between the company and members of the board, the senior management or the advisory board are only admissible if provided for in the company's articles of association.

Further provisions on disclosure regarding the remuneration of members of the board as well as other transactions can be found in the DCG and the SIX 'Directive on disclosure of management transactions' (DMT). The DCG requires all issuers with a primary listing at the SIX, irrespective of whether they are incorporated in Switzerland, to disclose information on the basic principles and elements of compensation and shareholding programmes for members of the board and senior management as well as the method for their determination. The DMT obliges listed issuers to disclose any buy or sell transaction concluded by the directors and members of the senior management in the respective issuer's equity securities or financial instruments.

29 Remuneration of senior management

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

The remuneration of the senior management is determined by the board. There is no regulation in regard to the determination of the executive management's remuneration amounts except for the OaEC (see question 28).

However, the remuneration must be justifiable both in regard to the financial situation of the company and the contribution of the individual manager to the company. This is in line with the established case law of the Swiss Federal Supreme Court in respect of the compensation for members of the board and, furthermore, corresponds with the principle of duty of care and loyalty of board members, which also applies when determining the compensation for the senior management.

The Swiss Supreme Court reviews in accordance with its settled case law remuneration decisions with certain restraint, as such decisions are essentially based on commercial experience and the board is best placed to take such decisions. In the event of an obvious disproportionate remuneration, the judge may impose its refund to the company. Under specific circumstances it may even give space to criminal actions for disloyal management.

30 D&O liability insurance

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

It is generally considered permissible for companies to insure their directors and officers against D&O liability as well as paying the premiums. This is standard practice in nearly all companies in Switzerland.

31 Indemnification of directors and officers

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

There is no explicit rule of law with regard to the indemnification of directors and officers. Moreover, as far as it is apparent, there is also no established case law in this regard. In general, it is seen as admissible (at least as long as no bankruptcy proceedings are commenced) that a company advances cost in connection with lawsuits and official investigations in relation to a claim for compensation of a third party against a director. The company may only envisage reclaiming such advances in case of an evident breach of the director's duty of care. If a director has not breached his or her duty of care intentionally or with gross negligence, is acquitted of the charge or the dispute is settled judicially or extrajudicially, the company may finally bear the cost and indemnify a director for liabilities incurred in their professional capacity. In case of an intentional or gross negligent breach, indemnification seems, in principle, not acceptable.

32 Exculpation of directors and officers

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

The preclusion of liability in advance is not possible neither through charter amendments nor any other shareholder action. But, the shareholders may vote in favour of granting discharge to the directors and officers for the preceding business year at the AGM. By doing so, the company itself and all shareholders voting in favour of the resolution are excluded from bringing forward any action against the directors and officers for facts known at the time of the shareholders' meeting. Shareholders not participating at the shareholders' meeting or voting against the discharge are precluded from taking action at the end of six months following the shareholders' vote on the discharge.

33 Employees

What role do employees play in corporate governance?

Employees do not play a specific role in corporate governance and they are not entitled to be represented on the board.

34 Board and director evaluations

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

There is no such requirement under Swiss Law. There is also no practice in this regard.

Update and trends

The revision of the stock corporation law is still ongoing. A final version of the new stock corporation law is expected for 2020. In the meantime, the Federal Council adopted the related dispatch for Parliament at its meeting on 23 November 2016. The focus of the review is on making the regulations for company foundations and capital more flexible, but also on strengthening shareholder rights. These aspects are set out in detail hereunder.

First of all, the following decisions shall be additionally reserved for the shareholders:

- approval or rejection of the interim management report and the declaration on interim dividends;
- approval or rejection of the reimbursement of the statutory capital reserve; and
- delisting of shares.

Furthermore, the following decisions shall be additionally reserved to the shareholders of listed companies:

- election of the chairman of the board;
- election of the members of the compensation committee;
- election of the independent proxy; and
- approval of the compensation of the board, of the management and of the advisory board (if any).

It is also planned to allow virtual general meetings of shareholders without a physical meeting. Under the current draft of the new stock corporation law and subject to a corresponding provision in the articles of association, the board may decide on the form of the general meeting of shareholders as long as an independent representative is designated to exercise the voting rights. Moreover, resolutions may be taken by written consent to a proposed motion, provided that all shareholders have given their consent to this form of decision-making.

The provisions of the OaEC shall be transferred into the relevant federal statutes. The current draft supplements the requirements of the OaEC in certain respects. In particular, it prohibits joining bonuses (sign-on bonuses or golden hellos) which do not offset any demonstrable financial disadvantage, as well as compensation for non-compete clauses that are not commercially justified. It also limits the level of such payments. Where shareholders vote in advance on variable remuneration for top managers, they must also be presented with the annual compensation report for a subsequent consultative vote. Finally, more effective options for claiming the reimbursement of unlawful payments will also be introduced.

In addition, gender guidelines for the boards and executive managements of major listed companies shall be introduced. The current draft of the new stock corporation law provides that women should account for at least 30 per cent of the board and at least 20 per cent of the executive management. If these targets are not met, the company will be required to state in its remuneration report the reasons and the action that is being taken to improve the situation (the 'comply-or-explain approach'). Adjustment periods of five years for board and 10 years for executive managements will provide sufficient time to seek suitable candidates.

Also, the disclosure rules shall be changed: for example, shareholders as well as creditors with a valid interest might request information on the content of the board regulations. Under the current legislation, these documents do not need to be disclosed.

Disclosure and transparency

35 Corporate charter and by-laws

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

The articles of association along with further information on the company must be filed with the commercial register at the registered office of the company. Via the commercial register, the articles of association can either be accessed directly or ordered online (for further details, see question 36). However, the organisational regulations of the board, in general, do not have to be made publicly accessible. Nonetheless, they are often made available on the websites of listed companies.

36 Company information

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

All companies must prepare an annual report with the annual accounts (of the individual entity and, if applicable, consolidated accounts), composed of the balance sheet, the profit and loss statement and the notes to the accounts. Larger companies additionally have to draw up a cash flow statement and a management report. In general, the annual report must be made available to the companies' shareholders, but not to the public. Only listed companies have to make their annual reports available on their website (see below). Companies also need to register certain fundamental information in the commercial register, the entries of which are available online for public inspection. Such fundamentals comprise:

- the company's purpose;
- its articles of associations (and any changes thereto);
- its share capital (and any increases and decreases);
- its members of the board and any other representatives;
- its auditors (or the fact that it has waived any audit);
- the fact that, if applicable, the transferability of its shares is restricted; and
- its means of publication.

Filings have to be made upon occurrence and are also published in the Swiss Official Gazette of Commerce. For listed companies, the FMIA and the rules and regulations of the SIX, which are based on the FMIA, set out various additional disclosure obligations:

- First, anyone who acquires or disposes of shares (or options relating thereto) of a Swiss company that is listed, at least partly, in Switzerland, or of foreign company mainly listed in Switzerland must notify the company and the stock exchange within four trading days of reaching, exceeding or falling below the thresholds of 3 per cent, 5 per cent, 10 per cent, 15 per cent, 20 per cent, 25 per cent, 33.3 per cent, 50 per cent or 66.6 per cent of the voting rights.
- Second, SIX listing rules sets periodic reporting obligations obliging issuers to publish at least bi-annual financial statements in accordance with the applicable financial reporting standards, as well as to publish and keep updated dates of major importance to investors in a corporate calendar. Issuers are also subject to regular reporting obligations with regard to, inter alia, information concerning the issuer or its capital structure.
- Third, issuers listed on SIX must inform the market of potentially price-sensitive facts (ie, facts that are not publicly known and that (from an ex ante perspective) are capable of leading to a significant price change), which have arisen in the company's sphere of activity (ad hoc publicity).
- Fourth, the DCG obliges its issuers to include a separate corporate governance section in their annual reports on information on management and control at the highest corporate level of their company. The information to be published (or the substantial reasons for their non-publication – the 'comply or explain' principle) comprises information on the company's group and capital structure, its board, senior management and auditors, compensation, shareholdings and loans, shareholders' participation rights, and change of control and defence measures.
- Lastly, members of the board or management committees are required to report within two days to the company transactions in its shares, convertible and purchase rights on its shares, or financial instruments. The issuer must notify the SIX within three trading days of such notifications.

Hot topics

37 Say-on-pay

Do shareholders have an advisory or other vote regarding executive remuneration? How frequently may they vote?

Since the fiscal year beginning in 2015, the OaEC requires the shareholders' meeting of stock-listed companies to vote annually on the aggregate amount for the compensation of each member of the board, the senior management and, if such exists, the advisory board. This vote is binding for the company, which means that every compensation needs to be ratified by the shareholders' meeting. This ratification can, however, be retrospective or prospective. The details of this binding say-on-pay need to be specified in the articles of association. In general, the vote shall cover a one-year period. However, it is admissible to set, as an example, the period for the compensation of the board to its term of office, which is often the year between one AGM and the next. There can also be several votes on different components of the compensation (eg, fixed and variable) and the vote may set an exact amount of compensation or a maximum amount.

Furthermore, some companies have their shareholders vote on a non-binding consultative basis on the compensation report. There is no equivalent obligation for non-listed companies.

38 Shareholder-nominated directors

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

The election and removal of directors is an inalienable power of the shareholders' meeting. In general, individual shareholders neither have the right to nominate directors nor the right to be represented on the board. However, shareholders who alone or together with others hold 10 per cent of the share capital or shares with a nominal value of at least 1 million francs of the company (these conditions may be eased but not tightened in the company's articles of association) may demand from the company (the board is responsible) that an item be placed on the agenda of the shareholders' meeting. Such item can consist of the appointment of a specific person to the board. Such right needs to be exercised before the shareholders' meeting is called, which by law has to be done at least 20 days before the meeting (this deadline may be prolonged but not shortened in the articles of association).

Furthermore, each shareholder (including those holding only one single share) may at the shareholders' meeting raise motions within the agenda items. Accordingly, a shareholder may nominate a director at the meeting under the common agenda item 'appointment of the board'.

In case the company has different share classes, the shareholders of each share class are entitled to appoint at least one representative to the board.

39 Shareholder engagement

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

Each shareholder is entitled to attend the shareholders' meetings, to vote, to request information and to inspect documents (confidentiality interests of the company reserved, for further details see question 7). In particular, the right to information is regularly used by activist shareholders to increase pressure prior to shareholders' meetings. As a first step, it is common for activists to seek personal contact with the company's executive management or board representatives in order to discuss their demands and ideas. If such private negotiations fail, activists often launch public campaigns in order to gather possible support of other shareholders. In such situations, the board is well advised to listen to the shareholders and consider their concerns. The board should closely examine the raised issues and stay in a constructive dialogue with the shareholders. To preserve credibility it is important that the board's engagement is consistent.

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Sources of corporate governance rules and practices

1 Primary sources of law, regulation and practice

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

The Turkish Commercial Code (TCC) dated 13 January 2011 (Law No. 6102) (TCC) entered into force on 1 July 2012. The TCC has important objectives such as ensuring transparency, adopting corporate governance standards and introducing internationally accepted auditing and reporting standards.

In addition to the above, the laws, communiqués and principles governing corporate rules and practice are as follows:

- Law No. 6335 amending the TCC (the Amendment Code);
- the Capital Markets Law (CML) dated 6 December 2012 (Law No. 6362) entered into force on 30 December 2012 replacing the former Capital Markets Law dated 30 July 1981 (Law No. 2499);
- the Capital Markets Communiqués (the CMB Communiqués); and
- the Corporate Governance Communiqué (CGC) dated 3 January 2014, serial II, No. 17.1 and Corporate Governance Principles (CGP) that are listed as annex 1 of the CGC.

According to the CGC, publicly held companies that have shares traded on the stock exchange are subject to the mandatory implementation of certain corporate governance principles; however, there are minor exceptions to mandatory principles (eg, the number of independent board members). As per the CGC, the criteria regarding the number of independent board members shall not be applied to third-group corporations (corporations that are excluded from the first and second groups, the shares of which are traded on National Market, Second National Market and Collective Products Market) and two board members are sufficient for third-group corporations.

There are also some listing requirements that are applied on a 'comply or explain' basis. For example, article 4.2.5 of the CGP stipulates that the responsibilities of the chairman of the board of directors and the chief executive officer or general manager must be explicitly separated; however, if it has been resolved that the roles of chairman of the board of directors and the chief executive officer or general manager are considered the same, this decision (and grounds for this decision) must be disclosed at the Public Disclosure Platform (PDP) (CGP, article 4.2.6).

2 Responsible entities

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

The Ministry of Customs and Trade is the regulatory body responsible for enforcing the TCC's provisions on corporations (article 210 of the TCC). The disputes arising from the TCC are mainly resolved before commercial courts.

The CML, CMB Communiqués and the CGP are enforced by the Capital Markets Board (CMB). The CMB is the regulatory and supervisory authority in charge of the securities markets in Turkey. The CMB is entitled to hand out administrative sanctions to companies or individuals in the event of non-compliance. In the event the conditions set forth under the CML and the relevant legislation occur, the public prosecutor may prepare an indictment upon the written request of the CMB.

As regards the associations whose views are often considered, two associations, namely the Capital Market Investors' Association (BORYAD) and the Turkish Industry and Business Association (TUSIAD), can be mentioned. TUSIAD was established in 1971 to represent the business world and BORYAD was established in 2001 to defend shareholder rights and promote investment.

Proxy advisory firms are expected to appear now that the TCC has come into force, as under the TCC there are legal grounds for them, especially to protect the rights of minority shareholders in public companies.

The rights and equitable treatment of shareholders

3 Shareholder powers

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

According to the TCC, apart from specific exceptions (ie, appointment of the initial board members of companies by the articles of association (AoA)), the shareholders have exclusive authority to appoint or remove board members. As per article 407 of the TCC, shareholders may use this authority during the general assembly (GA). An exception to this rule is that, in the event a board member leaves their post, it is the board's duty to temporarily appoint a new member. However, such temporary appointments must also be approved during the next meeting of the GA by shareholders.

Article 408 of the TCC similarly determines the authority of the GA to appoint and dismiss board members. Accordingly, the GA is authorised to make decisions as set forth under the law and the AoA. The same article also stipulates the non-transferable duties and authorities of the GA. Accordingly, privileges may be granted in respect of the election, nomination, release and dismissal of board members.

Under Turkish law, shareholders holding at least 10 per cent of the share capital of non-public companies and 5 per cent of the capital of public companies are defined as minority shareholders. The minority shareholders may:

- request the board to call an extraordinary meeting of the GA to question the company's management and request that additional items be added to the agenda (TCC, article 411);
- ask the GA to appoint a special auditor to investigate and clarify certain issues even if it is not on the agenda. In order for shareholders to use this option, they must first exhaust their rights of information and examination. If the GA accepts this request, minority shareholders can request the commercial court to appoint a special auditor (TCC, article 438). This is applicable not only for minority shareholders, but for all;
- request the board to issue registered share certificates. If made, such request of the minority shareholders must be accepted and

registered share certificates must be delivered to owners (TCC, article 486); and
- request the company to be dissolved, if there is a 'just cause' in that regard. The TCC does not define what a just cause would be, but it is accepted among scholars that there would be a just cause to request the dissolution of the company if the GA was called to numerous meetings contrary to the law, if the rights of minority shareholders are violated, especially the right to examine and demand information, if the company constantly loses its assets and does not generate any profit etc (TCC, article 531).

Further, all shareholders are entitled to request information and examination. Pursuant to article 1.2.1 of the CGP, which is applicable to public companies, this right cannot be limited or cancelled by the AoA or by a decision of the company.

In addition, any shareholder has the right to ask the GA to file a lawsuit for damages against board members or auditors (TCC, articles 553 to 555), request to inspect the company's books and records and request information from the company's auditor. Shareholders may also request from courts, if there is a just cause, that the managers' right to manage the company be limited or completely abolished (TCC, article 630).

As per article 620 of the TCC, the shareholder vote required to elect and dismiss directors is the simple majority of the votes represented in the GA meeting, unless provided otherwise by law or the AoA. The necessary quorum for the GA meeting is shareholders or their representatives corresponding to at least one-quarter of the capital. If this quorum cannot be reached in the first meeting, no quorum is sought for the second meeting (TCC, article 418).

4 Shareholder decisions

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

According to article 408 of the TCC, the GA has exclusive authority over:
- amending the AoA;
- releasing the auditors and the board of directors or holding them liable;
- appointing the members of the board of directors, determining their fees, term of duties, discharging and replacing them;
- appointing and discharging the auditor except for the cases set forth under the law;
- taking decisions regarding the financial statements, the annual report of the board of directors, savings on the annual profit, determination of the dividend and gain margin and including the injection of the reserve fund into the capital or into the profit to be distributed and deciding on the use of the reserve fund;
- deciding on the dissolution of the company except for the cases set forth under the law; and
- sale of a substantial part of the company.

In the event the conditions stated under the CML and the related legislation are met, some exclusive powers of the GA may be transferred to the board of directors. For example, if a company chooses the registered capital system, the share capital of the company can be increased upon the board of directors' resolution. Also, when it is permitted by the AoA, the board of directors may restrict the pre-emptive rights of shareholders (CML, article 18/5).

Under Turkish law, there are no matters that are resolved by a non-binding shareholder vote.

5 Disproportionate voting rights

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

As regards disproportionate voting rights, it should be noted that the TCC adopts the 'one share, one vote' principle. Accordingly, each share grants at least one voting right (TCC, article 434).

Pursuant to article 479 of the TCC, disproportionate voting rights may be granted to privileged shares. However, the voting privileges for private companies are limited to a maximum of 15 votes per share. This number can be increased only by a court decision for the sake of institutionalisation or because of a just cause. Thus, under the TCC regime, it is no longer possible to block a capital increase through the use of privileged shares. Further, privileged votes do not extend to resolutions regarding the amendment of the AoA of a company, or filing of discharge or liability suits.

6 Shareholders' meetings and voting

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

Article 1.3.1 of the CGP stipulates that the announcement regarding GA meetings should be made at least three weeks in advance of the meeting on the company's corporate website and on the PDP.

According to the TCC, shareholders are invited to the meeting as stipulated under the AoA, through an announcement published on the company's website (if the company is required to have a website) and in the Turkish Trade Registry Gazette. This announcement must be made two weeks before the GA meeting (TCC, article 414).

Article 415 of the TCC stipulates the shareholders who are entitled to attend meetings. Accordingly, shareholders whose names are written in the attendance list prepared by the board of directors have the right to attend the meeting.

Pursuant to article 437 of the TCC, regulating the right to examine and demand information, financial statements, consolidated financial tables, annual reports of the board, audit reports and suggestions of the board regarding the method of distribution of dividends shall be made available to the shareholders at least 15 days before the meeting.

Pursuant to the TCC, e-signatures can be used to prepare meeting documentation and meetings can be held electronically (TCC, article 1527).

The following requirements have to be met in order to vote online:
- the company must have a website allocated for this purpose;
- shareholders who wish to participate in the online GA meeting must make such a request in advance;
- a technical report must be produced to prove that the electronic platform tools are sufficient for efficient participation and this report should be registered and published; and
- the identities of the online voters must be kept confidential.

The Ministry of Customs and Trade issued the Regulation on General Assembly Meetings of Joint Stock Companies held electronically, regarding the procedures of online GA meetings, published in Official Gazette No. 28481 of 28 November 2012. The companies shall have integrated in their AoA the sample article stating that the meetings can be held electronically. The said article can be found in the Regulation published by the Ministry of Customs and Trade. The company shall integrate the article as is since it is not possible to amend the article while adopting it.

Electronic meetings are mandatory for publicly listed companies.

The shareholders acting by written consent without a meeting can be realised by meetings that are held electronically, as explained above.

7 Shareholders and the board

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

Article 411 of the TCC stipulates that shareholders holding at least 10 per cent of the company's capital and for public companies, shareholders holding at least 5 per cent of the company's capital may request a general meeting of the board. If such a meeting has already been convened, then they have the right to request certain topics to be included on the agenda including director nominations. If their request is not accepted by the board or not responded to within seven days, such shareholders have the right to apply to the commercial court to enforce their request.

According to article 446 of the TCC, the dissenting opinions of the shareholders must be recorded in the minutes of the GA meeting to grant shareholders a right to claim invalidity of such decisions.

8 Controlling shareholders' duties

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

Under Turkish law, controlling shareholders do not have any specific duties to the company or to non-controlling shareholders. However, it should be noted that all controlling shareholders must exercise their rights by complying with good faith principles. Further, there are special provisions for minority shareholders.

Additionally, the TCC regulates provisions with regard to group companies and article 202 of the TCC specifically stipulates that the dominant (controlling) company cannot exercise its dominance in a way that may give rise to a financial loss on the subsidiary (eg, instruct the subsidiary to be the guarantor of a loan), unless such loss is compensated within the same financial year or a right to claim compensation is granted to the subsidiary within the same financial year by providing details on when and how the loss will be compensated. The loss concept herein covers causing a potential risk to the company's financial assets or future profitability as well as value depreciation on them. Therefore, not only the actual losses sustained but also potential risks that may arise thereof fall within the definition of loss.

Both the shareholders of the subsidiaries and the creditors of the same may claim the indemnification of the loss of the subsidiary company from the dominant company by filing a lawsuit.

9 Shareholder responsibility

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

According to the TCC, the shareholders' only liability against the company is their subscribed capital contribution. There is an exception to this rule in the case of tax and public debts of the company.

If the company does not pay tax or public debts, the shareholders will be liable. Other than this, the shareholders are not responsible for the acts or omissions of the company, unless such an act or omission results from the shareholders' own acts and has criminal elements.

Corporate control

10 Anti-takeover devices

Are anti-takeover devices permitted?

At present, share transfer restrictions are not permitted except for legal grounds determined under the TCC. However, the TCC introduces specific provisions regarding the restriction of share transfers through the AoA separately for limited liability companies (LLCs) and joint-stock companies (JSCs). Article 492 of the TCC requires JSCs to include in their AoA the specific reasons why share transfers may be rejected. Reasons related to the nature of the shareholders' composition or the scope of the company's activities or the economic independency of the company are deemed as important grounds for rejection as per the TCC. This is not an exhaustive list, therefore shareholders will need to select and predetermine the grounds for share transfer rejections and be very specific about it, if they want this protection to be reflected in the AoA. Otherwise, limitations on share transfer will continue as a contractual obligation pursuant to the shareholders' agreement.

Article 493/1 of the TCC provides an escape clause for JSCs through the option to reject a share transfer, without basing its decision on the grounds explained above, by offering to acquire, at real value, the transfer shares itself or on behalf of its shareholders or a third party.

For shareholders to resolve on the transfer restrictions of registered shares, an affirmative vote of 75 per cent of the shareholders or their representatives is required (TCC, article 421/3).

In contrast to the JSCs, the TCC explicitly allows LLCs to limit share transfers based on pre-emptive purchase rights, call options or other ancillary or additional obligations by so providing for them in their AoA. Such limitations may also be subsequently included into the AoA by a decision of the GA. In this regard, the positive vote of two-thirds of the GA is required (TCC, article 621).

Share transfers are subject to the approval of the GA and may be rejected without a just reason, unless otherwise stipulated in the AoA (TCC, article 577).

Given the differences between LLCs and JSCs, investors aiming to reflect the provisions of the shareholders' agreement to the AoA may prefer to incorporate an LLC, provided that the regulations in their field of activity allow this.

Any agreement between the JSC and a third party for the acquisition by that third party of the JSC's shares in lieu of the JSC itself or its affiliate or the parent company must comply with the terms set forth under articles 379 and 380 of the TCC. An agreement or obligation to this effect in violation of the terms of article 379 of the TCC will be invalid.

The TCC bans a JSC, a third party or the JSC's subsidiary acting for the JSC, or the JSC's subsidiary promising shares in its parent company, from undertaking to sell treasury shares (TCC, article 380/2).

11 Issuance of new shares

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

Under the TCC, new shares are issued upon capital increases and this requires a shareholders' resolution. In public JSCs that adopt a registered capital system, capital can be increased without the approval of the shareholders, thus new shares can be issued accordingly, within the registered share capital (TCC, articles 459 and 460). In addition, according to article 461 of the TCC, existing shareholders have pre-emptive rights to acquire newly issued shares in proportion to their shareholding. Pre-emptive rights of shareholders may be restricted by a decision of the GA meeting, in the presence of just causes and with the positive vote of shareholders representing at least 60 per cent of the capital (TCC, article 461).

The TCC has introduced two new systems regarding capital. First, there is the new registered capital system for private JSCs, which was previously available only for public companies. A private JSC can adopt the registered share capital system by a provision to this effect in its AoA. The AoA must indicate the aggregate ceiling of the capital and the time limit for the board of directors' authority to increase capital within that set limit, which cannot be longer than five years. The company may then increase its capital without going through the burdensome procedures of holding a GA meeting up to a predetermined ceiling (TCC, articles 459 and 460). The minimum capital requirement for a JSC adopting the registered capital system is 100,000 Turkish liras (TCC, article 332).

Second, as a financing method for JSCs, the TCC brings a conditional capital increase system, through which the company's creditors (such as holders of bonds or other debt securities) and employees may partake in its equity. The conditional capital increase is not triggered by new capital commitments of the shareholders, but through the exercise of exchange (conversion option) and pre-emptive rights by creditors and employees (TCC, article 463).

12 Restrictions on the transfer of fully paid shares

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

The CMB prohibits the restrictions on the transferability of shares of a public company. Accordingly, the transfer of the shares must not be limited and other restrictions must not be imposed on the shareholders to prevent them from going public.

Further, pursuant to article 8(ç) of the Quotation Directive issued by Borsa Istanbul, a company is prohibited from including any share transfer restrictions in its AoA regarding the securities to be listed on Borsa Istanbul.

Article 490 of the TCC stipulates that fully paid, registered shares can be transferred without any restriction, unless otherwise provided by law or by the AoA. The transfers of bearer shares are subject to the transfer of possession.

13 Compulsory repurchase rules

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

A share buyback system that was already available for listed companies under capital markets legislation has been introduced by the TCC for

JSCs, in exceptional cases. The conditions for the buyback are as follows (TCC, article 379):

- authorisation of the board of directors by a GA meeting;
- acquisition and pledge may be accepted on condition that the shares it will acquire in the future and the shares held by its subsidiary companies do not exceed 10 per cent of the company's authorised or issued capital;
- the GA meeting can only delegate such authority for a maximum period of five years;
- the board of directors is required to state in the authorisation that these legal requirements have been fulfilled;
- the nominal value of the shares that will be accepted as an acquisition or pledge by the authority must be stated;
- the minimum and maximum limits of the consideration that will be paid for the shares must also be stated; and
- acquired shares must be fully paid-up. Shares so issued are stripped of any voting rights.

Further, article 385 of the TCC stipulates that shares acquired or accepted as a pledge in a way that is contrary to the principles set forth under the TCC shall be disposed of, or the pledge on them shall be released within six months from the date of their acquisition or acceptance as a pledge. Any specific procedure regarding selling off or disposing of the pledge has not been provided. The authority to sell off such shares is held by the board of directors, which shall perform its duty according to the principles of equality and public disclosure.

Similar principles apply to share buybacks in LLCs as well. An LLC may acquire its own capital shares with two conditions (TCC, article 612): it must have the necessary equity that may be freely used to purchase these shares; and the nominal value of the shares to be purchased must not exceed 10 per cent of the total share capital.

Capital shares acquired in excess of this amount must be disposed of or redeemed through a capital reduction within a maximum period of two years (TCC, article 612/2).

The Communiqué on Share Repurchase (the Communiqué) issued by the CMB entered into force on 3 January 2014. According to the Communiqué, the board of directors must be authorised by the GA in order for a publicly held company to repurchase its own shares (Communiqué, article 5/1). There is an exception to this rule where listed companies are allowed to repurchase the shares without the necessity of a GA authorisation, if such repurchase is necessary for the purpose of avoiding a probable and serious loss. A probable and serious loss is deemed to exist where the daily average price of shares is below the nominal value or has lost value over 20 per cent. Unless such circumstances are present, the only way for a listed company to repurchase its shares without a GA authorisation is to obtain the approval of the CMB (Communiqué, subparagraphs 4 and 5 of article 5).

The nominal value of the repurchased shares cannot exceed 10 per cent of the paid-in capital where the total value of the shares cannot exceed the total value of the resources subject to profit distribution. Repurchased shares may be kept for an indefinite period as long as they do not exceed the aforementioned limits. The shares repurchased in breach of the Communiqué must be sold within one year from the date of repurchase or else they will be amortised by way of capital decrease (Communiqué, article 19).

The maximum duration of the repurchase programme is three years for the companies listed on the stock exchange and one year for other publicly held companies, unless the repurchase programme does not foresee any specific duration (Communiqué, article 7).

The repurchase of shares is not permitted if there is any postponed disclosure process regarding internal matters or significant transaction that has not yet been disclosed to the public.

14 Dissenters' rights

Do shareholders have appraisal rights?

The TCC also provides categories of important reasons that allow JSCs to reject the transfer of registered shares under their respective AoAs. The company may choose not to approve the share transfer by claiming an important reason stated under the AoA, or to acquire the shares to be transferred on its or a shareholders' or any third party's behalf by offering nominal value of the shares to the transferee (TCC, article 493).

If the company prefers to use an escape clause, the nominal value of the shares must be offered to the transferee. There is no definite basis for how the nominal value of shares will be determined and the transferor may apply to court for a determination of the nominal value of the shares to be transferred. If the transferee is offered a nominal value and does not reject such value within one month of its acknowledgment, the acquisition offer will be deemed accepted. If the company remains silent for a period of three months from the date of the transferee's application for approval, it will be deemed that the company has approved the share transfer. As long as the company does not approve the share transfer, the ownership of shares will remain with the transferor together with all monetary and management rights (TCC, articles 493 and 494).

In addition, the TCC regulates an escape fund to be paid to shareholders in the event of a merger or change in the type of company. In this regard, if the shareholders disagree with a merger or change in the type of company, they have the right to sell their shares to the company at a fair value (TCC, articles 141, 183 and 202/2).

Moreover, the Communiqué on Common Principles of Significant Transactions and Retirement Rights issued on 24 December 2013 determines the extent of significant transactions and shapes the limits of voting rights and shareholders' retirement rights in publicly held companies. According to this communiqué, mergers, division transactions, change in the type of company or termination, along with other important transactions listed in article 5, require GA approval.

This communiqué details the provision regarding the retirement right in article 24 of the CML and determines the circumstances where the retirement right does not arise. In this respect, shareholders who voted against a significant transaction at the GA meeting and had their dissenting vote recorded in the minutes of that meeting will be able to sell their shares to the subject company.

According to this communiqué, it may be possible to abandon significant transactions where the total cost of the exercise of retirement rights exceeds the predetermined cost of the same or where certain shareholders, whose qualifications are specified beforehand, exercise the retirement right. Similar provisions are recognised for mandatory tender offers arising from a significant transaction. With an amendment dated February 2015, pursuant to article 11/1, in order to protect the rights and interests of investors, it has been provided that in case of a non-public company acquiring a publicly listed company, the controlling shareholders together with those acting with the controlling shareholders shall make a mandatory tender offer.

The responsibilities of the board (supervisory)

15 Board structure

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

Under Turkish law, the board structure for both listed and unlisted companies is one-tier.

16 Board's legal responsibilities

What are the board's primary legal responsibilities?

The principal duties of the board members are as follows:

- to act prudently and diligently when conducting business and performing their duties and the business of the company;
- to monitor and supervise the management and the business of the company to ensure that it is in compliance with principles of good faith, and for the interests of the company and its shareholders;
- to keep confidential the information obtained during and after the term of duty;
- to refrain from attending board meetings regarding their own interests or the interests of certain close relatives; and
- not to engage in transactions with the company unless the GA meeting authorises the board for a maximum period of five years regarding the repurchase of shares.

In addition to the above the TCC sets forth the non-transferable duties of board members. The most important non-delegable and indispensable duties and powers of the board of directors are as follows (TCC, article 375):

- determining top-level management of the company and giving instructions in this regard;
- establishing the necessary system for financial planning to the extent required, and for accounting and finance audit;
- appointing and dismissal of managers and persons performing the same function and authorised signatories;
- high-level supervision of whether the persons in charge of management act in accordance with the law, the AoA, internal regulations and written instructions of the board;
- keeping the share book, resolution book of the board and the GA meeting and discussion register, preparation of the annual report and corporate governance disclosure and submission thereof to the GA, organisation of GA meetings, and enforcement of GA resolutions; and
- notifying the court regarding the company's state of excess of liabilities over assets.

It must be noted that neither of these duties and authorities of the board of directors can be delegated to a duly authorised representative, the company management, a committee or the managers (TCC, article 367). The GA meeting cannot seize or deprive these duties and authorities of the board of directors, or transfer them to the GA meeting or the committees established under the provisions of the AoA. Similarly, the board of directors cannot waive such duties and authorities.

17 Board obligees

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

The board is responsible for the management and representation of the company (TCC, article 365). Pursuant to article 553 of the TCC, in the event that the board is liable due to their own faults arising from the law and the AoA, then the board will owe legal duties to the company, to the shareholders and to the company's creditors.

18 Enforcement action against directors

Can an enforcement action against directors be brought by, or on behalf of, those to whom duties are owed?

According to the TCC, the company, its shareholders and its creditors are entitled to file indemnification actions against the board members to indemnify the damages that occurred owing to their faults. Shareholders may initiate actions against the directors and request the indemnification of the damages that they directly incurred or request indemnification on behalf of the company for the damages that the company has incurred (TCC, article 553).

A voluntary insurance system for the damage incurred by the company through the fault of board members while performing their duties has been introduced by the TCC.

If the damage is insured at a price exceeding 25 per cent of the company capital and the company is secured, in the case of public companies, this matter shall be announced in the bulletin of the CMB, and if the shares are listed on a stock exchange this shall also be announced in the stock exchange bulletin, and such matter shall be taken into account in the assessment of compliance with the principles of corporate governance (TCC, article 361).

With regard to the civil and criminal liabilities of board members, unlike the previous TCC, the new TCC specifically regulates (in a separate article) the civil and criminal liabilities (TCC, article 553 and 562). If the board members do not comply with the obligations set forth under the law or under the AoA, they will be subject to civil and criminal liability.

19 Care and prudence

Do the board's duties include a care or prudence element?

According to the TCC, members of the board of directors and third parties in charge of management are under an obligation to act with care and in compliance with the rules of good faith (TCC, article 369).

20 Board member duties

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

According to the TCC, it is possible for a legal person to become a member of the board of directors (TCC, article 359/2).

The TCC requires that a chairman and at least one vice chairman be appointed among the board members (TCC, article 366). It should be noted that the board members do not have any special duty that should be performed individually except calling for board meetings. Also, under Turkish law, the board members do not have specific duties individually assigned to them. However, by inserting a relevant provision to the AoA or regulating an internal regulation, the board can always assign different duties to its members. Therefore, each board member can be held to be authorised and liable for different business transactions and may have different specific duties in that regard. If there is such distribution of duties, the duties and authorities of individual board members shall be disclosed in the activity report of the company (CGP, article 4.2.2). In the event the duties are not assigned, the management is performed by all board members (TCC, article 367).

21 Delegation of board responsibilities

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

According to the TCC, the board of directors can transfer all of the management rights of the company to one or more executive members or to a third party as the manager. However, at least one of the board members must be entitled to represent the company (TCC, article 370). In such an instance, the transferee party would have the same responsibilities that the board of directors had pre-transfer.

The CGP stipulates that if there is a delegation of authority among board members, it should be specifically disclosed under the activity report of the company (CGP, article 4.2.2).

An addition has been made to article 371 of the TCC, relating to the representative authority of companies, by the Omnibus Law No. 6552 adopted on 10 September 2014. Pursuant to the mentioned addition, the board of directors may appoint non-representative members of the board of directors or persons bound to the company by a labour contract, as commercial representatives with limited authority or as other commercial assistants. This act of the board of directors and the powers and duties of the appointed persons shall be explicitly reflected in the internal directive issued in accordance with article 367 and such internal directive shall be registered and announced. This amendment has enabled companies to impose different kinds of limitations or categorisations for their representative authorities that could not be done by a signatory circular.

22 Non-executive and independent directors

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

Non-executive and independent membership structures are regulated mainly under the CGP and in certain CMB communiqués. Pursuant to the CGP, the majority of the board members should consist of non-executive members (CGP, article 4.3.2) and some of these members should be independent board members (CGP, article 4.3.3). Since all members of the audit committee are independent board members (CGP, article 4.5.3), the audit committee comprises only non-executive members.

Additionally, the TCC also regulates the non-executive board members. Accordingly, members of the board may solely have non-executive powers provided that it is explicitly stated in the internal guidelines.

According to the CGP, the board must include the following:

- the majority of the board must consist of non-executive members;

- the total number of independent members shall not be less than one-third of the total number of members;
- in any case the number of independent members cannot be less than two; and
- a person who has been acting as a board member for more than six years within the past 10 years cannot be appointed as an independent board member (CGP, article 4.3).

Pursuant to the CGP, an individual not having any administrative duties within the company is defined as a non-executive member.

As per the definition of the independent member, the CGP sets forth specific requirements to be met by independent members (CGP, article 4.3.6).

Under Turkish law, non-executive or independent directors do not have different duties from the executive directors. It should be noted that, as a general principle, all members of the board are jointly and severally liable to the company, the shareholders and the creditors of the company for damage occurring due to their fault and owing to the non-fulfilment of the duties stated in the law or the AoA (TCC, article 553).

23 Board size and composition

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

The TCC allows the board of directors to consist of just one member (real person or legal entity) assigned by the AoA or elected by the GA and the requirement that a member of the board of directors has to be a shareholder in the company has been abolished. In the event that a legal entity is elected as a member of the board of directors, a real person should be determined by the legal entity on its behalf and such a decision needs to be registered and announced with the trade registry (TCC, article 359).

Both in the TCC and the CML, there is no ceiling stipulated for the size of the board of directors. For listed companies, it is stated that the number of members of the board of directors – provided that the number is not less than five in any case – shall be determined in order to ensure that the board members conduct productive and constructive activities, make rapid and rational decisions and efficiently organise the formation and activities of the committees (CGP, article 4.3.1). Regarding female members on the board, the company shall determine a target percentage no less than 25 per cent and a target time, and shall establish a strategy to reach these targets (CGP, article 4.3.9).

In LLCs, the management and representation of the company may be left to a shareholder or non-shareholder that has been elected as the manager. However, at least one of the shareholders must possess the right to management and representation of the company in the widest manner. If there is more than one manager of the company, one of these managers must be elected as the chairman of the management board by the GA.

Article 363 of the TCC stipulates that in the case of a vacancy on the board, the board of directors shall temporarily choose someone who satisfies the legal conditions and presents it for the approval of the GA. The member chosen this way carries out their duties until the GA meeting and, if he or she is approved, he or she continues working until the end of the mandate of their predecessor.

In listed companies, if there is a vacancy on the board and it is not possible to satisfy the board meeting quorum, or it is not possible for the shareholders to convene a meeting to appoint a new board member within 30 days of the vacancy, the CMB is entitled to appoint an independent board member (CML, article 128/1(k)).

24 Board leadership

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

Under Turkish law, it is possible for the same board member to hold both the titles of chairman and CEO. According to the CGP, the duties and authorities of the CEO and the chairman of the board must be specifically distinguished from each other and stipulated under the AoA. In addition, if it is decided that the CEO and the chairman of the board are one person instead of two separate persons, then this should be published on the PDP with its reasons (CGP, articles 4.2.5 and 4.2.6).

25 Board committees

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

According to article 25 of CMB Communiqué, serial X No. 22 regarding the standards of independent audit in capital markets (as updated with the Communiqué serial X No. 28, published on the Official Gazette on 28 June 2013), it is required that, within the framework of the CGP, the board appoints an audit committee constituting a minimum of two members of the board. In enterprises where it is not obligatory to establish an audit committee, the duties of the audit committee are fulfilled by the board of directors.

According to the CGP, an audit committee, a corporate governance committee, an early detection of risk committee, a nomination committee and a price committee must be formed. Regarding banks, only a corporate governance committee shall be formed. If the nomination committee and price committee cannot be formed, then the corporate governance committee will supersede the duties of such committees (CGP, article 4.5.1). Pursuant to the TCC, listed companies are under the obligation to constitute a committee that will be in charge of detecting and managing the risks in advance. In the event the auditor of the company deems it necessary, such a committee must also be formed by companies other than the listed ones. The committee submits an evaluation report to the board every two months and informs the board of the problems and solutions. The report shall also be sent to the auditor (TCC, article 378).

26 Board meetings

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

Frequency of board meetings is regulated under article 390 of the TCC. Accordingly, the law does not require a minimum number of board meetings per year. Therefore, in practice, the board convenes a meeting when it is deemed necessary, unless the AoA requires a minimum number of board meetings. The CGP states that the board of directors convenes the meeting on a regular basis in order to fulfil their duties effectively (CGP, article 4.4.1).

27 Board practices

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

The structure, members of the board, their term of office and remuneration of the members are determined in GA meetings and the minutes of GA meetings are registered with the relevant trade registry and published in the Turkish Trade Registry Gazette.

In addition to the TCC, capital stock companies subject to auditing will be required to set up and maintain a company website within three months following the incorporation of the company, and must allocate part of the website to the announcements legally required to be made (TCC, article 1524) (see question 36).

28 Remuneration of directors

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

Remuneration

According to the TCC, provided that the amount is determined by the AoA or the GA resolution, directors can be paid a remuneration (TCC, article 394).

The CGP stipulates that the remuneration of independent board members cannot be determined by taking into account the profit share, share options or the company's performance-related payment schedules (CGP, article 4.6.3). Pursuant to the same principle, the remuneration to be paid to independent board members shall be satisfactory so as to protect their independence. The remuneration to be paid to board members and all managers having administrative responsibilities shall be made available to the public in the annual activity report (CGP, article 4.6.5).

Length

There is no requirement as to the length of the service contract of the board members under the TCC. According to the TCC, board members can be appointed for a maximum term of three years and unless otherwise specified in the AoA of the companies, board members may be re-elected (TCC, article 362). The CGP also sets forth that the term for independent members is three years and that they may be re-elected (CGP, article 4.3.5).

Transactions between company and board members

In strengthening the arm's-length principle, the TCC prohibits a JSC from financing its shareholders and directors, aiming to preserve the company assets and protect the creditors of the JSCs. In this regard, a board member cannot conduct any transaction with the company in his or her or any other person's name without permission from the GA, otherwise the company can claim that the transaction is null and void. The counterparty cannot make such a claim (TCC, article 395).

In addition, in the case of a board member who is not a shareholder, his or her relatives including spouses, descendants, lineal ancestors and relatives by blood or marriage to (and including) the third degree, cannot be indebted in cash to the company. The prohibition provided for board members includes guarantees as well. In other words, the company cannot provide surety, guarantee or security for the persons listed above, undertake their liability or take over their debts. Otherwise, the creditors of the company are entitled to start execution proceedings directly against these people for the debt of the company in the amount for which the company is liable (TCC, articles 393 and 395).

If the related-party transaction principle is violated, a judicial fine will be imposed on the shareholder or board members (TCC, article 562).

Also, shareholders cannot become indebted to the company unless the debt arises from their due capital commitments and the company's profit, together with the legal reserves, do not meet the company's losses for the previous years (TCC, article 358). In LLCs, the same principles apply only for partners of the company (TCC, article 644).

In addition, according to article 1.3.6 of the CGP, majority shareholders, members of the board, managers having administrative responsibilities and their relatives (spouse, direct offspring or relatives up to the second degree by blood or by marriage) are obliged to provide information in the GA about the transactions that may be conflicting with the interests of the company or its affiliates. Also, according to article 1.3.10 of the previous CGP, the approval of the GA meeting was required for significant transactions, namely transferring or renting out all or a significant portion of company assets, establishing rights in rem on all or significant amounts of company assets, granting concessions to third parties or changing the scope and subject of already provided concessions, acquiring or renting significant amount of assets and delisting from Borsa Istanbul. Unless the decision of a GA meeting is not required by the relevant board for the execution of such a transaction, affirmative votes from the majority of independent directors are required. If this is not achieved, the transaction will be submitted to the approval of the GA meeting. In such a case, the reasoning of the independent directors will be disclosed to the public, notified to the CMB and explained to the shareholders in the next general meeting. Article 1.3.9 of the current CGP provides the same rule, by elaborating the definition of 'significant transactions'. Accordingly, when the ratio between the value of the purchase or sale of assets and services, as well as the transfer of obligations and similar transactions, and the value of the company exceeds 10 per cent, the mechanism described above has to be implemented.

If the above transactions fall under the category of related-party transactions, those parties shall not vote in the relevant GA meeting. Accordingly, there is no minimum meeting quorum requirement for the approval of the above transactions (CML, article 29/6).

Also, as per article 21(1) of the CML, in the case of transactions with another enterprise or individual with whom there is a direct or indirect management, administrative, supervisory, or ownership relationship, publicly held joint-stock corporations, collective investment undertakings and their subsidiaries shall not damage their profits or assets by engaging in deceitful transactions by applying a price, fee or value clearly inconsistent with similar transactions with unrelated third parties, market practices or principles of commercial prudence and honesty.

Compensatory arrangements between the company and board members

As mentioned above, under the TCC, the board members are under an obligation to act with care and in compliance with the rules of good faith (TCC, article 369). If they fail to do so and the company incurs damages as a result, shareholders and creditors of the company may initiate actions against the board members and request indemnification (TCC, article 553). In this context, there is no regulation regarding compensatory arrangements between the company and board members, but it is possible to lay down a clause in the agreement between the company and the board member stipulating how such damages shall be compensated. Accordingly, damages that were incurred due to the fault of board members can be compensated by the relevant board members.

29 Remuneration of senior management

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

According to the TCC, the board shall review the remuneration of the key executives and include the information in the activity report of the board of directors. However, there is no regulation that affects the remuneration of senior managers (TCC, article 516/2).

According to the CGP, remuneration of the senior management must be prepared in a written form and submitted for the approval of the shareholders. The remuneration paid to the board members and the key executives who have administrative duties and all other benefits to be provided to them are disclosed to the public through the activity reports. It is essential to disclose the remuneration for each of them. In the event specific disclosure is not made, at the very least a separation must be made between the key executives and board members. The remuneration policies of the company must be published on the company's website (CGP, article 4.6.2). There is no regulation regarding compensatory arrangements between the company and senior managers. However, similarly to the board members, the managers are under an obligation to act with care, and according to article 553 of the TCC, they can be held liable if they fail to do so. In this context, it is possible to lay down a clause in the agreement between the company and the manager stipulating that the damages incurred due to the fault of the manager shall be compensated by the relevant manager.

30 D&O liability insurance

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

A voluntary insurance system for the damage incurred by the company through the fault of board members while performing their duties has been introduced by the TCC. If the damage is insured at a price exceeding 25 per cent of the company capital and the company is secured, in the case of public companies, this matter shall be announced in the bulletin of the CMB, and if the shares are listed on a stock exchange this shall also be announced in the stock exchange bulletin, and such matter shall be taken into account in the assessment of compliance with the principles of corporate governance (TCC, article 361). The CGP stipulates this point as a requirement (ie, states that the damage shall be insured at a price exceeding 25 per cent of the company capital and this shall be announced in the bulletin of the CMB) (CGP, article 4.2.8).

31 Indemnification of directors and officers

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

There is no regulation preventing a company from indemnifying a director or officer against liabilities, but it should be noted that such indemnification claims are not common and have not been tested in the courts.

32 Exculpation of directors and officers

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

As stated in question 21, the liabilities of board members can be restricted by delegating his or her duties to other board members or managers. Such limitation can be realised through issuing an internal directive in accordance with article 367 of the TCC, and such internal directive shall be registered and announced with the trade registry. However, the board members have a continuing duty to observe the acts and actions of the third parties to whom liabilities are delegated. The restriction on authority of representation is not effective against third parties in good faith; however, the restrictions that are registered and announced in relation to limiting authority of representation solely to the business of the headquarters or to the exercising thereof jointly are valid. In addition, they still have the duty to prudently and diligently delegate the responsibilities to persons who are qualified enough and supervise them (TCC, article 371).

As per the addition to article 371 of the TCC, explained under question 21, limiting the liability of the board members or managers is only effective in the company and does not relieve them from responsibility against third persons. In this regard, the board of directors shall be liable jointly and severally towards the company or third persons for any damages caused by the commercial representatives with limited authority or other commercial assistants appointed pursuant to an internal directive.

33 Employees

What role do employees play in corporate governance?

According to the TCC, employees do not have a specific duty in terms of corporate governance. However, under the CGP, employees are also listed as stakeholders and companies must ensure that the rights and benefits of the stakeholders are protected (CGP, article 3.1.1).

34 Board and director evaluations

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

In listed companies, the board of directors shall issue its annual report in a detailed way that should include, among other things:

- information on the duties of the members of the board of directors and executives conducted out of the company and declarations on independence of the members of board of directors;
- information on the members of the committees formed within the structure of the board of directors, the meeting frequency of these committees, the evaluation of the board of directors regarding the working principles including the conducted activities and the efficiency of the committees; and
- number of meetings of the board of directors in a year and attendance of the members of board of directors to these meetings.

The annual report shall be published so that the public can access the complete and accurate information with respect to the activities of the corporation. Additionally, the nomination committee that is mandatory in listed companies regularly evaluates the structure and productivity of the board of directors and submits its advice regarding possible amendments in this respect to the board of directors.

In non-listed companies, a similar annual activity report is also annually prepared by the board including information on management, activities of the company and related important developments, financial status, risk assessment, etc, and submitted to the GA meeting.

The shareholders discuss the activities of the board and decide on the release of the board members' liabilities in the annual general meeting. This is one of the non-transferable duties of the general assembly (TCC, article 408).

Disclosure and transparency

35 Corporate charter and by-laws

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

The AoA of a company and any amendments thereto must be registered in the relevant trade registry and announced in the Turkish Trade Registry Gazette as of its incorporation. Further, the AoA of a company that is obliged to launch a website (see question 36) is also announced on the company website. According to the CGP, the AoA of a company must also be published on the company's website (CGP, article 2.1.1).

Update and trends

There have not been many developments in corporate governance area this year, due to the unfortunate events in Turkey, the most significant of which are terrorist attacks and the failed coup attempt in July. Following these events, the Turkish government announced a state of emergency on 21 July 2016 for an initial period of three months. Since then, the state of emergency period has been extended several times and is still in effect.

As a consequence of the state of emergency, many companies that were deemed to be connected to terrorist organisations have been assigned administrators or trustees. Assignment of administrators or trustees is regulated under article 133 of the Criminal Procedural Code. Pursuant to this article, during the criminal proceedings, if a criminal court find a strong suspicion that there is a connection between a company and terrorist organisations, it may decide to assign an administrator or trustee for the said company. The trade registry ex officio registers the decision. The decision is also published in the Turkish Trade Registry Gazette.

Recently, there has been an arrangement regarding the administrators or trustees appointed in such conditions. Accordingly, pursuant to article 19 of the Law No. 6758, the Savings Deposit Insurance Fund (TMSF) will be assigned as an administrator or trustee to the companies deemed to be connected to terrorist organisations. As a result, the companies in which administrators or trustees are appointed will continue to be managed in accordance with commercial practices and diligence in line with the commercial law requirements until the finalisation of investigation and prosecution processes. In this respect, such companies will be managed by the managers or board to be determined by the relevant Ministry office under the supervision of TMSF. The managing board of such companies will be appointed and (if required) dismissed by the relevant Ministry office.

36 Company information

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

With the TCC, each capital stock company subject to independent audit is obliged to maintain a company website within three months following the incorporation of the company and must allocate a specific part of the website to making the announcements legally required (TCC, article 1524).

Pursuant to the relevant provision of the TCC, companies that are subject to the independent audit must be determined by the Council of Ministers. The Council of Ministers issued this decision on 19 December 2012 (the Decision Regarding the Determination of the Companies to be Subject to an Independent Audit (the Decision), which has been revised by the Council of Ministers decision dated 16 February 2016 and published in the Official Gazette on 19 March 2016).

As per article 3 of the Decision, companies that fulfil at least two of the three conditions given in article 3 together with their affiliates, subsidiaries or by themselves for two consecutive account periods shall be subject to the independent audit.

These conditions are: companies with aggregate assets amounting to 40 million or more Turkish liras; companies with annual net sale revenues amounting to 80 million or more Turkish liras; and companies with 200 or more employees.

In addition to the above, the Amendment Code has narrowed the scope of the announcements to be made by the companies on their websites and has regulated that the announcements legally required to be made must be announced on the website, as well as having introduced certain time periods for publication of the commercial papers and documents, which are required to be published on the website of a company.

Companies that do not launch a website within three months as of the date the TCC entered into force will be subject to a judicial fine of between 100 and 300 days, and authorised bodies of companies that do not allocate part of the website to public information within the same period of time will be subject to a judicial fine of up to 100 days (see question 27) (TCC, article 562/12).

Hot topics

37 Say-on-pay

Do shareholders have an advisory or other vote regarding executive remuneration? How frequently may they vote?

According to the CGP, a written remuneration policy should be submitted to the shareholders during the GA meetings and discussed as a separate agenda article to give them the opportunity to air their views and suggestions in relation to the remuneration policy that applies to members of the board of directors and key executives. The remuneration policies of public companies are announced on their websites (CGP, article 4.6.2).

38 Shareholder-nominated directors

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

As per the TCC, shareholders have the ability to appoint directors provided that it is explicitly stipulated under the AoA of the company. Such ability can be granted to specific share groups, shareholders of a specific nature (eg, the founding family shareholders) or minority shareholders. Unless there is a just cause, the nominated director must be appointed as a member of the board of directors. In listed companies, the nominated directors of a corporation must be mentioned in the mandatory information form required to be published by proxy solicitors.

39 Shareholder engagement

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

The shareholders exercise their rights during the GA meetings; companies engage with shareholders mainly within the scope of GA.

Under the TCC, the management of a company is generally conducted by the board of directors, but GA is also an essential organ of the company and has fundamental duties. Duties such as the amendment of the AoA, appointment and removal of the board members, appointment of the auditor, passing of decisions concerning financial tables, the annual report of the board of directors, determinations of annual income, profit share and revenues, inclusion of reserve fund to the capital and profit to be distributed to the shareholders etc, must be determined by the GA (TCC, article 408).

An ordinary GA shall be convened within three months as of the end of each activity period. An extraordinary GA can be convened whenever required. The board of directors invites the shareholders to GAs. This invitation shall be made in the form provided in the AoA. Invitation to the GA shall also be published in the Turkish Trade Registry Gazette. Invitation shall be issued at least two weeks prior to the date of GA meeting (excluding the dates of announcement and meeting). All shareholders whose names appear on the attendance list prepared by the board of directors have the right to attend the meeting.

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Ukraine

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Sources of corporate governance rules and practices

1 Primary sources of law, regulation and practice

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

The primary sources of law relating to corporate governance in Ukraine are:
- the Civil Code of Ukraine (2003);
- the Commercial Code of Ukraine (2003);
- the Law of Ukraine on Commercial Companies (1991); and
- the Law of Ukraine on Joint Stock Companies (2008).

The Civil Code of Ukraine contains general provisions on legal entities, including the general regulatory framework for the most popular types of commercial companies for medium-sized and large businesses, which are the focus of this chapter – limited liability companies (LLCs) and joint-stock companies (JSCs). Scarce regulation concerning LLCs and JSCs can be found in the Commercial Code of Ukraine, which is primarily concerned with enterprises – a loosely regulated corporate form used by small businesses and in the state sector. The Law of Ukraine on Commercial Companies (the LLC Law) and the Law of Ukraine on Joint Stock Companies (the JSC Law) stipulate rules for the governance of LLCs and JSCs, respectively.

In addition, there are specific laws relating to corporate governance in certain business sectors, such as the Ukraine Law on Banks and Banking Activity for banks or the Ukraine Law on Management of State Property Objects for state-owned companies. The peculiarities of corporate governance in state-owned companies are established in the regulations of the Cabinet of Ministers of Ukraine.

The 'comply or explain' approach is not applicable in Ukraine. The National Securities and Stock Market Commission (the Securities Commission) approved the Principles of Corporate Governance (2014) (the Corporate Governance Principles), which are recommended or mandatory for public JSCs (depending on the level of their listing). Public JSCs are not required to explain publicly non-compliance with these principles. Other JSCs may adhere to the Corporate Governance Principles voluntarily. The National Bank of Ukraine (NBU) adopted the Methodological Recommendations on Improvement of Corporate Governance in Banks in Ukraine (2007) – non-binding recommendations that apply to Ukrainian banks.

2 Responsible entities

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

The general framework for corporate governance is established in the codes and laws enacted by the Ukrainian parliament.

The Securities Commission is the primary regulator for JSCs. The Securities Commission elaborates corporate governance rules for JSCs, oversees their application and has certain enforcement powers (eg, by ordering JSCs to remove violations or imposing fines). The NBU enforces corporate governance rules in Ukrainian banks.

The Ministry of Justice is responsible for ensuring operation of the Unified State Register of Legal Entities, Individual Entrepreneurs and Public Organisations – the public register containing information on all legal entities registered in Ukraine.

The enforcement of corporate governance rules may also take place in Ukrainian courts pursuant to actions brought by shareholders in their own name or derivative suits brought by shareholders on behalf of the company.

The rights and equitable treatment of shareholders

3 Shareholder powers

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

Corporate governance in Ukrainian JSCs is comprised of the general meeting of shareholders (GMS) as the highest governing body, a sole director or a management board as the executive body, and a supervisory board as the controlling body overseeing and regulating the activity of the management board and protecting shareholders' rights. Creation of a supervisory board is mandatory for JSCs with 10 or more shareholders and optional for JSCs with fewer than 10 shareholders. In addition, an audit commission (or a sole internal auditor), a corporate body separate from the supervisory board, may be created in a JSC for auditing the company's financial and commercial activities.

As a general rule, members of the supervisory board are elected and removed by the GMS, and members of the management board are elected and removed by the supervisory board. At the same time, the GMS may resolve any matter of the company's business and its decisions override the decisions of the supervisory and management boards, so effectively the GMS may also elect and remove the management board. In addition, the JSC's charter may determine that election or removal of the management board is a matter reserved for the GMS, in which case the supervisory board will not have the right to elect or remove the management board.

Supervisory board members of a public JSC are elected at a GMS for the term until the next annual GMS (effectively, they must be re-elected at each annual GMS) by way of cumulative voting. In private JSCs, the term of office and type of voting for election of supervisory board members (ie, by cumulative voting or by simple or qualified majority of votes) are determined in the charter.

The GMS can terminate the powers of supervisory board members at any time and in cases where the supervisory board was elected by cumulative voting the decision on termination applies to the whole composition of the supervisory board. The GSM does not need to have any grounds for such termination. In addition, if a supervisory board member was elected as a representative of a shareholder (as opposed to an independent member), the shareholder may replace its representative in the supervisory board at any time by providing notice to the company (ie, without the need to convene a GMS).

The procedure of appointment and removal of the director or management board members in a JSC is prescribed in its charter.

As regards LLCs, their corporate governance is comprised of the general meeting of participants (GMP) as the highest governing body and a sole director or a board of directors as the executive body. LLCs can arguably also have supervisory boards, but this is neither expressly recognised nor prohibited by law. Appointment and removal of a sole director or a management board of a LLC is within the exclusive competence of the GMP. The relevant decision may be taken by the GMP at any time by a simple majority of votes of participants present at the GMP. Moreover, the GMP generally has the right to decide on all matters relating to the activity of the LLCs, including matters delegated to the executive body.

4 Shareholder decisions

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

Ukrainian law reserves a number of decisions to the exclusive competence of the GMS/GMP (depending on the corporate form). Exclusive competence of the GMS of a JSC includes:

- determination of main areas of activity of the company;
- amending the company charter;
- increasing or decreasing the company's charter capital;
- placement, cancellation, split-up, consolidation, redemption of shares;
- determination of the type of the JSC (public or private);
- approval of internal regulations on GMS, the supervisory board, the management board and the audit commission, corporate governance code, and of other internal documents provided for in the charter;
- approval of annual reports of the company;
- distribution of profit and covering losses, approval of the amount of annual dividends;
- election of supervisory board members, approval of the terms of their engagement and remuneration, termination of their powers;
- election of audit commission members (internal auditor), termination of their powers, approval of conclusions of the audit commission (internal auditor);
- approval of significant transactions if the market value of the property, works or services in the transaction exceeds 25 per cent of the company's net assets;
- approval of interested-party transactions if the market value of the property, works or services in the transaction exceeds 10 per cent of the company's net assets; and
- spin-off from the company, wind-up and liquidation of the company.

Exclusive competence of the GMP of a LLC includes:

- determination of main areas of activity of the company, approval of business plans and reports on their performance;
- amending the company's charter, including changes in charter capital;
- determination of the amount and form of additional contributions to the charter capital;
- redemption of participation interest in the company and expulsion of a participant from the company;
- appointment and removal of the executive body;
- determination of forms of control over the executive body, creation of respective controlling bodies;
- approval of annual reports, distribution of profit, payment of dividends, covering losses;
- establishment, reorganisation and liquidation of subsidiaries, branches and representative offices, approval of their charters and regulations;
- taking decisions to bring the company's officers to material liability;
- determination of the company's organisational structure;
- determination of remuneration of officers of the company, its subsidiaries, branches and representative offices; and
- wind-up and liquidation of the company.

Taking decisions on matters within the exclusive competence of the GMS/GMP may not be delegated to other governing bodies. In addition to the decisions listed above, the law allows for the designation of additional matters to the exclusive competence of the GMS/GMP.

The concept of non-binding shareholder votes is not common in Ukraine.

5 Disproportionate voting rights

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

As a general rule, one ordinary share in a JSC gives the shareholder one vote to decide on all issues considered at the GMS, but there are a number of exceptions:

Cumulative voting – a type of voting used at the GMS for electing members of collegial bodies. Cumulative voting is mandatory for the election of supervisory board members in public JSCs and can be used in private JSCs or for the election of management board members if this is provided for in the charter. During cumulative voting, the total number of votes of a shareholder is multiplied by the number of members to be elected and the shareholder may give all votes to one nominee or distribute the votes between several nominees. Cumulative voting takes place for all nominees simultaneously. The nominees who receive most votes secure election.

During votes at the GMS on the issue of approval of an interested-party transaction, the interested shareholders do not vote and the decision is passed by a majority of those participating shareholders who do not have a conflict of interest.

Treasury shares are not taken into account for the purpose of determination of quorum and voting at a GMS.

The Law on the Depository System of Ukraine, which took effect in October 2013, established that all shares must be converted into non-documentary (electronic) form and required owners of all JSC shares existing in documentary form to open securities accounts with depository institutions and transfer their shares to such accounts by October 2014. If a shareholder has failed to do so, his or her shares are not taken into account for the purpose of determining a quorum and voting at the GMS.

JSCs may issue preference shares or several classes of preference shares with limited voting rights. Preference shares may not exceed 25 per cent of charter capital of the JSC. Owners of preference shares of a certain class have voting rights on the following decisions:

- wind-up of the company that provides for conversion of preference shares of this class into preference shares of another class, ordinary shares or other securities;
- making amendments to the company's charter providing for limitation of rights of owners of this class of shares;
- making amendments to the company's charter providing for the placement of a new class of preference shares whose owners will have priority for receipt of dividends or distributions in case of the company's liquidation or the increase of shareholder rights – owners of preference shares having priority for receipt of dividends or distributions in case of company liquidation; and
- the charter of a private JSC may also provide owners of preference shares with voting rights on other issues.

A JSC may not establish limitations on the amount of shares or the amount of votes under shares owned by one shareholder.

Participants of an LLC have a number of votes at the GMP proportional to their participation interests (ie, stakes held in the charter capital of an LLC). Participation interest redeemed by the company is not taken into account for the purpose of determination of quorum and voting at the GMP. When the GMP decides on the expulsion of a participant from the company, the expelled participant does not participate in voting.

The Civil Code additionally prescribes that a shareholder or participant may not vote at the GMS or GMP on issues related to a transaction or a dispute between the company and such shareholder or participant.

It should be mentioned separately that the NBU and the National Commission on State Regulation of Financial Services Markets may temporarily restrict the use of voting rights of shareholders of banks and non-banking financial institutions, respectively. This is a sanction for certain violations of legislation (eg, failure to obtain prior approval for acquisition of a significant shareholding in a bank or a non-banking financial institution).

6 Shareholders' meetings and voting

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

Persons included on the list of shareholders having the right to participate in the GMS and their proxies may participate in the GMS. This list is prepared by the central depository three business days in advance of the GMS. Amendments to this list following compilation are prohibited. Shareholders or their proxies must register with the registration commission appointed by the supervisory board. Powers of attorney for representation at the GMS must be made in writing, and, if issued by an individual, must be notarised or certified by a depository institution.

A GMS is deemed quorate if shareholders owning more than 50 per cent of voting shares register for participation in the GMS. The quorum requirement is mandatory and may not be derogated in the charter of a JSC.

Voting at the GMS may be carried out only with the use of voting bulletins.

Absentee voting may be allowed in JSCs having not more than 25 shareholders in cases provided for by the charter. In such cases, the draft resolution in question is sent to shareholders, who must return their votes within five days from receipt thereof. A unanimous vote of all shareholders with voting shares is required to take a decision via absentee voting.

If a JSC has a sole shareholder, written resolutions of this shareholder have the status of GMS decisions and there is no need to convene and hold a GMS.

As regards LLCs, all participants of the LLC or their proxies have the right to participate in the GMP. A GMP is deemed quorate if participants owning more than 50 per cent of votes are present. The Charter of an LLC, in which the state does not hold a participatory interest, may establish a different quorum for the GMP. Absentee voting in LLCs may be allowed in cases prescribed by the charter. All participants of the LLC must take part in absentee voting in order for the vote to be valid.

7 Shareholders and the board

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

A JSC is obliged to convene an annual GMS to be held not later than 30 April each year. An extraordinary GMS can be convened by the supervisory board at its own initiative, at the request of the executive body, audit commission or shareholders owning at least 10 per cent of ordinary shares, and in other cases provided by the charter. If the supervisory board does not convene an extraordinary GMS within 10 days from receipt of the convocation demand, the GMS may be convened by the requesting shareholders.

Each shareholder of a JSC has the right to submit proposals to the agenda of the GMS at least 20 days in advance of the GMS and propose nominees to the company's governing bodies at least seven days in advance of the GMS. Proposals of shareholders owning at least 5 per cent of ordinary shares are mandatory for inclusion into the agenda of the GSM.

A GMP of an LLC is convened at least twice a year, unless otherwise provided by its charter. Participants of an LLC owning more than 20 per cent of votes have the right to demand convocation of an extraordinary GMP at any time and on any matter. If the company fails to convene the GMP within 25 days, the participants may proceed with the convocation themselves. Any participant may demand an issue to be considered at the GMP provided it is notified at least 25 days before the GMP. The GMP may take decisions on issues that were not included into the agenda, subject to the consent of all participants present at the GMP.

8 Controlling shareholders' duties

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

The law does not prescribe any specific duties of controlling shareholders of JSCs or participants of LLCs with respect to the company and non-controlling shareholders or participants.

9 Shareholder responsibility

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

As a general rule, shareholders of a JSC and participants of an LLC are not liable for the obligations of the company and bear the risk of losses related to the company's activity within the value of their shares or contributions into the company's charter capital. However, shareholders or participants may face subsidiary liability for the company's obligations if the company is declared bankrupt due to their fault.

Corporate control

10 Anti-takeover devices

Are anti-takeover devices permitted?

Due to a lack of actual public takeovers, the concept of anti-takeover devices has not been developed in Ukraine. The JSC law provides that any person (or persons acting in concert) intending to acquire a significant shareholding in a JSC (more than 10 per cent of ordinary shares) must give a 30-day written notice to the JSC, the stock exchange where the JSC is listed, and the Securities Commission, and to make a printed publication of such notice. The JSC does not have the right to take measures aimed at preventing such acquisition.

11 Issuance of new shares

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

Taking decisions on the issuance of new shares or increases of charter capital is within the exclusive competence of the GMS or GMP. The supervisory and management boards are not permitted to issue new shares or decide on increases of charter capital.

Shareholders of JSCs enjoy a pre-emptive right of purchase of newly issued shares proportionally to their shareholding, but only in cases of private placement of shares (ie, placement among shareholders and a pre-defined list of investors not exceeding 100 persons). Owners of preference shares only have these pre-emptive rights if specified in the company charter. It should be noted that private JSCs can only carry out the private placement of shares, while public JSCs may carry out both private and public placement of shares.

LLCs do not have shares as such, but rather participation interest in the charter capital, which do not qualify as securities.

12 Restrictions on the transfer of fully paid shares

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

Shareholders of public JSCs may freely dispose of their shares. A charter of a private JSC with not more than 100 shareholders may provide for the shareholders' right of first refusal in cases involving the transfer of shares to third parties. Transfer of participatory interest in an LLC to third parties may be prohibited by the charter, otherwise participants always have the right of first refusal.

13 Compulsory repurchase rules

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

Compulsory share repurchase in a JSC at the company's initiative is not allowed. Shareholders may force the JSC to redeem its own shares at market value if they disagree with certain decisions at the GMS (see question 14).

14 Dissenters' rights

Do shareholders have appraisal rights?

Owners of ordinary shares of a JSC have the right to demand the mandatory buyout of their shares by the company if they voted at a GMS against any of the following decisions: corporate reorganisation or change of company type; approval of a significant or interested party transaction; or change of the amount of charter capital.

Owners of preference shares of a JSC have the right to demand mandatory buyout if they voted at a GMS against making amendments to the company's charter providing for placement of a new class of preference shares whose owners will have a priority for receipt of dividends or distributions in case of the company's liquidation or increase of rights of shareholders – owners of preference shares having priority for receipt of dividends or distributions in case of the company's liquidation.

The company is obliged to buy shares from shareholders who have made a mandatory buyout demand at a price which may not be lower than market price determined based on stock exchange quotations or, failing that, by an independent valuator.

The responsibilities of the board (supervisory)

15 Board structure

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

Ukraine has adopted a two-tier board structure: JSCs have a supervisory board and a management board (executive body). Members of the supervisory board may not be members of the management board. Most LLCs have only an executive body (either a sole director or a board of directors) and do not form a supervisory body.

16 Board's legal responsibilities

What are the board's primary legal responsibilities?

The supervisory board of a JSC is responsible for protecting shareholder rights while controlling and regulating the activity of the management board. The JSC law refers a number of matters to the exclusive competence of the supervisory board that cannot be delegated to the management board. Such matters include the appointment and removal of the executive body, convocation of a GSM, placement and buyout of securities (other than shares), selecting the company's auditor, approval of qualifying significant and interested party transactions, etc. The charter may extend the exclusive competence of the supervisory board.

17 Board obligees

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

The supervisory board of a JSC represents its shareholders and protects their rights. The duties of supervisory board members are outlined in the company's charter and by-laws, as well as agreements between the supervisory board members and the company.

18 Enforcement action against directors

Can an enforcement action against directors be brought by, or on behalf of, those to whom duties are owed?

Officers of JSCs and LLCs (ie, members of the supervisory and management boards) are liable for damages caused to the company if such damages were caused by: excess or abuse of the officer's powers; actions committed by the officer without prior approval when required, or if they received prior approval for such actions by providing false information; or other guilty damaging actions of the officer. A claim against the officer for recovery of such damages may be filed by the company or by shareholders or participants owning at least 10 per cent of the company's charter capital on behalf of the company (a derivative suit).

19 Care and prudence

Do the board's duties include a care or prudence element?

Ukrainian law does not expressly impose duties of care or prudence upon supervisory board members. However, the Corporate Governance Principles provide that a company's officers (including members of the supervisory and management boards) must act in good faith, reasonably, and in the best interests of the company.

20 Board member duties

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

Ukrainian law does not provide for any differences in the duties of individual supervisory board members depending on their skills or experience, etc.

21 Delegation of board responsibilities

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

Powers and responsibilities of the supervisory board that fall under its exclusive competence in accordance with the law or the company's charter may not be delegated to its committees, the management board or other persons. The supervisory board may create committees for reviewing and preparing conclusions on issues within its competence, but supervisory board committees are not vested with decision-making powers.

22 Non-executive and independent directors

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

Ukrainian law does not distinguish between 'executive' and 'non-executive' directors due to the two-tier board structure where supervisory board members do not have executive functions.

The supervisory board of a public JSC or of a JSC in which the state owns more than 50 per cent of shares must have at least two independent members. The law does not establish any different duties and responsibilities of shareholders' representatives and independent supervisory board members. A person may be an independent supervisory board member if that person:

- is not and during the past five years was not an affiliated party of shareholders or the company or its subsidiary, or an officer of the company or its subsidiary;
- does not and did not previously receive substantial additional remuneration from the company or its subsidiary, except the remuneration of an independent director;
- does not and within the past year did not have substantial business relations with the company or its subsidiary;
- is not and within the previous three years was not an employee of the current or past independent auditor of the company or its subsidiary;
- is not and was not the chairperson or member of an executive body of the company's affiliates; or
- is not a close relative of the mentioned persons.

23 Board size and composition

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

The size of the supervisory board is determined in the JSC's charter as long as the minimal size of the supervisory board of a public JSC is five members. The election of supervisory board members is within the exclusive competence of the GMS. If the supervisory board is elected by cumulative voting, filling a vacancy is possible only by termination of powers of the entire supervisory board and election of a new supervisory board by the GMS. These rules do not affect the rights of shareholders whose representatives were elected to the supervisory board to replace such supervisory board members at any time by notice to the company (ie, without the need to convene a GMS).

Supervisory board members must have full legal capacity. Persons with a criminal record of offences against property or white-collar crime may not become officers (including supervisory board members) of a JSC.

JSCs are required to disclose to the Securities Commission the following information on supervisory board composition on a regular basis:

- information on members of the supervisory board (name, passport data, date of birth, education, work experience, number of shares of the JSC owned by the member, criminal record, if any) and their terms of powers, specifying whether they are independent members or shareholders' representatives; and
- information on changes in the composition of the supervisory board, specifying reasons.

24 Board leadership

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

As the supervisory board and the management board are separate bodies, the CEO may not sit on the supervisory board.

25 Board committees

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

Establishing an audit committee and a nomination and remuneration committee is mandatory in public JSCs and JSCs in which the state owns more than 50 per cent of shares. These committees must be composed exclusively or predominantly of independent supervisory board members and presided over by them. JSCs may establish other temporary or permanent supervisory board committees for consideration of issues within the supervisory board's competence.

26 Board meetings

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

The law requires supervisory board meetings at least once a quarter. The charter may provide for more frequent meetings of the supervisory board.

27 Board practices

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

A publicly disclosed annual report on corporate governance in a JSC should contain, inter alia, information on the composition of the supervisory board, average annual number of supervisory board meetings for the last three years, committees created in the supervisory board, and how the amount of remuneration of supervisory board members is defined.

28 Remuneration of directors

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

Establishing the amount of remuneration of supervisory board members is within the exclusive competence of the GMS. Remuneration must be determined in a civil law or labour contract with the supervisory board member. The length of contracts with supervisory board members is dependent on the term of powers for which they are appointed.

The Corporate Governance Principles recommend that supervisory board members receive reasonable remuneration for their work, providing incentives including variable remuneration elements dependent on the performance of the respective member and the company as a whole. The Corporate Governance Principles also recommend that the company's policy on lending officers should be clearly defined in its internal documents and that decisions to provide a loan to a company's officer are approved by the supervisory board.

29 Remuneration of senior management

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

In JSCs, establishing the amount of remuneration of management board members (director) is within the competence of the supervisory board or the GMS. Remuneration must be determined in the labour contract with the management board member (director). The length of contracts with management board members (director) is dependent on the term of powers for which they are appointed.

According to the Corporate Governance Principles, the amount and form of remuneration of management board members should be determined by the supervisory board pursuant to recommendations of the nomination and remuneration committee (if created) and should correlate with the company's performance in view of the company's and shareholders' long-term interests.

In LLCs, establishing officers' remuneration is within the exclusive competence of the GMP. Levels of remuneration are determined in labour contracts.

30 D&O liability insurance

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

D&O liability insurance is permitted and the company may pay premiums, but it is not common in Ukraine.

31 Indemnification of directors and officers

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

Ukrainian law does not prohibit or constrain indemnification of officers for liabilities incurred in their professional capacity, but is not very common in practice.

32 Exculpation of directors and officers

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

According to the law, officers of JSCs and LLCs (ie, members of the supervisory and management boards) are liable for damages caused

Update and trends

On 23 March 2017, the parliament of Ukraine passed two draft laws allowing shareholder agreements to be entered into under the Ukrainian law (No. 4470) and improving takeover (squeeze-out and sell-out) rules for Ukrainian joint stock companies (No. 2302a-d). These laws are still awaiting the President's signature and official publication in order to take effect.

Historically, Ukrainian corporate governance laws have been rather inflexible, as they did not allow shareholders of private companies to deviate from mandatory rules prescribed by the law and contractually agree on the regulation of relations among themselves. Draft law No. 4470 introduces a legal framework for agreements between shareholders of Ukrainian limited liability companies and joint-stock companies. The draft law also sets out a general framework for the enforcement of shareholder agreements and introduces certain legal instruments that should ensure the performance of obligations under shareholder agreements, such as an irrevocable powers of attorney and specific contractual termination rights.

Draft law No. 2302a-d aims to implement provisions of EU Directive 2004/25/EC on takeover bids into Ukrainian joint-stock company legislation. In accordance with the draft law, direct or indirect acquisition by a person (or persons acting in concert) of a shareholding exceeding 95 per cent of ordinary shares of a joint stock company triggers the right to squeeze out the remaining minority shareholders. In turn, minority shareholders will have the right to sell out their shares should the majority shareholder omit to use the right of squeeze-out. Notably, during a two-year transition period following the effective date of the law, persons owning a more than 95 per cent shareholding as of that date will also have the right to trigger a squeeze-out.

In addition, the draft law also exempts public joint-stock companies that have decided to change their status to private joint-stock company or to reorganise into another corporate form such as a limited liability company from the requirement to procure re-issue of licences, permits and other documents, which would otherwise be triggered as a result of a change of the company's official name. This is one of the moves encouraging 'quasi-public' companies to transform into private companies following recent legislative amendments enhancing corporate governance and disclosure requirements for public companies.

On 20 December 2016, the parliament of Ukraine passed in the first reading the draft law 'On Limited Liability Companies' (No. 4666). The draft law is currently awaiting a second reading in Parliament. When enacted, the draft law will overhaul the legal framework for LLCs in Ukraine. It aims, among other things, to give more discretion to LLC participants in arraigning the management of the company. In particular, the draft law will allow for the creation of supervisory boards in LLCs, improve the regulation of procedure for accession, withdrawal and expulsion of participants and simplify the participatory interest transfer procedure.

to the company if these damages were caused by: excess or abuse of the officer's powers; actions committed by the officer without prior approval if required, or if they received prior approval for such actions by providing false information; or other guilty damaging actions of the officer. The law does not allow limits to officers' liability for damages caused to the company as a result of their actions. Moreover, the law stipulates that shareholders are jointly liable for damages caused to the company by their representatives in the supervisory board.

33 Employees

What role do employees play in corporate governance?

In JSCs, a labour union representative may be present at any GMS and meeting of the management board, and may be invited to supervisory board meetings with the right of advisory vote. Other than that, employees do not have powers to affect the decision-making process in governing bodies, unless otherwise provided for by the company's by-laws.

34 Board and director evaluations

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

Current law and regulations do not require mandatory evaluation of the supervisory board, its committees, or the management boards. However, according to the Corporate Governance Principles, the supervisory board should annually evaluate its performance as a whole and the performance of each member individually. The main tasks of determining evaluation criteria and procedures should be performed by the nomination and remuneration committee or other committee composed predominantly of independent members, with at least the following criteria taken into account: attendance of meetings, level of preparation for meetings and impartiality in decision-making. The supervisory board should also regularly evaluate the performance of the management board.

Publicly disclosed annual information on corporate governance in a JSC should specify whether the supervisory board carried out self-evaluation of its composition, organisation of activity and, if so, information on the competence and effectiveness of the supervisory board (or its members and committees) and performance of its tasks.

Disclosure and transparency

35 Corporate charter and by-laws

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

A public JSC must publish its charter and by-laws on its own website.

In addition, charters of all companies registered after 1 January 2016, and charters restated after that date are contained in the Unified State Register of Legal Entities, Individual Entrepreneurs, and Public Organisations in electronic form; however, they can only be downloaded with an access code that should be requested from the respective company.

36 Company information

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

The Securities Commission requires JSCs to disclose regular and special information in a publicly available database (www.stockmarket.gov.ua), official printed media, and on their website. This information includes:

- Regular annual information including:
  - general information about the company;
  - information on the company's officers;
  - information on owners of 10 per cent or more of the company's shares;
  - information on the GMS;
  - information on the company's securities;
  - information on the company's commercial and financial activity;
  - information on corporate governance; and
  - an annual financial report;
- Annual information of a public JSC should additionally include:
  - information on licences (permits) for specific types of activity;
  - information of the company's participation in other companies;
  - information on corporate secretary;
  - information on the company's rating agency;
  - information on shareholders and the amount of shares owned;
  - information on dividends;
  - information on professional participants of the stock market, auditors, legal consultants, insurers and rating agencies engaged by the company;
  - description of business; and
  - the text of the auditor's report;

- Regular quarterly information (applicable to issuers of publicly traded securities and JSCs in which the state owns 25 per cent or more of shares) which includes:
  - general information about the company;
  - information about the company's officers;
  - information on professional participants of the stock market, auditors, legal consultants, insurers and rating agencies engaged by the company;
  - information on the company's securities;
  - information on the company's commercial and financial activity;
  - information about the company's participation in other companies;
  - information on corporate secretary; and
  - quarterly financial reports;
- Special information which must be disclosed within one business day upon occurrence of the respective event:
  - decision on placement of securities exceeding 10 per cent of charter capital;
  - decision on repurchase of company shares;
  - listing or delisting of shares on a stock exchange;
  - decision on approval of significant or affiliated party transactions;
  - change of the company's officers;
  - change of owners of 10 per cent or more of voting shares;
  - decision on establishing or liquidating branches or representative offices;
  - decision to reduce charter capital;
  - initiation of proceedings on recovery by the company's officer of damages caused to the company;
  - decision to pay dividends;
  - initiation of bankruptcy proceedings;
  - decision to liquidate the company; and
  - change of type of the JSC;
- JSCs are also obliged to publish notifications on the convocation of a GMS and changes in its agenda (if any).

In addition, public JSCs are obliged to disclose the following documents on their websites: charter, by-laws on GMS, supervisory board, management board, audit commission and other governing bodies, by-laws of branches and representative offices, corporate governance code, GMS minutes, conclusions of the audit commission and independent auditor, securities issue prospectuses, list of the company's affiliated persons, and notifications to shareholders as may be required by legislation.

Hot topics

37 Say-on-pay

Do shareholders have an advisory or other vote regarding executive remuneration? How frequently may they vote?

In JSCs, the GMS may decide on remuneration of the management board even if according to the charter such decisions are within the competence of the supervisory board. In LLCs, deciding on the remuneration of the management board (director) is within the exclusive competence of the GMS. There is no limitation on the frequency of such decisions.

38 Shareholder-nominated directors

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

In JSCs, each shareholder may nominate candidates to the company's governing bodies to be appointed by the GSM as long as the number of nominees from one shareholder does not exceed the number of members of the respective body. Nominations must be made at least seven days prior to the GMS. Nominations from shareholders owning 5 per cent or more of shares are mandatory for inclusion into the GSM agenda.

39 Shareholder engagement

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

In Ukraine, shareholders are typically actively engaged in the company's activity throughout the year, and not only during the annual meeting season. This engagement is typically through the company's senior management. The law provides that the supervisory board of a JSC may appoint a corporate secretary, who is responsible for interaction with the company's shareholders. However, in practice corporate secretaries are rarely appointed.

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Sources of corporate governance rules and practices

1 Primary sources of law, regulation and practice

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

The UK's corporate governance regime consists of laws, rules and practices, which ensure that companies operate with integrity and that those responsible for their management are accountable for their actions. Its purpose is to encourage investor and public confidence in UK companies and thus to promote economic stability. The main sources of corporate governance in the UK are as follows:

Statute

The Companies Act 2006 (CA 2006) is the principal statute relating to corporate governance in the UK. CA 2006 codifies and replaces certain common law duties of directors (CA 2006, section 170(3)) (see 'Common law'). The statutory duties of directors under CA 2006 are as follows:

- to act within powers (ie, in accordance with the company's constitution) (section 171);
- to promote the success of the company (section 172);
- to exercise independent judgement (section 173);
- to exercise reasonable care, skill and diligence (section 174);
- to avoid conflicts of interest (section 175);
- not to accept benefits from third parties (section 176); and
- to declare any interest in a proposed transaction or arrangement with the company (section 177).

However, these statutory duties must be interpreted and applied in accordance with the common law duties that are discussed below (CA 2006, section 170(4)). Indeed, in respect of directors' duties that have not been codified under CA 2006 (such as the duty to keep the affairs of the company confidential) the common law rules remain the only relevant law. CA 2006 contains further provisions relevant to corporate governance, which are discussed at various points in this chapter.

Statutes including the Corporate Manslaughter and Corporate Homicide Act 2007, the Financial Services and Markets Act 2000 (FSMA 2000), the Criminal Justice Act 1993, the Insolvency Act 1986, the Bribery Act 2010, the Financial Services Act 2010 and various statutory instruments also contain provisions relating to corporate governance.

Common law

Company directors have a range of fiduciary, or common law, duties derived from a long line of case law dating back to the early nineteenth century. These fiduciary duties include a requirement:

- to exercise skill and care;
- to act in good faith in the best interests of the company;
- to act within the powers conferred by the company's constitution and to exercise these powers for proper purposes;
- not to fetter discretion;
- to avoid interests that conflict with those of the company and to avoid duties that conflict with the director's duties to the company;
- not to make a secret profit; and
- to keep the affairs of the company confidential.

Some of these common law duties have now been codified and replaced by CA 2006, sections 171 to 177 (see 'Statute').

The listing regime

The Listing, Prospectus, Disclosure Guidance and Transparency Rules (the LPDT Rules) play a significant role in regulating UK-listed companies. They form part of the Financial Conduct Authority's (FCA) Handbook, which contains the rules and guidance made under FSMA 2000, the principal statute relating to financial services in the UK. The LPDT Rules comprise the following sets of rules, which are mandatory for those companies to which they apply.

- The Listing Rules (LRs), which apply to issuers who have applied for their securities to be listed, or whose securities are already listed, on the United Kingdom Listing Authority's (UKLA) Official List and set out:
  - the requirements a company must meet for its securities to be admitted to listing;
  - rules relating to listing particulars; and
  - certain obligations that a company must continue to comply with after its securities have been admitted to listing (known as 'continuing obligations'). Note that certain LRs will apply only to companies with a premium listing and not to those with a standard listing.
- The Prospectus Rules (PRs), which implement the Prospectus Directive and require issuers of securities, subject to certain exemptions, to publish a prospectus if they offer their shares to the public or make a request for their shares to be admitted to trading on a regulated market in the UK. The PRs contain rules on the contents of a prospectus and the approval process for such a document; and
- The Disclosure Guidance and Transparency Rules (DTRs), which apply to a company that has applied for its securities to be admitted, or whose securities are already admitted, to trading on a regulated market in the UK (this includes companies whose shares are admitted to the Official List and are traded on the London Stock Exchange (LSE), but not companies whose securities are quoted on the Alternative Investment Market).

Perhaps the two most important elements of the LPDT Rules are the Listing Principles set out at LR7 (which assist companies in understanding their duties under the LPDT Rules and encourage issuers of securities to take their role in maintaining market confidence and ensuring fair and orderly markets seriously) and the continuing obligations contained in the LRs and DTRs with which a UK-listed company must comply in order to maintain its listing. Broadly speaking, in terms of complying with corporate governance disclosure obligations, listed companies must ensure that they comply with DTRs 7.1 and 7.2, and LR9.8. Additionally, there are various disclosure requirements contained in the UK Corporate Governance Code, the details of which are outlined in schedule B to the Code (see question 27).

The UK has a two-tier listing regime, which, as of 6 April 2010, is divided into a premium listing and a standard listing (before this date the two tiers were referred to as a primary listing and a secondary listing). Issuers of securities with a premium listing must comply with super-equivalent standards (standards that exceed the minimum standards set down by the relevant EU directive). Issuers of securities with a standard listing need only comply with the minimum standards of EU legislation.

The UK Corporate Governance Code (the Code)

The Code represents key corporate governance recommendations of best practice for companies. The Financial Reporting Council (FRC) first published the Code on 28 May 2010 when it superseded the existing Combined Code on Corporate Governance (Combined Code). A new version of the Code was published in September 2012, applying to accounting periods beginning on or after 1 October 2012, and a further revised version was published in September 2014 and applies to accounting periods beginning on or after 1 October 2014 (see below). The old versions of the Code will continue to apply to the historic accounting periods to which they relate. This chapter concentrates on the application of the Code. The Code is applicable to all companies with a premium listing of equity shares in the UK, regardless of whether the company is incorporated in the UK or elsewhere. The Code is divided into main principles, supporting principles and provisions. The Code does not have statutory force, rather it establishes principles of good governance and provides recommendations and guidance. However, companies with a premium listing of equity shares incorporated either in the UK (LR9.8.6R(5)) or overseas (LR9.8.7R) are required to include a statement in their annual financial report that explains how the company has applied the main principles of the Code, in a manner that would enable shareholders to evaluate how the principles have been applied. Such companies must also set out in the annual financial report whether or not they have complied with all of the provisions of the Code over the course of the accounting period and give reasons for any non-compliance (the 'comply or explain' regime) (LR9.8.6R(6)). Companies are not obliged to comply with the Code and the board may explain why it has not complied, but failure to comply with the Code could damage investors' confidence in a company if good governance has not been adhered to. This could ultimately lead to its shareholders voting against resolutions proposed by the company or even selling their shares. The FRC acknowledges that a listed company may wish to deviate from the provisions of the Code, and the intention of the 'comply or explain' approach is to encourage engagement with the shareholders and to ensure good governance, perhaps in a different guise.

The Code states that the purpose of corporate governance 'is to facilitate effective, entrepreneurial and prudent management that can deliver the long-term success of the company'. Some of the crucial principles and provisions that the Code encompasses are:

- effective board management in the long-term interests of the company;
- definitions of the role of the board, the chairman and the non-executive directors of a company;
- the separation of the roles of the chairman and the chief executive officer of a company;
- the role of the chairman in leading the board and ensuring effectiveness;
- the role of non-executive directors in constructively challenging strategy and scrutinising performance;
- the composition of the board;
- open and rigorous procedures for the appointment of directors from a wide pool of candidates, with due regard for the benefits of diversity;
- formal evaluation of the performance of boards, committees and individual directors, along with provision for the induction and professional development of non-executive directors;
- the number of independent non-executive directors that a company must have on its board;
- close relationships between the chairman, the senior independent director, non-executive directors and major shareholders of a company;
- the role of a company's audit committee in monitoring the integrity of its financial reporting, reinforcing the independence of the external auditor and reviewing the management of financial and other risks;
- the composition of the board to be such that it has a balance of skills, experience, independence and knowledge of the company; and
- the requirement for all directors to allocate sufficient time to the company to discharge their responsibilities effectively.

The Combined Code was renamed the UK Corporate Governance Code in May 2010 in an effort to make its status as the UK's corporate governance standard apparent to foreign investors and foreign companies listed in the UK. The May 2010 version of the Code was largely influenced by the third FRC review of the Combined Code and an independent review led by Sir David Walker into corporate governance in the financial services sector (the Walker Review). The Walker Review was also instrumental in the implementation of the Stewardship Code (see 'The UK Stewardship Code'). The May 2010 version of the Code therefore evidenced a number of significant changes to the Combined Code, including a greater emphasis on long-term success, a requirement for a clearer statement of the board's responsibilities relating to risk, greater focus on the importance of board diversity and a recommendation that all directors of FTSE 350 companies be put up for re-election every year.

By introducing new main principles and by elevating certain existing supporting principles, the FRC ensured that listed companies would have to explain in their annual financial reports how they have applied them. It should be noted that there is technically no such obligation to demonstrate compliance with supporting principles, though by their nature the supporting principles are closely linked to the main principles. The following principles of the Code were substantively extended or amended:

- the board became responsible specifically for the long-term success of the company, whereas in the 2008 version of the Combined Code the board was simply responsible for the 'success' of the company (main principle A.1);
- the chairman of the board of directors is required to promote a culture of openness and debate, and to ensure that adequate time is available for discussion (supporting principle A.3);
- the board must specifically consider the benefits of diversity, including gender diversity, when appointing new directors to the board (supporting principle B.2);
- the board became responsible for determining the nature and extent of the significant risks it is prepared to take in achieving its strategic objectives, whereas previously it was simply required to maintain sound risk management and internal control systems (main principle C.2); and
- the chairman of a company should ensure that all directors are made aware of their major shareholders' concerns (supporting principle E.1).

The following provisions were introduced into the Code for the first time:

- the chairman should regularly review and agree with each director their training and development needs (provision B.4.2);
- the evaluation of the boards of FTSE 350 companies should be externally facilitated every three years, and any link between the company and the facilitator should be disclosed (provision B.6.2); and
- the board must provide an explanation of the company's business model in its annual report (provision C.1.2).

Certain existing provisions were also amended and extended:

- the senior independent director should provide a sounding board for the chairman and act as an intermediary for the other board directors when necessary (provision A.4.1);
- FTSE 350 directors should be put forward for re-election annually (provision B.7.1);
- the remuneration of non-executive directors should not include performance-related elements (provision D.1.3);
- non-executive directors should be offered the opportunity to attend scheduled meetings with major shareholders and should expect to attend meetings if requested by major shareholders (provision E.1.1); and

- where resolutions are passed by a show of hands at a general meeting, specific information relating to the resolution must be given at the meeting and made available on the company website as soon as reasonably practicable (provision E.2.2).

The FRC also concluded that companies need to focus more on following the spirit of the Code, and not simply adhering to the letter of the Code. The 2012 update to the Code followed an FRC consultation document, published on 20 April 2012, which suggested potential amendments both to the Code and the accompanying guidance on audit committees. Changes to the 2012 Code included requirements for:
- FTSE 350 companies to put the external audit contract out to tender at least every 10 years (provision C.3.7);
- audit committees to report to shareholders on how they have carried out their responsibilities (provision C.3.8);
- boards to confirm that the report and accounts, taken as a whole, are fair, balanced and understandable and provide the information needed for shareholders to assess the company's performance, business model and strategy (provision C.1.1);
- companies to explain and report on their policies on boardroom diversity (provision B.2.4); and
- provision of fuller explanations to shareholders as to why they choose not to follow a provision of the Code (paragraph 3).

The FRC published a further consultation document on 24 April 2014, which considered its biennial review of the Code. The consultation proposed a number of changes, including:
- amending main principle D.1 relating to remuneration of executive directors, such that the requirement that remuneration levels be sufficient to 'attract, retain and motivate directors' be replaced with the requirement that remuneration levels be designed to promote the long-term success of the company;
- amending provision D.1.1, to require schemes of performance-related remuneration to include provisions allowing the company to claw back or withhold payment; and
- changing the approach to assessing and reporting on the company's future viability through changes to the Code provisions relating to risk management and internal control (provision C.2.1).

On 17 September 2014 the FRC published a feedback statement of the April review (above), along with a new version of the Code. This 2014 version of the Code is applicable to financial years beginning on (or after) 1 October 2014. The changes reflect much of the April consultation proposals; for example, at D.1.1 – '[schemes of performance-related remuneration for executive directors] should include provisions that would enable the company to recover sums paid or withhold the payment of any sum, and specify the circumstances in which it would be appropriate to do so.'

Minor changes were also made to the Code in April 2016, effective for financial years beginning on or after 17 June 2016. This update has been implemented predominantly to reflect the requirements of the new EU Regulation (537/2014) and Directive (2014/56), which prescribe more robust provisions to protect auditor independence in public interest entities (meaning large listed companies and insurance and banking companies). Provision C.3 of the Code on audit committees has been updated accordingly.

In November 2016, the government published a Green Paper on corporate governance reform. The consultation focused on proposals designed to:
- increase shareholder engagement on the subject of executive remuneration;
- enhance interaction between the board and stakeholders in the company; and
- strengthen corporate governance and reporting standards in the largest private companies.

The government is analysing feedback from the consultation process, while the FRC has since announced that it will be carrying out a fundamental review of the Code in 2017. Consultation on the FRC's proposals will begin later in 2017, based on the outcome of its review and the government's response to the Green Paper.

The Code is supplemented by the following published guidance, and it is considered good practice to comply with this guidance, although it has no formal status:
- FRC Internal Control: Guidance for Directors (formerly known as the Turnbull Guidance), which assists companies in complying with the internal control requirements of the Code (namely section C.2);
- FRC Guidance on Audit Committees, which was updated by the FRC in December 2010, September 2012 and April 2016;
- FRC Guidance on Board Effectiveness, which replaced the Good Practice Suggestions from the Higgs Report following a review undertaken by the Institute of Chartered Secretaries and Administrators (ICSA) and was last updated on March 2011; and
- FRC Guidance on Risk Management, Internal Control and the Going Concern Basis of Accounting.

The Guidance on Board Effectiveness was published in March 2011 in order to assist companies in applying the Code, primarily sections A and B on leadership and effectiveness. The Guidance on Board Effectiveness is not intended to be prescriptive and it is intended as a means of stimulating thought on board governance. Areas that the Guidance on Board Effectiveness address are:
- the role of the board and directors;
- board support and the role of the company secretary;
- decision-making;
- board composition and succession planning;
- evaluating the performance of the board and directors;
- audit, risk and remuneration; and
- relations with shareholders.

The UK Stewardship Code (the Stewardship Code)

The FRC first published the Stewardship Code on 2 July 2010, and it came into immediate effect. This version of the Stewardship Code was replaced by a new version published on 28 September 2012 and effective from 1 October 2012. The Stewardship Code is applicable to those firms who manage assets on behalf of institutional shareholders, including pension funds, insurance companies, investment trusts and other collective investment vehicles. The Stewardship Code, like the Code, operates a 'comply or explain' approach and the FRC recommends that a company publishes a statement of compliance on its website. At present, there is no requirement to disclose whether or not a relevant company has complied with the Stewardship Code principles, though this is being reviewed. However, all institutional investors are encouraged to observe the Stewardship Code and to observe the 'comply or explain' approach, on the same basis as asset managers. The Stewardship Code is complementary to the Code and replaced Schedule C of the Code, which was removed with effect from 1 August 2010. The intention of the Stewardship Code is to promote greater engagement between institutional shareholders and company boards and to encourage greater transparency about the way in which institutional investors oversee the companies they own. The FRC believes that good governance is underpinned by high quality dialogue between boards and investors. The principles of the Stewardship Code are that institutional investors should:
- publicly disclose their policy on how they will discharge their stewardship responsibilities;
- have a robust policy on managing conflicts of interest in relation to stewardship which should be publicly disclosed;
- monitor their investee companies;
- establish clear guidelines on when and how they will escalate their stewardship activities;
- be willing to act collectively with other investors where appropriate;
- have a clear policy on voting and disclosure of voting activity; and
- report periodically on their stewardship and voting activities.

The Stewardship Code is based upon the Code on the Responsibilities of Institutional Investors, published by the Institutional Shareholders' Committee, which is discussed further below.

In December 2011, the FRC published a report on the impact and implementation of the Code and the Stewardship Code, revealing a broadly positive reception to the Stewardship Code. The later published version of the Stewardship Code, which applies to relevant companies with accounting periods beginning on or after 1 October 2012, does not represent a change in policy or direction, but attempts to create a common understanding of the term 'stewardship', with greater clarity on the roles and responsibilities of asset owners and managers. The revised Stewardship Code also takes into account changes in market practice, such as the issuance of standards on assurance reports, and the FCA's requirement that firms authorised to manage funds on behalf of others disclose the nature of their commitment to the Code.

In 2016, the FRC introduced a tiering system, whereby signatories to the Stewardship Code are categorised according to the quality of their statements, in an effort to improve standards of reporting against the seven principles. The FRC believes that the quality of reporting has improved substantially as a result of the exercise. In November 2016, of the nearly 300 signatories to the Stewardship Code, over 120 were placed in the highest tier (of three for asset managers and two for other signatories), representing an increase from approximately 40 at the beginning of the exercise. Although those with weaker reporting standards are encouraged to engage with the FRC to discuss improvements, asset managers who have not achieved at least Tier 2 status by mid-2017 are set to be removed from the signatory list, as their reporting fails to demonstrate the level of commitment expected by the FRC to the objectives of the Stewardship Code.

City Code on Takeovers and Mergers (the Takeover Code)
The Takeover Code regulates takeovers and mergers of certain companies in the UK, the Isle of Man and the Channel Islands, including companies whose shares are listed on the LSE. It consists of six general principles that set out the standards of behaviour expected of companies engaged in a merger or takeover and 38 rules (with accompanying notes), which expand on the general principles and provide detailed guidance on the conduct of takeovers and mergers.

Broadly, the aim of the Takeover Code is to ensure that:
- shareholders of the same class in a target company are treated equally and have adequate information so that they can reach a properly informed decision about whether to approve the proposed takeover or merger;
- a false market is not created in the securities of the offeror or the target company; and
- the management of the target company do not take any action that would frustrate an offer for that company without the consent of its shareholders.

The Takeover Code has statutory force and the Panel on Takeovers and Mergers (Takeover Panel) has statutory powers in respect of transactions to which the Takeover Code applies. Breach of any Takeover Code rules that relate to the consideration offered for a target company could lead to the offending party being ordered to compensate any shareholders who have suffered financial loss as a result of this breach. A person who breaches any Takeover Code rules relating to the content requirements of offer documents and response documents may be guilty of a criminal offence and liable to a fine (subject to certain exceptions) (CA 2006, section 953(2), (3), (4) and (6)). The Takeover Panel may also issue rulings compelling parties who are in breach of the Takeover Code to comply with its provisions. Such rulings are enforceable by the court (CA 2006, section 955(1)). In addition, the Takeover Panel may require a party who is in breach of the Takeover Code to remedy such breach and may withdraw or impose conditions on any exemption from the Rules that it has granted and issue a private or public reprimand to companies in respect of any breach.

Institutional investor guidelines
Bodies representing institutional investors, most notably the Association of British Insurers (ABI) and the Pensions and Lifetime Savings Association (PLSA) (until October 2015 known as the National Association of Pension Funds (NAPF)), issue guidelines to their members advising them how to vote in relation to certain resolutions proposed by companies. The ABI, for example, has published guidelines relating to the level of authority to allot shares that should be granted to directors, which it updated in December 2009. The ABI's Investment Affairs division merged with the Investment Management Association (IMA) on 30 June 2014 to form a body called, since January 2015, the Investment Association (IA). Before it was renamed, the enlarged IMA issued updated guidelines on share capital management in July 2014. The Pre-Emption Group, a body consisting of listed companies and their investors, has issued guidance as to how its members should vote on resolutions to disapply shareholders' pre-emption rights. This guidance, originally published in May 2006, was updated in July 2008 and again in March 2015.

The PLSA's corporate governance policy and voting guidelines (the PLSA Guidelines) aim to assist its members to interpret the Code when considering how to vote on certain resolutions proposed by the company. The PLSA Guidelines are updated on a regular basis to reflect amendments made to the Code, and the most recent PLSA Guidelines were published in January 2017. The PLSA Guidelines cover the following matters, among others:
- how to vote if the chairman is not sufficiently independent (on appointment);
- the separation of the role of the chairman and the chief executive officer (and how shareholders should vote if these roles are not properly divided);
- the independence of non-executive directors;
- how shareholders should vote if the board contains insufficient non-executive directors;
- how shareholders should vote if the company's audit, remuneration and nomination committees are improperly constituted;
- how to vote if a company fails to properly disclose its strategic objectives or fails to properly report on its risk management and internal control principles;
- the processes that a company should have in relation to appointments to the board, including the need to disclose its diversity policy and its application of that policy;
- how to vote in relation to the remuneration report and new share scheme proposals;
- the re-election of directors;
- the ability of companies to hold meetings at short notice;
- how to vote when a company fails to comply with the Code and does not provide an adequate explanation;
- how shareholders should vote on proposed changes to the company's memorandum and articles of association;
- how shareholders should vote if their approval is not sought for final dividends;
- how shareholders should vote on share issues and share purchases;
- how to vote if shares have been issued in excess of the Pre-Emption Group guidelines; and
- the payment of political donations.

The PLSA notes the growing trend towards shareholder resolutions in recent years and encourages their use only where engagement has failed.

In October 2009, the ABI Investment Committee published updated guidance on various provisions that it believes public companies should include in their articles of association. This guidance covers the following areas, among others: corporate representatives; directors' fees (the guidance recommends that a company's articles of association should contain a cap on the fees paid to directors); and penalties for shareholders who fail to comply with CA 2006, section 793 (which relates to notice given by a company requiring information about interests in its shares). The ABI published a position paper in relation to directors' remuneration on 15 December 2009, and a full set of Principles of Remuneration in September 2011, following the implementation of the Code. These Principles were updated in November 2013 to reflect changes to the CA 2006 (see question 28), and following the merger of the ABI's Investment Affairs division with the IMA were updated in October 2014 and again in November 2015 under the IA name. These Principles set adherence to the CA 2006, the LRs and the Code as a minimum standard to be followed, and call for remuneration policies to be set up so as to promote value-creation through transparent alignment with the agreed corporate strategy. They call for remuneration principles to have a long-term focus and incentive structures to be based on a similar approach. It is advised that attention be paid to market environment, company performance, and the possibilities of divergence between executive and shareholder interest in relation to remuneration strategy. Further, in September 2011, the ABI had also published a paper on Board Effectiveness, highlighting the need for succession planning, and diversity on boards, and setting out best practice in this regard, including reporting and monitoring progress. This paper was also updated in December 2012 to reflect additions made to the new Code.

The ABI and the then NAPF also issued a joint statement entitled 'Best Practice on Executive Contracts and Severance', which was last updated in February 2008.

In November 2009, the Institutional Shareholders' Committee, of which the ABI and the PLSA were members, published its Code on the Responsibilities of Institutional Shareholders (ISC Code). The ISC Code is based on a statement of principles that was originally published by the ISC in 2002 and revised in 2007. The statement of principles highlights the corporate governance duties of institutional investors in relation to the companies in which they invest, and these principles are supplemented by additional guidance. The ISC Code operates on a 'comply or explain' basis. The principles of the ISC Code that institutional investors should adhere to have been largely replicated in the Stewardship Code, and for that reason they are not repeated here. The Institutional Shareholders' Committee was renamed and reconstituted as the Institutional Investor Committee on 18 May 2011 and was dissolved in 2014 after the merger of the Investment Affairs division of the ABI and the IMA.

The ICSA, although not a body representing institutional investors, is an important authority on corporate governance. It has published guidance on a range of corporate governance matters including corporate representation at general meetings, matters reserved for the board, voting at general meetings and model terms of reference for audit, remuneration and nomination committees. Its terms of reference for audit committees were updated in June 2013 (see question 25). On 16 April 2012, the ICSA Registrars Group published guidance on the practical issues of voting at general meetings. The aim of the guidance is to address the perceived misconceptions in the market regarding management of general meetings, and it covers areas such as proxy voting, notice of meetings and voting periods. The guidance recommends, among other things, that all issuers with CREST shareholders announce meetings via CREST, encourages electronic voting, and states best practice for proxy voting. The ICSA also launched a consultation document in October 2012 on stewardship titled 'Improving Engagement Practices by Companies and Institutional Investors' designed to examine the efficiency of investor-director communications. On 14 March 2013, the ICSA published its guidance 'Enhancing Stewardship Dialogue'. This guidance provides four key messages for how to improve engagement practices: the need to develop an engagement strategy; the importance of getting housekeeping issues right; strengthening the conversation on strategy and long-term sustainable performance; and providing feedback in a way that adds value for all participants. In April 2015, the ICSA published guidance on Code provision E.2.4 (relating to the notice requirements for AGMs and other general meetings) and on good practice and the required contents of annual reports. Finally, it is anticipated that, jointly with the IA, the ICSA will in 2017 publish practical guidance aimed at assisting boards to understand and engage effectively with the views of employees and other stakeholders.

The Pensions Investments Research Consultants (PIRC) is an independent body that publishes guidance of relevance to institutional investors. The PIRC's UK Shareholder Voting Guidelines, published yearly, set out its views on issues such as board structure, remuneration policy and the management of social and environmental issues, applying these to the listed companies it covers in the UK market. Notably, the 23rd edition of the Guidelines, published in 2016, gave support for the recommendation in Lord Davies' final report on improving gender balance on boards. The report, which was published on 29 October 2015, recommends that a target of 33 per cent of board positions in FTSE 350 companies be held by women by 2020. The 2017 version of the Guidelines reiterates this position, and states that the PIRC will not support the re-election of a nomination committee of a FTSE 350 company where current female representation on the board falls below these expectations, and there are no clear and credible proposals for reaching these objectives.

In January 2015, Institutional Shareholder Services (ISS) published its first stand-alone UK and Ireland Proxy Voting Guidelines: 2015 Benchmark Policy Recommendations. These guidelines constitute a codification and update of ISS' approach and align with the NAPF Guidelines but do not represent a materially different approach to the previous one.

The guidance issued by bodies representing institutional investors does not have statutory force but failure to comply with it could lead to institutional investors voting against any resolutions proposed by it or selling their shares in the company.

Articles of association

A company's articles of association will contain provisions as to what its directors may and may not do in respect of the company. Directors who do not comply with the provisions of their company's articles of association may be in breach of their statutory duty to act within their powers under CA 2006, section 171. A company may place additional corporate governance requirements on the board of directors, beyond the scope of CA 2006 and the statutory framework.

European legislation

In May 2003, the European Commission released an action plan on company law and corporate governance (entitled 'Modernising Company Law and Enhancing Corporate Governance in the EU'). The action plan's main objectives are to strengthen shareholders' rights and protection for third parties who deal with companies and to encourage companies to improve their efficiency and competitiveness.

A number of corporate governance measures have already been implemented under the action plan, including:

- the Company Reporting Directive (2006/46) (which has been implemented in the UK by DTR7);
- the Shareholder Rights Directive (2007/36) (which was implemented in the UK on 9 July 2009 by the Companies (Shareholders' Rights) Regulations 2009 (SI 2009/1632) (the Shareholders' Rights Regulations);
- a recommendation aimed at enhancing the role of non-executive directors; and
- a recommendation aimed at giving shareholders greater control over directors' remuneration (which has been implemented in the UK by the Directors' Remuneration Report Regulations 2002 (SI 2002/1986) and schedule 8 of the Large and Medium-sized Companies and Groups (Accounts and Reports) Regulations 2008 (SI 2008/410)).

At present, the EU does not intend to introduce its own corporate governance code but hopes that the measures implemented under the action plan will increase consistency between national corporate governance codes. The European Commission published a Green Paper on 5 April 2011 and launched a consultation into the effectiveness of the existing EU corporate governance framework for listed companies, with a view to improving the way in which companies are run. The questions in the Green Paper deal with issues of executive remuneration, diversity, risk management, shareholder cooperation and minority-shareholder protection. A feedback statement summarising the results was published in January 2012, and a non-legislative resolution was adopted by the European Parliament in March 2012, which, among other things, welcomed the European Commission's proposed revision of the EU corporate governance framework initiated by the Green Paper of April 2011.

Also in March 2012, the European Commission published a consultation paper on gender imbalance in corporate boards in the EU, which resulted in the publication of a proposal for a directive on improving gender balance among corporate boards of listed companies in November 2012. In November 2013, the European Parliament adopted the directive (with amendments), which, among other things, sets an objective for listed companies to increase non-executive directors of the under-represented sex (usually women) to 40 per cent by 1 January 2020 (see question 23).

In December 2012 the European Commission published an additional action plan on European company law and corporate governance, which included proposals such as:

- amending the Accounting Directive to increase disclosure of company board diversity policies and non-financial risks;
- creating an initiative to improve corporate governance reports, focusing specifically on the quality of explanations to be provided by companies departing from the corporate governance code of their jurisdiction;

- new legislation to improve visibility of listed company shareholdings;
- creating new initiatives, for example, by amending the Shareholder Rights Directive: to improve disclosure of voting and engagement policies and voting record by institutional investors; to improve transparency on remuneration policies and grant shareholders a vote on remuneration policy and the remuneration report; to improve shareholder control of related-party transactions; and to improve the transparency and conflict of interest frameworks applicable to proxy advisers; and
- increasing legal certainty on shareholder cooperation concerning concert party issues.

The European Commission has started to implement these proposals.

- In April 2014, the European Commission proposed a directive to amend the Shareholder Rights Directive (2007/36), with the aim of further encouraging shareholder engagement and corporate transparency. The proposed legislation is yet to be properly ratified.
- In April 2014, the European Commission adopted a draft recommendation on the quality of corporate governance reporting.
- In December 2014, the European Commission implemented Directive (2014/95) on disclosure of non-financial and diversity information (amending the Accounting Directive); it had to be transposed by member states into national legislation by 6 December 2016. This requires certain large companies to disclose relevant environmental and social information in the management report, and was implemented in the UK by the new DTR 7.2.8A (see question 23 and 'Update and trends').

The United Kingdom voted to leave the European Union on 24 June 2016 and triggered the negotiation process for withdrawal on 29 March 2017. It is too early to speculate on the potential consequences for corporate governance in the United Kingdom but with effect from 29 March 2019, the United Kingdom will cease to be a member of the European Union and will cease to be bound by European legislation, except to the extent that European legislation has been incorporated into domestic legislation and not repealed.

2 Responsible entities

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

Until 1 April 2013, the FSA was responsible for regulating the UK's financial services industry and was also the competent authority for the purposes of FSMA 2000 part IV, which relates to the listing regime (although it was referred to as the United Kingdom Listing Authority (UKLA) in this capacity). The UKLA was responsible for, among other things, maintaining the Official List and administering the LPDT Rules. However, as a response to the perceived failings of this regulatory regime in preventing the financial crisis, the government enacted The Financial Services Act 2012, abolishing the FSA and replacing it with a new UK financial regulation regime consisting of three separate entities: the Financial Conduct Authority, the Financial Policy Committee and the Prudential Regulation Authority. The Financial Services Act 2012 received Royal Assent on 19 December 2012, and the majority of its provisions came into force on 1 April 2013. Pursuant to the legislation:

- the Financial Policy Committee is a macro-prudential authority within the Bank of England;
- the Prudential Regulation Authority (PRA) is a micro-prudential regulator with responsibility for ensuring effective prudential regulation of banks, insurers and designated investment firms; and
- the FCA is a conduct of business regulator and the micro-prudential regulator of firms not supervised by the PRA. The FCA also includes the UKLA function and is responsible for enforcing the market abuse regime. The FSMA, as amended by the Financial Services Act, continues to be the principal piece of financial services legislation in the UK.

The Takeover Panel is responsible for administering the Takeover Code (see question 1). It has various duties and powers conferred by CA 2006, chapter 1 of part 28 and by the Takeover Code itself. The Takeover Panel has the power to make rules allowing it to modify or dispense with certain Takeover Code provisions in particular cases (CA 2006, section 944(1)(d)). The Takeover Panel therefore has a degree of freedom to decide how to apply the Takeover Code, notwithstanding that this code now has statutory force.

Other entities that play a significant role in corporate governance include the FRC (which is responsible for administering the Code) and various bodies representing institutional investors and other parties with an interest in the operation of UK-listed companies, including the PLSA, IA, ICSA and PIRC (see question 1).

The rights and equitable treatment of shareholders

3 Shareholder powers

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

Shareholders can appoint directors to the board by way of an ordinary resolution (that is, a resolution that requires a simple majority of shareholders to vote in favour of it) passed at a general meeting. If more than one director is to be appointed, separate resolutions must usually be passed in respect of each appointment, unless a resolution permitting a single resolution is passed (CA 2006, section 160(1)). If a company's articles of association provide that the board may appoint a director, such an appointment must usually be approved by an ordinary resolution at the company's next annual general meeting (AGM) (Code, provision B.7.1). In addition, directors of FTSE 350 companies are expected to be put up for annual re-election by shareholders (Code, provision B.7.1). This latter requirement is likely to focus directors on the concerns of the company's shareholders, though as with all provisions of the Code, companies do not strictly have to comply with this requirement as long as they explain the reasoning behind any decision not to comply.

Shareholders can also remove directors by way of an ordinary resolution under CA 2006, section 168(1), notwithstanding any provision to the contrary in any agreement between the company and the director. Special notice (notice given at least 28 days before the general meeting of the company at which the resolution will be considered) of a proposed resolution to remove a director must be given to the company by the shareholders proposing that resolution (CA 2006, sections 168(2) and 312(1)). The board must then decide whether to place the resolution on the agenda of the company's next general meeting. If the resolution is placed on the agenda, the company must notify its shareholders of this in the same manner and at the same time as it gives them notice of the general meeting (CA 2006, section 312(2)). If this is not practicable, the company must notify its shareholders of the resolution at least 14 days before the general meeting through an advertisement in a newspaper with appropriate circulation or in any other manner allowed by its articles of association (CA 2006, section 312(3)).

The company must notify a director of any proposed resolution to remove him or her (CA 2006, section 169(1)). Any written representations made by the director in respect of his or her proposed removal should, at the request of that director, be circulated to shareholders or, failing this, be read out at the general meeting at which the resolution is to be considered (CA 2006, sections 169(3) and (4)). The director, whether or not he or she is a shareholder of the company, also has the right to be heard on the resolution at the general meeting (CA 2006, section 169(2)). The director may be entitled to compensation if his or her removal from office pursuant to CA 2006, section 168(1) amounts to a breach of the terms of his or her service contract (CA 2006, section 168(5)(a)).

Many listed companies require their directors to retire and present themselves for re-election not less than every three years in accordance with provision B.7.1 of the Code, and many companies have included this requirement in their articles of association. Companies are also able to comply with the annual re-election requirement without making this compulsory under their articles of association. There is an additional dual voting requirement for electing independent directors where a listed company has a controlling shareholder. Indeed under the Listing Rules the election of independent directors must be approved by a vote of all shareholders, as well as a separate vote of the independent (ie, non-controlling) shareholders only (LR9.2.2ER). However, if either vote is defeated, the company may propose a single further vote of all shareholders to elect the proposed independent directors after waiting for at least 90 days (LR9.2.2FR). In such circumstances, a separate vote of independent shareholders is not required. The effect is to impose a 90-day 'cooling off' period to allow shareholders to engage in discussions to try to reach a solution acceptable to both the controlling and independent shareholders. However, if the controlling shareholder is not minded to accept a compromise candidate, it will be able to use its voting power to support the election of its chosen independent director.

Shareholders have the right to requisition meetings of the company to deal with matters that they wish to be considered and have historically used this power to require resolutions to be put for the purpose of removing or appointing directors (see question 7 for further information on shareholders' power to requisition meetings). Shareholders may also compel the board to pursue a particular course of action by passing a special resolution (that is, a resolution requiring at least three-quarters of shareholders to vote in favour of it), which either alters or overrides the company's articles of association (CA 2006, section 21(1)).

4 Shareholder decisions

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

Shareholder approval is required in respect of many matters. Such matters include the following.

Alterations to the company's articles of association
A company's articles of association may only be amended by way of special resolution passed by its shareholders (CA 2006, section 21(1)).

Change of name
In order for a company to change its name, it is necessary for the shareholders to pass a special resolution (CA 2006, section 77(1)(a)). This is subject to the company's articles of association allowing the company to change its name by other means (CA 2006, section 77(1)(b)). Many companies' articles of association therefore permit the board to change the name of the company, although some shareholder groups do not approve of the board having such power.

Re-registration of a public company as private limited company
In order for a public company to re-register as a private company, the shareholders must pass a special resolution to that effect (CA 2006, section 97(1)). This is subject to certain other conditions being satisfied.

Takeovers
A company that is subject to the Takeover Code may only be acquired by another company if shareholders holding at least 50 per cent of the voting rights in the target company agree to sell their shares to the offeror, although in exceptional circumstances the Takeover Panel may be willing to waive this requirement subject to prior consultation and appropriate safeguards (Takeover Code Rule 10). In certain cases, shareholders holding more than 50 per cent of the voting rights in the company may need to consent to the takeover (for instance, a condition that shareholders holding 90 per cent of the voting rights in the company must consent to the takeover is often imposed, in order to allow the offeror to take advantage of certain provisions relating to the acquisition of minority shareholders' interests) (see question 13).

Class 1 transactions
The Listing Rules require companies with premium listings to classify certain transactions by comparing the size of the proposed transaction with the size of the company. This classification requires specific tests (relating to the gross assets, profits, the consideration payable and gross capital of the company) to be applied to the proposed transaction, which result in a percentage ratio. The purpose of this classification is to ensure that shareholders are informed of certain transactions entered into by the company, and to enable shareholders to vote on larger proposed transactions (LR10.1.2G). If any of the tests produces a ratio of 25 per cent or more the transaction will be a class 1 transaction for the purposes of the LRs and shareholder approval must therefore be obtained in a general meeting before the transaction can proceed (LR10.5.1R and annex 1 to LR10). Any agreement giving effect to a class 1 transaction should be conditional on shareholder approval being obtained (LR10.5.1R(3)).

Related-party transactions
A company with a premium listing may only enter into a transaction with certain related parties if authorised to do so by its shareholders (LR11) (see question 36). Related parties include the company's directors and substantial shareholders (defined as those controlling more than 10 per cent of the voting rights of the company, disregarding those voting rights held for a period of five trading days or less, during which the voting rights are not exercised and no attempt is made to exert influence on the management (see question 36)). The related party and its associates must not vote on the resolution to authorise the proposed transaction (LR11.1.7R(4)). The object of these safeguards is to prevent a related party from taking advantage of its position, and also to prevent any perception to that effect (LR11.1.2G(2)).

Allotment of shares
A director must not allot shares, nor grant rights to subscribe for or to convert any security into shares, unless authorised to do so by the company's articles of association or by an ordinary resolution passed by its shareholders (subject to certain exceptions) (CA 2006, sections 549(1) and 551(1)). Any such resolution must state the maximum amount of shares that may be allotted under it and specify the date on which it will expire, which must not be more than five years from the date on which the resolution was passed (CA 2006, section 551(3)). Shareholders may renew, revoke or vary this authorisation by a further resolution (CA 2006, section 551(4)). Such a renewing resolution must state the maximum amount of shares that may be allotted under the authorisation, or the amount remaining to be allotted under it, and specify the date on which the renewed authorisation will expire (CA 2006, section 551(5)). If a director fails to comply with these provisions they may be guilty of an offence and liable to a fine (CA 2006, section 549(5)). It is also necessary for a copy of the resolution to be forwarded to the Registrar of Companies House within 15 days after it is passed, and failure to do this will also result in the company and its officers committing an offence (CA 2006, sections 551(9) and 30).

Disapplication of pre-emption rights
A company's shareholders may, by way of special resolution, authorise a director who is generally authorised to allot shares under CA 2006, section 551 to allot such shares as if their rights of pre-emption (that is, rights of first refusal of any freshly issued shares in the company) under CA 2006, section 561 did not exist (CA 2006, section 570(1)). Shareholders may also resolve by way of special resolution that CA 2006, section 561 may be disapplied only in respect of a specified allotment of shares, or applies to such allotment with such modifications as may be specified in the resolution (although such a resolution may only be passed if recommended by a director in accordance with CA 2006, sections 571(5) to (7)) (CA 2006, section 571(1)) (see question 11).

Variation of class rights
If a company's articles of association do not contain any provisions as to how the rights attaching to a particular class of shares may be varied, then those rights may only be varied if the written consent of the holders of at least three-quarters in nominal value of such shares is obtained, or a special resolution approving such variation is passed at a separate general meeting of the holders of such shares (CA 2006, sections 630(2) and (4)).

Reduction of share capital
A public company that wishes to reduce its share capital may only do so by way of a special resolution passed by its shareholders that is confirmed by the court (CA 2006, section 641(1)(b)).

Alteration of share capital
A company may sub-divide, consolidate and redenominate its shares, or reconvert its shares into stock only if authorised to do so by a shareholder resolution, subject to certain rules and exceptions (CA 2006, sections 617 to 628). A company may purchase its own shares, provided

that after such purchase there are still members who hold shares other than redeemable shares (CA 2006, section 690 (1) and (2)).

A public company may purchase its own shares either 'on-market' (that is, on a recognised investment exchange) or 'off-market' (CA 2006, section 693) by way of an ordinary shareholder resolution (CA 2006, sections 701(1) and 694(2) respectively). It should be noted that private companies are able to purchase their own shares out of capital in certain circumstances, whereas public companies are not able to do this (CA 2006, sections 692 (1) and 709 to 722).

Ratification of directors' conduct

Shareholders may ratify conduct by a director that would otherwise amount to negligence, default or breach of duty or trust by way of ordinary resolution (unless the company's articles of association require a higher majority of shareholders to approve the resolution) (CA 2006, section 239(1) and (2)). The resolution must be passed without including any votes attached to shares held by the director whose conduct is being ratified or by any person connected with him or her, as defined in CA 2006, section 252 (CA 2006, section 239(4)) (see question 32 for further information on the ratification of directors' conduct).

Directors' service contracts

Shareholder approval is required for any director's service contract, which is, or may be, for a period in excess of two years (CA 2006, sections 188(1) and (2)) (see question 28).

Transactions with directors

A company may not enter into substantial property transactions with its directors or their connected persons (as defined in CA 2006, section 252), nor may it make loans or quasi-loans to its directors or their connected persons, nor enter into credit transactions with its directors or their connected persons, unless authorised to do so by way of an ordinary resolution of its shareholders, subject to certain rules and exceptions (CA 2006, sections 190 to 214) (see question 28).

Directors' remuneration report and policy

A quoted company with a financial year ending before 30 September 2013 was required to give its shareholders the opportunity to pass an ordinary resolution to approve its directors' remuneration report at the general meeting of the company before which its annual accounts for the year were to be laid (CA 2006, section 439(1) and (4)). The vote was advisory only and the directors' remuneration was not conditional upon such a resolution being passed (CA 2006, section 439(5)). For quoted companies with financial years ending on or after 30 September 2013, the directors' remuneration reports are now required to be prepared and put to the shareholders in two distinct parts:

- the annual report on remuneration, which sets out remuneration payments made to directors in the year under review and a statement describing how the company intends to implement the approved remuneration policy in the next financial year. This report is required annually and is subject to an advisory vote; and
- the directors' remuneration policy setting out the company's policy on remuneration of directors. This is subject to a binding shareholder vote at least every three years (CA 2006, section 439A(1)). Once the policy is approved, the company is not permitted to make remuneration payments to a person who is (or is to be or has been) a director unless the payment is consistent with the approved policy (CA 2006, section 226B). Any payments that are inconsistent with the remuneration policy must be otherwise approved by shareholders (CA 2006, section 226B) (see question 37).

Payment to a director for loss of office

If a company wishes to make a payment to a director or past director to compensate him or her for loss of office, for example due to retirement, then the shareholders must authorise such a payment by way of an ordinary resolution (CA 2006, sections 215 and 217). This is subject to certain other requirements.

For quoted companies, the new framework on directors' remuneration requires any loss of office payments to be consistent with the approved remuneration policy (described above) or separately approved by a shareholder resolution (CA 2006, section 226C).

Appointment of auditors

The directors of a newly incorporated company, or of a company in respect of which the role of auditor has become vacant, will appoint an auditor before the annual general meeting at which the company's accounts for the relevant financial year are considered (CA 2006, section 489(1) to (3)). A company's articles of association may impose restrictions on its ability to act without first obtaining shareholder approval.

The company's shareholders may appoint an auditor at the 'accounts meeting' (usually the annual general meeting (AGM)), if the company should have appointed an auditor but failed to do so or where the directors had the power to appoint an auditor under CA 2006, section 489(1) to (3) but failed to do so.

5 Disproportionate voting rights

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

UK listed companies may issue classes of shares with different voting rights if their articles of association permit such an issue, but the UKLA will not grant such companies a listing (although it will admit companies with non-voting preference shares to standard listing but not premium listing). A few companies that have shares with different voting rights and were listed many years ago still exist but are disappearing. The general rule, therefore, is 'one share, one vote'. The UK investment community is particularly averse to structures that deliberately block takeover bids ('poison pills'). An issue of disproportionate voting rights is one means of challenging a takeover bid, and the UKLA and the Takeover Panel would object to such a structure.

The FCA consulted on (in its consultation paper CP12/25), and decided to proceed with (as expressed in CP13/12, its feedback to CP12/25), a new listing principle requiring all equity shares of a class admitted with a premium listing to carry an equal number of votes, as implemented in May 2014 under a revised LR7.2.1.

6 Shareholders' meetings and voting

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

All ordinary shareholders of a company have a right to receive notice of and to attend and vote at its general meetings. An AGM of a public company that is not a traded company must be called by notice of at least 21 days, while any other company meeting must be called by notice of at least 14 days, unless the company's articles of association require a longer notice period than this (CA 2006, section 307(A1)(a), (2) and (3)). A meeting of a public company that is not an AGM may be called by shorter notice than that otherwise required if its shareholders agree to this (CA 2006, section 307(4) to (7)). These provisions also apply to a traded company that is an opted-in company (as defined by CA 2006, section 971(1)) in certain circumstances set out in CA 2006, section 307(A1)(b).

CA 2006, section 307A provides that the default notice period for general meetings of traded companies (which includes companies that trade on the LSE) may be reduced from 21 days to 14 days provided that certain conditions are met. However, the notice period for an AGM of a traded company may not be reduced in this way (CA 2006, section 307A(2)). The company's articles of association may provide for a longer notice period (CA 2006, section 307A(6)).

The Code recommends that companies to which it applies give at least 20 working days' notice of an AGM and 14 working days' notice of any other general meeting (Code, provision E.2.4).

A shareholder may appoint a proxy to exercise his or her rights to attend, speak and vote at meetings of the company on his or her behalf (CA 2006, section 324(1)). A shareholder may appoint more than one proxy, although each proxy must exercise their powers in respect of a different share, or a different £10 or multiple of £10 of stock held by that shareholder (CA 2006, section 324(2)). However, a company's articles of association may permit shareholders to appoint more proxies than would be possible under CA 2006, section 324(2).

In relation to a meeting of a traded company, the appointment of a proxy must be notified to the company in writing by the relevant shareholder (CA 2006, section 327(A1)(a)). The company may also require certain evidence to be provided in respect of the appointment of the proxy (CA 2006, section 327(A1)(b)). Shareholders must notify the company of any proxy appointments before any cut-off point set by the company. However, the company may not make this cut-off point earlier than:

- in the case of a meeting or adjourned meeting, 48 hours before the relevant meeting; and
- in the case of a poll taken more than 48 hours after it was demanded, 24 hours before the time appointed for the taking of the poll.

CA 2006 has enhanced the rights enjoyed by proxies under the Companies Act 1985 as follows:

- proxies now have a right to speak, rather than to simply attend and vote, at general meetings of the company (CA 2006, section 324(1));
- proxies now have an automatic right to one vote on a show of hands, rather than only having an automatic right to vote on a poll (CA 2006, section 285(1));
- on a vote on a show of hands, a proxy will have one vote for and one vote against a resolution if they have been appointed by more than one shareholder and have been instructed by one or more of those shareholders to vote for a resolution and by one or more of those shareholders to vote against it (CA 2006, section 285(2));
- if a shareholder appoints multiple proxies, each will have one vote on a show of hands (CA 2006, sections 285(1) and 324(2)); and
- on a poll, all or any of a shareholder's voting rights may be exercised by one or more proxies (CA 2006, section 285(3)).

Sections 285(1) and (2) are subject to any provisions of the company's articles (CA 2006, section 285(5)).

Shareholders that are companies have the right to appoint one or more individuals to act as their corporate representatives at company meetings as an alternative to appointing proxies (CA 2006, section 323(1)). It is not necessary to notify the company of the appointment of a corporate representative, although evidence of the corporate representative's authority will be required when voting at a general meeting. Corporate representatives are able to exercise all the powers that the corporate shareholder could exercise if it were an individual member of the company and may therefore: speak at a general meeting; vote on both a poll and on a show of hands; and appoint a proxy if permitted to do so by the corporate shareholder (CA 2006, section 323(2)).

If two or more corporate representatives appointed by the same corporate shareholder purport to exercise that shareholder's powers in relation to the same shares, in conflicting ways, then that power will be treated as not having been exercised (CA 2006, section 323(4)(b)).

On 2 February 2010, the PIRC published best-practice principles for proxy voting and voting advisory organisations to encourage such organisations to be more open and accountable. The latest version of the advice was published in March 2014.

Shareholders of a private company can also pass written resolutions that would have the effect of resolutions passed by the company in a general meeting (CA 2006, section 288), except for resolutions to remove either a director or auditor before the expiry of their term which would require a general meeting to be held. The resolutions can be proposed by either the directors or the shareholders. It is not, however, possible for shareholders of a public company to pass a resolution without a meeting. A resolution of the shareholders of a public company must be passed at a meeting of the shareholders (CA 2006, section 281(2)).

Subject to any restrictions found in a company's articles, there is no statutory prohibition on holding electronic or 'virtual' meetings by, for example, teleconference. A company holding such a meeting need only ensure that persons who are not present together at the same place may by electronic means attend and speak and vote at it (CA 2006, section 360A(1)). In the case of traded companies, the use of electronic means to enable shareholders to participate in meetings can only be subject to such restrictions and requirements as are necessary to ensure the identification of the participants of the meeting and the security of the electronic communication. Any such restrictions and requirements must be proportionate to the achievement of those objectives (CA 2006, section 360A(2)).

7 Shareholders and the board

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

Shareholders holding at least 5 per cent of the voting rights of a company may require its directors to call a general meeting (CA 2006, sections 303(1) and (2)(a)). Such a request for a general meeting to be called must state the general nature of the business to be dealt with at the general meeting and may include the text of a resolution that the shareholders requesting the general meeting wish to be moved at that meeting (CA 2006, section 303(4)). However, the company's directors may not be required to move the requested resolution at the general meeting if it would be ineffective or if it is defamatory, frivolous or vexatious (CA 2006, section 303(5)). The company's directors must call a meeting requested by its shareholders under CA 2006, section 303 within 21 days from the date on which they became subject to the requirement to call the meeting and the meeting must be held not more than 28 days after the date of the notice convening the meeting (CA 2006, section 304(1)). If the request by the company's shareholders for a meeting to be convened included the text of a resolution, then the notice of the meeting must include notice of the resolution (CA 2006, section 304(2)).

If a company's directors fail to call a meeting requested by its shareholders under CA 2006, section 303 in accordance with the provisions of CA 2006, section 304, then the members who requested the meeting, or any of them holding more than half of the total voting rights of all of them, may themselves call a general meeting (CA 2006, section 305(1)). This meeting must be called for a date no later than three months after the date on which the company's directors became subject to the requirement to call a general meeting (CA 2006, section 305(3)). If the request to the company's directors to call a general meeting included the text of a resolution intended to be moved at that meeting, then notice of this resolution must be included in the notice of the meeting to be called by the shareholders themselves (CA 2006, section 305(2)). This resolution may then be dealt with at such a meeting (CA 2006, section 305(5)). The shareholders calling such a meeting may recover from the company any expenses incurred due to the directors' failure to call the meeting (CA 2006, section 305(6)). These expenses shall be retained by the company out of any sums due or to become due from the company to the directors who were in default (CA 2006, section 305(7)).

Further, a company's shareholders and directors may request the court to call a general meeting if it is impracticable for one to be held otherwise (CA 2006, sections 306(1) and (2)).

The rules relating to public companies and traded companies are somewhat different. Where a public company is concerned, shareholders may require it to give notice of a resolution that is intended to be moved at the next AGM to members of the company entitled to receive notice of that AGM (CA 2006, section 338(1)). The company must give such notice if it receives requests to do so from shareholders holding at least 5 per cent of the total voting rights of all members who have a right to vote on the resolution at the AGM, or from at least 100 members who have a right to vote on the resolution at the AGM and who hold shares on which an average sum of not less than £100 per shareholder has been paid up (CA 2006, section 338(3)). The request must identify the resolution of which notice is to be given, it must be authenticated by the person or persons making the request and it must be received by the company not later than six weeks before the AGM to which the request relates, or if later, the time at which notice is given of that meeting (CA 2006, section 338(4)(b) to (d)). However, the company need not circulate the resolution if it would be ineffective, or if it is defamatory, frivolous or vexatious (CA 2006, section 338(2)).

The company will not be required to comply with a request from shareholders to circulate such a resolution if it does not receive a sum reasonably sufficient to meet the cost of doing so at least six weeks before the AGM, or if later, the time at which notice is given of that meeting (CA 2006, section 340(2)(b)). The shareholders requesting circulation of the resolution will be required to meet these costs unless the company provides otherwise, or requests sufficient to require the company to circulate the resolution are received before the end of the financial year preceding the meeting (CA 2006, section 340(1) and (2)(a)).

Shareholders may require a company to circulate a statement of not more than 1,000 words to shareholders entitled to receive notice of a general meeting in respect of any business to be dealt with at that meeting, including a matter referred to in a resolution to be dealt with at that meeting (CA 2006, section 314(1)). The company must circulate such a statement if it receives requests to do so from shareholders holding at least 5 per cent of the total voting rights of all shareholders who have a relevant right to vote (that is, who have a right to vote on any resolution to which the statement refers or, in respect of any other statement, a right to vote at the meeting to which the request relates), or from no fewer than 100 members with a relevant right to vote and holding shares on which an average sum per shareholder of not less than £100 has been paid up (CA 2006, section 314(2) and (3)). The shareholders' request to circulate a statement must identify the statement to be circulated, it must be authenticated by the person or persons making it and it must be received by the company at least one week before the meeting to which it relates (CA 2006, section 314(4)(b) to (d)).

The public company will not be required to comply with a request from shareholders to circulate a statement if it does not receive a sum reasonably sufficient to meet the cost of doing so at least one week before the company meeting (CA 2006, section 316(2)(b)). The shareholders requesting circulation of a statement will be required to meet these costs unless the company provides otherwise, or the meeting to which the request relates is an AGM and requests sufficient to require the company to circulate the statement are received before the end of the financial year preceding the meeting (CA 2006, section 316(1) and (2)(a)).

Failure by the public company's directors to circulate a statement, if required to do so by CA 2006, section 314, in the same manner as the notice of the meeting and at the same time as, or as soon as reasonably practicable after, it gives notice of the meeting, will constitute an offence (CA 2006, section 315(1) and (3)). However, a company will not be required to circulate a shareholders' statement if it persuades a court that the rights conferred on its shareholders by CA 2006, sections 314 and 315 are being abused (CA 2006, section 317(1)).

Where a traded company is concerned, shareholders may request a traded company to include in the business to be dealt with at an AGM any other business that may properly be dealt with at that meeting other than a proposed resolution (CA 2006, section 338A(1)). The company must include such a matter once it has received requests to do so from shareholders holding at least 5 per cent of the total voting rights of all shareholders who have a right to vote at the meeting, or from at least 100 members who have a right to vote at the meeting and hold shares in the company on which there has been paid up an average sum per member of at least £100 (CA 2006, section 338A(3)). Such a request must identify the matter to be included in the business of the meeting, as well as being accompanied by a statement setting out the grounds for the request being authenticated by the person or persons requesting it (CA 2006, section 338A(4)(b) to (d)). It must be received by the company at least six weeks before the meeting, or if later, the time at which notice is given of the meeting (CA 2006, section 338A(5)). However, a company need not include such business in the business of the company's AGM if it is defamatory, frivolous or vexatious (CA 2006, section 338A(2)).

The traded company will not be required to comply with a request from shareholders to include the relevant business in the business to be dealt with at the company's AGM if it does not receive a sum reasonably sufficient to meet the cost of doing so at least six weeks before the AGM to which the request relates, or if later, the time at which notice is given of that meeting (CA 2006, section 340B(2)(b)). The shareholders requesting the inclusion of such business in the business of the AGM will be required to meet these costs unless the company provides otherwise, or the meeting to which the request relates is an AGM and requests sufficient to require the company to include the business are received before the end of the financial year preceding the meeting (CA 2006, section 340B(1) and (2)(a)).

Failure by the traded company's directors to give notice of any such business to each shareholder entitled to receive notice of the AGM, in the same manner as the notice of the AGM and at the same time as, or as soon as reasonably practicable after, it gives notice of the AGM, will constitute an offence (CA 2006, section 340A(1) and (3)). The company must also publish notice of such business on the same website as that on which the company publishes certain information required by CA 2006, section 311A (CA 2006, section 340A(1)(b)).

8 Controlling shareholders' duties

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

If the rights of non-controlling shareholders are unfairly prejudiced by controlling shareholders voting in accordance with their own self-interest, the non-controlling shareholders may petition the court for a remedy (CA 2006, sections 994 to 999).

Non-controlling shareholders may also bring a claim against controlling shareholders on behalf of the company if an act of the controlling shareholders amounts to a fraud on the non-controlling shareholders. This is an exception to the rule established by the case of *Foss v Harbottle* (1843) 2 Hare 461, in which it was held that the proper claimant in an action for a wrong done to a company is the company itself.

9 Shareholder responsibility

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

Shareholders in a company limited by shares are generally not liable for its debts beyond the amount paid up (or to be paid up) on the shares held by them. However, there are some exceptions to this principle, including that where shareholders know or have reasonable grounds for believing an unlawful distribution has been made to them, they are liable to repay it to the company (CA 2006, section 847(1) and (2)).

Corporate control

10 Anti-takeover devices

Are anti-takeover devices permitted?

Article 11 of the EU Directive on Takeover Bids (2004/25) (Takeover Directive) prevents a company from using certain measures, including restrictions on the transfer of shares and restrictions on voting rights, to defend itself from a takeover bid. The Takeover Directive provides that once a bid for a company is made public, the offeror will be able to override or 'breakthrough' such defensive measures. The Takeover Directive allows member states to opt out of the provisions of article 11, with the effect that companies registered within that member state's territories do not have to apply article 11. However, member states that take this route must give companies the option to opt back in (Takeover Directive, article 12). The UK government has opted out of article 11 but provisions allowing UK traded companies to opt back in by way of special resolution (and to opt back out again by way of special resolution) are set out at CA 2006, sections 966 to 973. The effect of opting in for a UK company is that any pre-bid defensive measures that have been put in place will be invalid once the bid is made public (CA 2006, section 968(1) and (2)).

Companies should also ensure that any anti-takeover devices that they deploy do not breach the following provisions of the Takeover Code and CA 2006:

- the board of a target company must afford the shareholders sufficient time and information to enable them to reach a properly informed decision on the bid; where it advises the shareholders, the board must give its views on the effects of implementation of the bid on employment, conditions of employment and of the company's places of business (General Principle 2 of the Takeover Code);
- the board of a target company must act in the interests of the company as a whole and must not deny the holders of its securities the opportunity to decide on the merits of the bid (General Principle 3 of the Takeover Code);
- the board of a target company must not, without shareholder approval, engage in any 'frustrating action' as set out in rule 21.1 of the Takeover Code;

- each document or advertisement published, or statement made, during the course of an offer must be prepared with the highest standards of care and accuracy and the information given must be adequately and fairly presented (rule 19.1 of the Takeover Code);
- parties to an offer or potential offer (and their advisers) must not make statements that, while not factually inaccurate, mislead shareholders and create uncertainty in the market (rule 19.3 of the Takeover Code) (directors should also be aware of the common law prohibitions against negligent misstatement and the prohibitions against misleading statements contained in the Financial Services Act 2012, sections 89 to 91);
- a target company cannot withhold information about itself from any offeror who requests such information where that information has already been given to any other offeror or potential offeror (rule 21.3 of the Takeover Code);
- a director must act in accordance with the company's constitution and only exercise his or her powers for the purpose for which they are conferred (CA 2006, section 171); and
- a director must act in the way he or she considers, in good faith, would be most likely to promote the success of the company for the benefit of its members as a whole (CA 2006, section 172(1)).

11 Issuance of new shares

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

The board of directors may generally only issue shares without prior shareholder approval if permitted to do so by the company's articles of association or by resolution of the company (CA 2006, section 551(1)). Any such provision contained within a company's articles of association must be renewed at least every five years (CA 2006, section 551(3)(b)(i)).

The board of directors may also allot new shares without shareholder approval if those shares:

- relate to an employee share scheme (CA 2006, section 549(2)(a));
- are allotted pursuant to a right to subscribe for, or to convert any security into, shares in the company (CA 2006, section 549(3)); or
- are allotted after the directors' authority to allot has expired but are allotted pursuant to an authorisation or agreement entered into before that authority expired, provided that the authorisation allowed the company to enter into agreements that may require shares to be allotted after it had expired (CA 2006, section 551(7)).

The board of directors does not require authorisation, pursuant to CA 2006, section 551, to sell or transfer treasury shares (CA 2006, section 727), as this will not constitute an allotment of shares.

The board of directors generally must not issue new shares unless it has given the company's existing shareholders an opportunity to exercise their rights of pre-emption (that is, their right of first refusal of any freshly issued shares in the company) in relation to these newly issued shares (CA 2006, section 561(1)). However, this right of pre-emption does not apply to: shares that relate to an employees' share scheme (CA 2006, section 566); subscriber shares (CA 2006, section 577); bonus shares (CA 2006, section 564); or an allotment of shares or securities if these are, or are to be, wholly or partly paid up otherwise than in cash (CA 2006, section 565). Existing shareholders must also be afforded the opportunity to exercise their pre-emption rights in relation to the sale or transfer of treasury shares, in accordance with CA 2006, section 561 (CA 2006, section 560(3)).

If the board of directors has a general authority to allot shares pursuant to CA 2006, section 551, then they may be empowered by the company's articles of association, or by a special resolution passed by the company's shareholders, to allot shares under that authority as if the pre-emption rights set out under CA 2006, section 561 did not apply (CA 2006, section 570(1)). These pre-emption rights may also be disapplied in relation to a specified allotment of such shares only, although this requires a special resolution to be passed (CA 2006, section 571(1)). It is also possible for directors to sell treasury shares free from pre-emption rights, provided that the directors are authorised to do so by the company's articles of association or by special resolution (CA 2006, section 573(1) and (2)). Where treasury shares are being sold and a disapplication of pre-emption rights is being relied upon, that disapplication should expressly allow directors to sell treasury shares.

LR9.3.11R also requires that when a company with a premium listing issues equity securities for cash, or sells treasury shares that are equity securities for cash, these equity securities must first be offered to holders of that class of equity shares and holders of other equity shares who are entitled to be offered them. However, LR9.3.11R does not apply:

- to issues of shares in respect of which pre-emption rights have been disapplied under CA 2006, section 570 or 571;
- in certain circumstances relating to a rights issue or open offer;
- to a sale of treasury shares for cash by a listed company to an employee share scheme;
- to an overseas company with a premium listing that has obtained the consent of its shareholders, subject to certain conditions being met; or
- to an open-ended investment company (LR9.3.12R).

Institutional investors should have regard to guidance published by the IA and the Pre-emption Group when deciding whether to vote in favour of resolutions to grant directors the authority to allot shares and to disapply pre-emption rights (see question 1).

12 Restrictions on the transfer of fully paid shares

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

It is a cardinal principle of the Listing Rules that fully paid shares in listed companies must be freely transferable (LR2.2.4R(1)). Shares must be fully paid up and free from any restriction on the right of transfer (except for any restriction imposed for failure to comply with a notice given under CA 2006, section 793) if they are to be listed (LR2.2.4R(2)).

13 Compulsory repurchase rules

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

It is not generally permissible for a public company to require its own shareholder to sell their shares back to the company. Following a takeover offer, an offeror may compulsorily acquire the shares of a target company that are held by minority shareholders if it acquires, or unconditionally contracts to acquire, 90 per cent of the shares in the company to which the offer relates and 90 per cent of the voting rights carried by those shares (known as 'the squeeze-out' procedure) (CA 2006, section 979(1) and (2)). Minority shareholders whose shares are acquired under CA 2006, section 979 must be offered the same consideration as was offered under the terms of the original offer, although special provisions apply if the original form of consideration offered is no longer available (CA 2006, section 981(1), (2) and (5)). The compulsory acquisition of the minority shareholders' shares will become mandatory once the offeror has given notice of his or her intention to acquire these shares in accordance with CA 2006, section 979(2) (CA 2006, section 981(2)).

A minority shareholder who receives notice that their shares are to be acquired pursuant to CA 2006, section 979 may apply to the court in respect of this acquisition within six weeks from the date on which the notice was given (CA 2006, section 986(1) and (2)). The court may order that the offeror is not entitled and bound to acquire the shares to which the notice relates, or that the terms on which the shares are to be acquired shall be such as the court thinks fit (CA 2006, section 986(1)). However, the court may not require consideration of a higher value than that specified in the terms of the offer to be given for the shares to which the application relates unless the holder of the shares shows that this value would be unfair, nor may it require consideration of a lower value than the offer value to be given for the shares (CA 2006, section 986(4)). A party who brings an application before the court in respect of CA 2006, section 979 must comply with certain notice requirements (CA 2006, section 986 (6) to (10)).

CA 2006, section 983 gives the minority shareholders of a target company the right to have their shares compulsorily acquired by an offeror if that offeror has acquired or unconditionally contracted to acquire some (but not all) of the shares to which the offer relates and those shares: amount to not less than 90 per cent in value of all the voting rights in the company (or would do but for certain circumstances); and carry not less than 90 per cent of the voting rights in the company (or would do but for certain circumstances) (CA 2006, section 983(1) and (2)) (known as 'the sell-out procedure'). CA 2006, section 983 also gives minority shareholders who hold non-voting shares and minority shareholders who hold shares of a certain class the right to have their shares compulsorily acquired in certain circumstances by an offeror (CA 2006, section 983(3) and (4)).

The offeror must acquire these shares on the terms of the offer that it has made for the target company, or on such other terms as may be agreed (CA 2006, section 985(1) and (2)). Special provisions apply if the original form of consideration offered is no longer available (CA 2006, section 985(5)).

Both a minority shareholder whose shares are acquired pursuant to CA 2006, section 983 and the offeror required to purchase such shares in accordance with this section can apply to the court for an order that the terms on which the offeror is entitled and bound to acquire the shares be such as the court thinks fit (CA 2006, section 986(3)). The restrictions set out in CA 2006, section 986(4) apply to any order that the court may make in respect of the acquisition of these shares (see above). A party who brings an application in respect of CA 2006, section 983 must comply with certain notice requirements (CA 2006, section 986(6) to (10)).

14 Dissenters' rights

Do shareholders have appraisal rights?

A dissenting shareholder whose shares are acquired pursuant to CA 2006, section 979 or 983 may ask the court to make an order in respect of this acquisition under CA 2006, section 986(1) or 986(3) respectively. On such an application, the court may require consideration of a higher value to be given for the dissenting shareholders' shares than that specified in the terms of the offer if the dissenting shareholder can show that the offer value would be unfair (CA 2006, section 986(4)(a)) (see question 13).

The responsibilities of the board (supervisory)

15 Board structure

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

The board structure for UK-listed companies is best categorised as one-tier. UK companies do not have separate executive boards and supervisory boards. Instead, both executive directors and non-executive directors (who exercise a supervisory function) act as one board. This places greater emphasis on the composition of the board and the balance of independent and non-independent directors. The Code specifically addresses the issue of board composition, and bodies such as the PLSA have issued influential guidance on this topic (see questions 1 and 23).

16 Board's legal responsibilities

What are the board's primary legal responsibilities?

The board must discharge its statutory duties under CA 2006, sections 171 to 177 (see question 1). In addition, the board has a number of legal responsibilities, including the following:

- keeping the company's statutory books up to date;
- filing certain documents with Companies House, such as the company's annual return;
- preparing the company's accounts and reports (including a directors' report and a directors' remuneration report for each financial year);
- ensuring that the company complies with its statutory obligations under, among other things, CA 2006, FSMA 2000, health and safety legislation, environmental legislation and competition legislation;
- ensuring that the company complies with its obligations under the LPDT Rules, particularly the disclosure requirements and continuing obligations contained within those rules;
- monitoring the company's compliance with the Code and reporting on its performance in this regard in accordance with LR9.8.6R(5) and (6);
- ensuring that the company complies with the Takeover Code if it becomes subject to takeover discussions; and
- ensuring that the provisions of the Insolvency Act 1986 are complied with if the company falls into financial difficulty.

17 Board obligees

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

The board represents and owes its legal duties to the company (ie, to its shareholders as a whole) rather than to any individual shareholder or group of shareholders (CA 2006, section 170(1)). However, when discharging his or her duty to promote the success of the company, a director must have regard to the interests of stakeholders in the company including its employees, suppliers and customers and the local community and environment, as well as considering the need to act fairly as between members of the company (CA 2006, section 172). The idea that the directors must consider not simply the interests of its members is known as 'enlightened shareholder value', and it has been enshrined in statute through CA 2006.

The directors of a company that is in financial difficulty will be obliged to act in the best interests of its creditors, rather than in the interests of the company itself (CA 2006, section 172(3)).

18 Enforcement action against directors

Can an enforcement action against directors be brought by, or on behalf of, those to whom duties are owed?

Shareholders may bring a derivative claim (ie, an action brought by a shareholder on behalf of the company and in respect of a cause of action vested in the company) (CA 2006, section 260(1)). The cause of action must arise from an actual or proposed act or omission involving negligence, default or breach of duty or trust by a director of the company (CA 2006, section 260(3)). The cause of action may be against the director or another person or both (eg, a third party who has knowingly benefited from a director's negligence, default or breach of duty, etc) (CA 2006, section 260(3)).

The person bringing the claim must be a member of the company but need not have been a member at the time that the cause of action arose (CA 2006, sections 260(1) and (4)). Concerns have arisen that this may lead to activists acquiring shares in certain companies in order to obtain the right to bring a derivative claim against that company and thus disrupt its activities (for example, animal rights activists may consider buying shares in a company involved in vivisection). However, the requirement for shareholders seeking to bring a derivative claim to establish a prima facie case for that claim should be sufficient to prevent the rights granted by CA 2006, section 260 from being abused in this way (see below).

A shareholder seeking to bring a derivative claim under CA 2006, section 260 must obtain the court's permission to continue that claim (CA 2006, section 261(1)). To obtain such permission, the shareholder must convince the court that it has a prima facie case against the director (or other relevant person) (CA 2006, section 261(2)).

A shareholder may also apply to the court to continue as a derivative claim a claim that has been brought by the company, the cause of action for which could be pursued as a derivative claim under CA 2006, chapter 1 of part 11 (CA 2006, section 262(1)). The shareholder may apply to the court to continue such a claim as a derivative claim on the ground that:

- the manner in which the company commenced or continued the claim amounts to an abuse of the process of the court;
- the company has failed to prosecute the claim diligently; and
- it is appropriate for the member to continue the claim as a derivative claim (CA 2006, section 262(2)).

As with claims brought under CA 2006, section 260, the shareholder must convince the court that it has a prima facie case before they will be permitted to continue the claim (CA 2006, section 262(3)).

If a shareholder seeking to bring a derivative claim or seeking to continue a claim as a derivative claim, under CA 2006, sections 261 or 262 respectively, fails to make a prima facie case for their claim, the court must dismiss their application for permission to continue such a claim and make any consequential order it considers appropriate (CA 2006, sections 261(2) and 262(3)). If the court does not dismiss their application on this ground then it may:

- seek evidence in respect of the claim from the company;
- give permission to continue the claim on such terms as it thinks fit;
- refuse permission and dismiss the application; or
- adjourn the proceedings on the application and give such directions as it thinks fit (CA 2006, sections 261(3) and (4) and 262(4) and (5)).

CA 2006, section 263 sets out the factors that the court must have regard to when deciding whether to grant permission to bring a derivative claim under CA 2006, sections 261 or 262. In particular, the court must dismiss such a claim if it is satisfied that: a person acting in accordance with the general duty to promote the success of the company under CA 2006, section 172 would not seek to continue the claim (CA 2006, section 263(2)(a)); or an act or omission giving rise to the cause of action has been authorised or ratified by the company (either before or after that act or omission occurred) (CA 2006, section 263(2)(b) and (c)). Additional factors that the court must take into account when considering whether to grant permission to bring a derivative claim under CA 2006, sections 261 or 262 are set out at CA 2006, section 263(3). Notably the member bringing the derivative claim must be acting in good faith (CA 2006, section 263(3)(a)). When deciding whether to grant permission, the court must have particular regard to the views of members who have no personal interest in the matter (CA 2006, section 263(4)).

A shareholder may also apply for permission to continue a derivative claim that has been brought or continued by another shareholder of the company if: the manner in which the proceedings have been commenced or continued by the shareholder amounts to an abuse of the process of the court; the shareholder has failed to prosecute the claim diligently; and it is appropriate for the applicant shareholder to continue the claim as a derivative claim (CA 2006, sections 264(1) and (2)). Once again, the shareholder seeking to continue the derivative claim must establish a prima facie case (CA 2006, section 264(3)). If the court is satisfied that the claim should not be dismissed on this ground then it may give the same directions under CA 2006, section 264(4) and (5) as those mentioned above in relation to CA 2006, sections 261(3) and (4) and 262(4) and (5).

It should be noted that, where the cause of action for a derivative claim arose before 1 October 2007, the court may allow an application made under CA 2006, sections 260 to 264 to proceed if it would have been allowed to proceed as a derivative claim under the common law rules that applied before that date.

If any proceedings for negligence, default, breach of duty or breach of trust are brought against a director, the court can relieve that director either wholly or partly of his or her liability to the company if it finds that he or she acted honestly and reasonably and that, having regard to all the circumstances, he or she ought fairly to be excused (CA 2006, section 1157).

If a shareholder has suffered unfair prejudice, the shareholder is able to petition the court in accordance with CA 2006, section 994. However, a shareholder who sues under the unfair prejudice provision is claiming in his or her own capacity, whereas a shareholder who claims under the derivative action provisions claims on the company's behalf.

19 Care and prudence

Do the board's duties include a care or prudence element?

Company directors must exercise reasonable care, skill and diligence, that is, the level 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 that director in relation to the company; and the general knowledge, skill and experience that the director has (CA 2006, section 174(1) and (2)).

The first limb of this test of the level of care and skill required from a director is objective and sets a minimum standard of behaviour that all directors must meet. The second limb of this test is subjective and requires directors with superior knowledge, skills and experience to meet a higher standard of care and skill than would be expected under the first limb (for example, a director with an accountancy qualification may be expected to demonstrate a higher standard of skill and care in certain circumstances than would be expected of a director who did not have such a qualification).

20 Board member duties

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

The statutory duties set out at CA 2006, sections 171 to 177 are owed to the company by all of its directors (CA 2006, section 170(1)). A 'director' is defined as including any person occupying the position of director, by whatever name called: this includes executive directors, non-executive directors and its de facto directors (CA 2006, section 250). These statutory duties currently only apply to shadow directors where, and to the extent that, they were held to so apply at common law (CA 2006, section 170(5)). However, the Small Business, Enterprise and Employment Act 2015 amended the CA 2006 from May 2015, such that the general duties apply to shadow directors to the extent that they are capable of applying.

A more skilled and experienced director may be required to demonstrate a higher level of care and skill than a less skilled and experienced director, in accordance with the subjective test of the level and care of skill owed by a director set out at CA 2006, section 174(2)(b) (see question 19).

ICSA guidance published in January 2013 suggests that it is not reasonable for non-executive directors to be expected to have the same knowledge and experience of a company's affairs as executive directors. However, under the objective test in CA 2006, section 174(2)(a) when determining whether a non-executive director has breached his or her duty to exercise reasonable care, skill and diligence, a court would consider the steps a reasonably diligent non-executive director in the same position would have taken to familiarise themselves with the company's business and operations.

See question 22 for further information on how the roles of executive and non-executive directors differ.

21 Delegation of board responsibilities

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

In practice, a company's board will delegate responsibility for the day-to-day operations of the company to its management. In July 2013, the ICSA issued updated guidance on matters that should be reserved for the board, rather than delegated to executive management. These matters include strategy and management, structure and capital and financial and reporting controls. Further, the Code requires the board to publish a formal schedule of matters specifically reserved for its decision and to include in its annual report a high level statement of which types of decisions are to be taken by the board and which are to be delegated to management (Code provision A.1.1). Companies should comply with this provision although, as mentioned in question 1, a listed company does not strictly have to comply with any provision of the Code but it will need to explain its rationale for non-compliance.

In addition, the board will delegate responsibility for certain matters to its audit, remuneration and nomination committees (see question 25). A company may also have additional committees to which the board delegates responsibility for matters such as risk, health and safety, corporate social responsibility and share plans. Some of these committees may be formally constituted by the board while others may be management committees. The FRC has suggested in its Guidance on Board Effectiveness that boards can minimise the risk of poor decisions by investing time in the design of their decision-making policies and processes, including the contribution of committees (Guidance on Board Effectiveness, paragraph 3.1).

Many companies' boards appoint an executive committee, which typically comprises the executive directors and the most senior members of the management team. The executive committee will usually be formally appointed by the board as the chief executive's forum for major operational decisions. An ICSA guidance note published in July 2013 suggests that the executive committee should report back to the board and have written terms of reference and delegated authorities, which are agreed by the board in advance as a matter of good practice.

Many companies' articles of association also include provisions allowing directors to appoint alternate directors to act for them in their absence.

22 Non-executive and independent directors

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

The Code recommends that a company's board should include an appropriate balance of executive and non-executive directors (and in particular, independent non-executive directors) such that no individual or small group of individuals can dominate the board's decision-making process (Code, supporting principle B.1). It also recommends that for companies listed in the FTSE 350, at least half of the board, excluding the chairman, should be made up of independent non-executive directors (Code, provision B.1.2). Criteria for assessing the independence of a non-executive director are set out at provision B.1.1 of the Code. These provisions should be complied with, or an explanation should be given for non-compliance (see question 1). The PLSA has also published guidance on this matter in its 'Corporate Governance Policy and Voting Guidelines' published in December 2014, and it helps institutional investors in determining whether a director is indeed independent (see question 1). The PLSA suggests that voting sanctions could be warranted in the event that the appointment of a non-independent non-executive director compromises the composition of key committees or the board itself.

CA 2006 does not distinguish between the duties owed to a company by its executive directors and its non-executive directors (see question 20). However, executive directors owe special duties arising out of their contracts of employment over and above these statutory obligations. These contractual obligations are generally different to the supervisory responsibilities discharged by non-executive directors. Executive directors, for example, are responsible for the day-to-day running of the company, while the role of the non-executive director is to challenge, review and monitor the performance of the board. The FRC's Guidance on Board Effectiveness states that constructive challenge from non-executive directors is an essential aspect of good corporate governance, and it should be welcomed by the executive directors (Guidance on Board Effectiveness, paragraph 1.17).

The standard of skill and care owed to the company by its directors and its non-executive directors is also likely to be different due to the subjective test of the level of skill and care owed by a director to their company that is set out at CA 2006, section 174(2)(b) (see question 19). As non-executive directors are less involved with the day-to-day management of the company, they may not be expected to demonstrate a standard of skill and care that is as high as the standard of executive management (see question 20). It is accepted that non-executive directors are likely to devote significantly less time to a company's affairs than an executive director and that the detailed knowledge and experience of a company's affairs that could reasonably be expected of a non-executive director will generally be less than for an executive director. However, if a non-executive director serves on a board committee, they will be expected to exercise greater skill and care in relation to matters within the remit of that committee than would directors who are not members of the relevant committee.

The Code advises that the board should appoint one of the independent non-executive directors as senior independent director. The role includes leading a meeting of the non-executive directors to appraise the chairman's performance (without the chairman being present) at least annually and on such other occasions as deemed appropriate. The senior independent director should also hold meetings with the non-executive directors without the executives present. The senior independent director should also be available to shareholders if they have concerns that contact with the company through the normal channels of chairman, chief executive officer or other executive directors has failed to resolve or for which such contact is inappropriate (Code, provisions A.4.1 and A.4.2).

23 Board size and composition

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

It is a company law requirement that public companies have at least two directors (CA 2006, section 154 (2)). At least one of these directors must be a natural person (CA 2006, section 155(1)), though in practice listed companies will have considerably more. Note that this requirement will be superseded when section 87 of the Small Business, Enterprise and Employment Act 2015 (SBEEA 2015) comes into force. This will repeal CA 2006, section 155 and replace it with a new provision prohibiting the appointment of corporate directors and requiring all company directors to be natural persons. Although the Secretary of State will have the power to provide for exceptions and a transition period of a year will apply for companies with corporate directors already in place, an appointment made in contravention of this section will be void and it will be an offence to breach the prohibition. There is no set implementation date for this section of the SBEEA 2015 (having initially been planned for October 2016), but the provision is expected to come into force, possibly later in 2017.

Subject to certain exceptions, a person may not become a director of a company unless he or she has attained the age of 16 years (CA 2006, section 157(1)), although an appointment can be made before the individual reaches 16 years provided that the appointment does not take effect until that time (CA 2006, section 157(2)).

In certain circumstances, the courts of England and Wales may make a disqualification order against a person, to the effect that for a defined period that person must not be a director of a company (Company Directors Disqualification Act 1986, section 1(1)(a)). A court may make such an order for a number of reasons, such as the person being convicted of certain offences or being persistently in default in relation to companies legislation.

Except for the CA 2006 requirement stated above, and subject to the comments made below, there is no specified minimum or maximum number of seats on the board, although the size of the board may be determined by the company's articles.

The Code specifically addresses the issue of board composition.

- Main principle B.1 of the Code states that the board (and its committees) should have the appropriate balance of skills, experience, independence and knowledge of the company to enable them to discharge their respective duties and responsibilities effectively. As this is a main principle of the Code, it will be necessary for listed companies to include a statement in their annual financial report that discloses how the board has applied this principle. Listed companies incorporated in the UK must make this disclosure in order to comply with LR9.8.6R(5), and companies incorporated overseas must disclose in order to comply with LR9.8.7R. The preface to the Code also encourages company chairmen to report personally in their annual statements how the principles contained in sections A and B of the Code have been applied, though this is not a requirement.
- The Code specifies that the board should be of sufficient size that the requirements of the business be met and changes to board composition can be managed without disruption, but the board should not be so large as to be unwieldy (Code, supporting principle B.1).
- When appointing new directors to the board, it is necessary to consider supporting principle B.2 of the Code. This stipulates that the criteria for appointing new directors should be objective, and with due regard for diversity, including gender. The FRC published guidance to accompany the new Code in May 2010 and this emphasises that the appointment of new directors should be based on merit.

- The board should also include an appropriate combination of executive and non-executive directors (and in particular independent non-executive directors) in order to prevent an individual or small group of directors from dominating the decision-making of the company (Code, supporting principle B.1)(see question 22).

The FRC's Guidance on Board Effectiveness, although not prescriptive, is intended to assist companies in applying the Code. The Guidance on Board Effectiveness explains that diversity in board composition is an important driver of a board's effectiveness, creating a breadth of perspective among directors and countering a tendency for 'group think' (Guidance on Board Effectiveness, paragraph 1.3). Although the Code itself does not define 'diversity', the Guidance on Board Effectiveness specifically comments that diversity of psychological type, background and gender is important (Guidance on Board Effectiveness, paragraph 4.3). In terms of knowledge and experience, directors must possess the right skill set to enable them to run the company and to ensure that they can make a positive contribution to the company (Guidance on Board Effectiveness, paragraph 4.1).

The nomination committee, usually led by the chairman, should be responsible for board recruitment of companies with a premium listing of equity securities. This should be a continuous and proactive process and should take into account the company's agreed strategic priorities (Guidance on Board Effectiveness, paragraph 4.2). The shareholders will still need to approve any appointment of a director (see question 3). If a company's articles of association provide that the board may appoint a director, for example, to fill a vacancy, such an appointment must usually be approved by an ordinary resolution at the company's next annual general meeting (AGM) (Code, provision B.7.1).

Institutional investors have also considered the topic of board composition. As mentioned in question 1, the guidelines set out by entities such as the IA and the PLSA are not enshrined in statute but it remains ill-advised to ignore their suggestions. In particular, the PLSA has produced its corporate governance policy and voting guidelines. In the context of section B.2 of the Code, the PLSA expects to see proper disclosure of the steps being taken towards bringing diversity to the boardroom. Where disclosure is poor, or where there is a lack of board succession planning, or there is a lack of due consideration of diversity and the balance of skills on the board, the PLSA suggests that investors may wish to abstain, or even vote against the re-election of the chairman of the nomination committee (who is responsible for appointments to the board and succession). Where there is no statement on a company's diversity policy and its application at all, the PLSA advises that shareholders may wish to vote against the election of a director. The PLSA has also encouraged companies to state more fully the skills and experience that a director brings to his or her role, including a statement of other current appointments that might affect his or her ability to contribute to the work of the board.

The ABI published its second Report on Board Effectiveness in December 2012. It emphasises that diversity of perspective should be a key objective when appointing board members, and that companies should disclose the steps they are taking to promote a diversity of perspective in their boardroom, as well as the challenges they face in seeking out relevant skills and experience. In addition, the chairman should widen the search for non-executive directors, broadening traditional talent pools, when making board appointments. The ABI report also focuses on succession planning. The biggest improvements that need to be made here are in relation to disclosure and companies are encouraged to provide meaningful disclosures on their succession plans. In contrast to the 2011 Report on Board Effectiveness, the 2012 report does not specify that the diversity of perspective and succession planning disclosures should be contained in the annual report, however, such a disclosure would continue to satisfy the requirements.

When the Code is interpreted together with the Guidance on Board Effectiveness and the Report on Board Effectiveness, it is apparent that, practically speaking, companies listed in the UK must give due consideration to attaining the appropriate balance of skills, experience, independence, knowledge and diversity. Although strictly speaking a company can decide how well it applies the main principles of the Code, it will have to make a statement in its annual financial report as to the application of the main principles and 'comply or explain' in relation to the provisions, and it is unlikely that shareholders will allow poor application to persist, in the absence of alternative justification.

Monitoring gender representation and diversity on boards has become a particular focus in recent years. As advised by the Davies Report (February 2011) 'Women on Boards', the FRC has consulted on the issue of gender diversity at an executive level. Lord Davies had recommended that FTSE 350 boards should aim for a minimum of 25 per cent female representation by 2015. In May 2011, the FRC published a consultation document, concerned with whether further steps were required to reach the goal of more diverse boards; what, if any, these changes should be; and when they should be introduced. In March 2015 Lord Davies released his fourth annual progress report on this matter, reporting on the progress that FTSE 350 companies have made towards reaching the 2015 targets. The report states that progress had been positive, with women accounting for 23.5 per cent of FTSE 100 and 18 per cent of FTSE 250 board directors at that time.

Lord Davies' final report was published on 29 October 2015. It noted that there were no male-only boards in the FTSE 100 and that women held 26.1 per cent of board positions in those companies; and that in FTSE 250 companies, women held 19.6 per cent of board positions and there were 15 male-only boards. It also made five recommendations, including that the voluntary, business-led approach to improving the number of women in board positions be continued until 2020 and targeting 33 per cent female board representation in FTSE 350 companies in the same time frame.

This voluntary target has been reiterated in the latest report on board diversity, the Hampton-Alexander Review, published on 8 November 2016. The Review highlights increases in female board representation for the FTSE 100 and 250, to 26.6 per cent and 21.1 per cent respectively – an overall increase to 23 per cent for the FTSE 350, up from 21.9 per cent in the previous year. Further recommendations include, for example, the suggestion that FTSE 350 companies should voluntarily publish details of the number of women on the executive committee in their annual reports or on websites.

Gender diversity on boards has also become an area of legislative change. In October 2013, the Companies Act (Strategic Report and Directors' Report) Regulations 2013 was implemented for companies with financial years ending on or after 30 September 2013. The regulations contain a requirement for listed companies to make three separate disclosures on the proportion of women and men who are, respectively, directors, senior managers and employees of the company (CA 2006, section 414C(8) and (9)).

In November 2012 the European Commission announced that it was 'taking action to break the glass ceiling that continues to bar female talent from top positions', and published proposals for a directive aimed at achieving gender balance on the boards of European companies. The proposed directive sets an objective for listed companies to increase non-executive directors of the under-represented sex (usually women) to 40 per cent by 1 January 2020. Listed companies will also be required to publish information annually on the gender composition of their boards. The quotas are not described in the directive as being mandatory; however, companies would have to provide reasons for not meeting the quotas. As the directive is currently drafted, member states may provide that not meeting the 40 per cent quota in respect of non-executive directors can be justified if a listed company can show that members of the under-represented gender hold at least one-third of all director positions, irrespective of whether they are executive or non-executive directors. On 20 November 2013, the European Parliament adopted the European Commission proposal, with amendments. However, it was announced in December 2014 that the Council was unable to reach a general approach on this directive, so this still remains in the legislative pipeline.

In the meantime, new DTR 7.2.8A has been introduced to implement EU Directive (2014/95) on disclosure of non-financial and diversity information, applicable to large issuers for financial years commencing on or after 1 January 2017. Affected companies' corporate governance statements must now include an additional description of the diversity policy applied to their administrative, management and supervisory bodies, and how it has been implemented. If no diversity policy is applied then the statement must contain an explanation as to why this is the case.

The PLSA has acknowledged the recent emphasis on gender diversity and now expects boards to set out an explicit policy for achieving a greater degree of diversity than has been the practice in the past. Boards should also track the implementation of this policy, including explaining any measurable objectives that they have set for implementing the policy and the progress they have achieved on these objectives. Similarly, the ABI Report on Board Effectiveness recommends that companies should develop and disclose the initiatives they have in place to develop women in their organisation as well as disclosing the proportion of women not only on their board, but also in senior management and in the whole organisation.

Furthermore, the Equality and Human Rights Commission published in March 2016 its 'six step guide to good practice' on how to improve board diversity. This is a guide for companies and executive search firms to improve the diversity of company boards within the frameworks set out by the Equality Act 2010 and the Financial Reporting. The six steps are as follows.

Making an appointment:
- Define the selection criteria in terms of measurable skills, experience, knowledge and personal qualities.
- Reach the widest possible candidate pool by using a range of recruitment methods and positive action.
- Provide a clear brief, including diversity targets, to your executive search firm.
- Assess candidates against the role specification in a consistent way throughout the process.

Ongoing action to improve diversity:
- Establish clear board accountability for diversity.
- Widen diversity in your senior leadership talent pool to ensure future diversity in succession planning.

24 Board leadership

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

The Code states that the positions of chairman and chief executive officer (CEO) should not be occupied by the same person, to ensure that no one individual has unfettered decision-making powers (Code, provision A.2.1). Most UK-listed companies separate the role of chairman and CEO.

Any decision to combine the roles of chairman and CEO in one person must be publicly justified in accordance with the 'comply or explain' principle of the Code (LR9.8.6R(6) and LR9.8.7R). Major shareholders should be consulted in advance of the appointment and the reasons for the failure to separate the two roles should be set out at the time of the appointment and in the company's next annual report (Code, provision A.3.1).

The Code recommends that the division of responsibility between the chairman and CEO should be clearly established, set out in writing and agreed by the board (Code, provision A.2.1). The Code further provides that the chairman should meet the independence criteria set out at provision B.1.1 (Code, provision A.3.1).

Guidance published by the PLSA has reiterated that the division of the roles of chairman and CEO is a cornerstone of good governance in the UK, a position supported by the PIRC in its Shareholder Voting Guidelines 2017, which state that it will oppose the re-election of a CEO holding the position of chairman except in exceptional circumstances. The PLSA guidance also suggests that the succession of the CEO to chairman would only be acceptable on rare occasions, and that the contravention of this tenet for a period of over one year may require shareholder action.

25 Board committees

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

A company's directors may delegate certain powers and responsibilities to board committees if permitted to do so by its articles of association.

The Code provides that a listed company should establish the following committees, the chairmen and members of which should be identified in the annual report:
- a nomination committee comprising a majority of independent non-executive directors to recommend new appointments and reappointments to the board and senior executive office. Its aim is to promote objectivity in the appointment of directors and to ensure that a company's board is balanced and is not dominated by a particular individual or group of individuals (Code, provision B.2 and supporting principle B.1);
- a remuneration committee made up entirely of independent non-executive directors. FTSE 350 companies should have at least three members on the committee, and companies below the FTSE 350 should have at least two members. It should make recommendations to the board on executive remuneration and determine specific remuneration packages for each of the executive directors and the chairman, including pension rights and compensation payments. The remuneration committee will also monitor the level and structure of remuneration for senior management. Establishing a remuneration committee helps to ensure that executive directors play no part in determining their own remuneration (Code, provision D.2) (see question 28); and
- an audit committee consisting entirely of independent non-executive directors. FTSE 350 companies should have at least three members on the committee, and companies below the FTSE 350 should have at least two members. It should select accounting policies, review draft accounts and maintain an appropriate relationship with the company's auditors (Code, provision C.3). On 16 November 2009, the FRC published 'Challenges for audit committees arising from current economic conditions', which sets out additional issues that audit committees should take into account in view of the global financial crisis when preparing corporate reports. In September 2012, the FRC published a new version of its Guidance on Audit Committees, which is intended to assist listed companies in implementing the relevant provisions of the Code, although the Guidance itself is non-binding. The Guidance was updated in April 2016. The requirement for a UK-listed company to establish an audit committee is also enshrined in law by DTR7.1, which provides that such a committee should have at least one independent member and a member that has competence in accounting or auditing, or both (DTR7.1.1R). There is a degree of overlap here with provision C.3.1 of the Code, which states that at least one member of the committee should have recent and relevant financial experience.

The Competition and Markets Authority also published its order relating to statutory audit services for large companies (the CMA Order) on 26 September 2014. The CMA Order, among other things, requires the terms of the statutory audit services for a FTSE 350 company to be negotiated and agreed by the audit committee only.

In addition, the FRC's Guidance on Board Effectiveness states that, notwithstanding a board's delegation of decision-making to committees in relation to audit, risk and remuneration, the board retains responsibility for, and makes the final decisions on, all of these areas (Guidance on Board Effectiveness, paragraph 6.1).

In June 2013, the ICSA published guidance on the terms of reference for the nomination, remuneration, audit and risk committees of a company seeking to comply fully with the provisions of the Code, following the latter's publication in September 2012. The guidance note on terms of reference for the audit committee was updated in March 2017 to reflect revisions to the Code made in April 2016 and the FRC's latest Guidance on Audit Committees (see above).

26 Board meetings

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

The Code provides that the board should meet regularly enough to discharge its duties effectively (Code, provision A.1.1). However, this will be subject to the company's articles, which may specify a minimum number of board meetings that must be held per year. The Code does provide that a company should set out in its annual report the number of meetings of the board and its committees that took place, as well as the level of individual attendance by directors (Code, provision A.1.2).

27 Board practices

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

Annex I of appendix 3 to the PRs requires an issuer of securities to include details of certain aspects of its board practices in any prospectus that it publishes, including information about its audit and remuneration committees and a summary of the terms of reference of these committees (PR appendix 3, annex I, item 16.3).

Schedule B to the Code sets out various details relating to a board's practices that should be disclosed in its annual report, including the following:

- a statement of how the board operates, including a high-level statement of which types of decisions are to be taken by the board and which are to be delegated to management (Code, provision A.1.1);
- the number of board and committee meetings that have occurred each year and individual attendance by directors at such meetings (Code, provision A.1.2);
- the work of the nomination committee and the process it has used in relation to board appointments (Code, provision B.2.4);
- how performance evaluation of the board, its committees and its individual directors has been conducted (Code, provision B.6.1);
- an explanation from the directors of their responsibility for preparing the company's accounts (Code, provision C.1.1);
- an explanation from the directors of the basis on which the company generates or preserves value over the longer term (the business model) and the strategy for delivering the objectives of the company (Code, provision C.1.2);
- the work of the audit committee in discharging its responsibilities (Code, provision C.3.3);
- the work of the remuneration committee as required under the Large and Medium-sized Companies and Groups (Accounts and Reports) Regulations 2013 (Code, provision D.1.2); and
- the steps that the board has taken to ensure that the members of the board, and in particular the non-executive directors, develop an understanding of the views of major shareholders (Code, provision E.1.2).

A listed company needs to disclose these practices in order to comply with the Code.

The Code also recommends that the terms and conditions of appointment of non-executive directors should be made available for inspection (Code, provision B.3.2), as should the terms of reference of the nomination, remuneration and audit committees (Code, provisions B.2.1, D.2.1 and C.3.3).

28 Remuneration of directors

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

The remuneration of a director of a private company is set by the board. In a listed company, its remuneration committee will be tasked with determining the remuneration of its directors. It is a provision of the Code that FTSE 350 companies should establish a remuneration committee of at least three independent non-executive directors, and companies below the FTSE 350 should establish committees of at least two such directors (Code, provision D.2.1). The remuneration committee should have delegated responsibility for setting remuneration of all executive directors and the chairman, including pension rights and any compensation payments (Code, provision D.2.2). The remuneration committee should take care to recognise and manage conflicts of interest when consulting the chief executive in relation to their proposals relating to the remuneration of other directors (Code, supporting principle D.2). The remuneration of non-executive directors should be determined by the board itself, subject to the shareholders reserving this responsibility through the company's articles of association (Code, provision D.2.3).

It is a requirement that the directors of a quoted company prepare a directors' remuneration report for each financial year of the company (CA 2006, section 420(1)). It is also a requirement for directors of quoted companies with a financial year ending on or after 30 September 2013 to prepare a remuneration policy to be set out in a separate part of the report, which must be approved by shareholders at least every three years (CA 2006, section 421(2A)). The shareholders of the company must be given the opportunity to approve the remuneration report (annually) and remuneration policy (at least every three years) by ordinary resolution (see questions 4 and 36). The requirements as to the form and content of the directors' remuneration report and remuneration policy are outlined in schedule 8 to the Large and Medium-sized Companies and Groups (Accounts and Reports) Regulations 2008.

Legislative changes in relation to executive remuneration came into effect on 1 October 2013. The Large and Medium-sized Companies and Groups (Accounts and Reports) (Amendment) Regulations 2013 implemented new content requirements for directors' remuneration reports, including the requirement for companies to publish in their remuneration report a single figure for total remuneration for each person that has held the office of director in that financial year. In addition, sections 79 to 82 of the Enterprise and Regulatory Reform Act 2013 (ERRA 2013) added the following requirements to CA 2006:

- an amendment to section 421 to allow for regulations to be published setting out the content requirements of a directors' remuneration policy regarding future remuneration payments and payments for loss of office, which will be set out in a separate part of the directors' remuneration report;
- the introduction of section 439A which requires a binding ordinary shareholder resolution to approve the remuneration policy at least every three years; and
- the introduction of sections 226A to 226F which restrict remuneration payments and payments for loss of office to directors to those specified within the approved remuneration policy. Section 226E is particularly noteworthy as it requires any directors who approve payments that contradict the approved remuneration policy to indemnify the company, jointly and severally, against any losses that arise from the payment (although relief is available to directors who can show that they acted honestly and reasonably).

Section D of the Code specifically addresses the issue of board remuneration. It contains the following two main principles on directors' remuneration:

- executive directors' remuneration should be designed to promote the long-term success of the company. Performance-related elements should be transparent, stretching and rigorously applied (Code, main principle D.1) (this was amended in the 2014 version of the Code from the previous requirement that the levels of remuneration be sufficient to attract, retain and motivate directors); and
- there should be a formal and transparent procedure for developing policy on executive remuneration and for fixing the remuneration packages of individual directors. No director should be involved in deciding his or her own remuneration (Code, main principle D.2).

Pursuant to the Listing Rules, a listed company incorporated in the UK must include in its annual financial report a board report addressed to the shareholders containing details of the unexpired term of the director's service contract of a director proposed for election or re-election at the forthcoming annual general meeting, and, if any director proposed for election or re-election does not have a directors' service contract, a statement to that effect (LR9.8.6R(7) and LR9.8.8R).

Executive remuneration has been the focus of various discussion papers and industry guidance in recent years. In February 2008, the ABI and the then NAPF published a joint statement on 'Best Practice On Executive Contracts and Severance', which contains guidance on matters including contract terms, notice periods, severance payments, pensions, and arrangements for shareholder inspection of directors' contracts and side letters relating to severance terms and pension arrangements.

The ABI also published guidance on directors' remuneration in its Principles of Remuneration, updated and republished by the then IMA in October 2014. This guidance provides that remuneration committees should have regard to risk management when setting executive remuneration and also deals with matters including base pay, bonuses, pensions and performance criteria. This guidance focuses on five core principles: the role of shareholders, the role of the board and directors, the remuneration committee, remuneration policies and remuneration structures. The Principles of Remuneration also include initial guidance on the IMA's approach to disclosures under the executive remuneration reporting regime introduced for listed companies in October 2013.

In November 2013 the then NAPF and HERMES EOS published a joint advisory paper on the Remuneration Principles ('Remuneration Principles for Building and Reinforcing Long-Term Business Success'). This paper advocated aligning pay with the long-term success of the company and returns to shareholders, and ensuring that pay schemes were simple and understandable for investors and executives. In October 2016, the Investment Association published an open letter to the FTSE 350 on executive pay in which it called for pay ratios between the CEO and median employee and the CEO and the executive team to be disclosed.

A company must not enter into a director's service contract containing a guaranteed term of employment that is, or may be, more than two years unless authorised to do so by a shareholder resolution passed during a general meeting of the company (CA 2006, sections 188(1) and (2)). Contravention of this requirement will result in the relevant provision being void and the service contract being deemed to contain a term entitling the company to terminate it at any time by giving reasonable notice (CA 2006, section 189). The Code provides that service contracts should be no more than 12 months in duration. If it is necessary to offer longer contract periods to new directors, these should reduce to 12 months or less after the initial period (Code, provision D.1.5).

CA 2006 provides that, subject to certain rules and exceptions, a company must not, unless authorised to do so by shareholder resolution:

- make loans or quasi-loans to directors or persons connected to a director, nor provide any guarantee or security in respect of a loan or quasi-loan made to a director or persons connected to a director (CA 2006, sections 197 to 200, 203 to 214 and 223 to 225);
- enter into a credit transaction as a creditor for the benefit of a director or persons connected with a director, nor provide any guarantee or security in connection with a credit transaction entered into by a director (CA 2006, sections 201 to 214 and 223 to 225);
- enter into substantial property transactions with directors or persons connected with directors (CA 2006, sections 190 to 196 and 223 to 225); nor
- make certain payments to a director in respect of a loss of office (CA 2006, sections 215 to 225, noting that, where the company is a quoted company, the restrictions in CA 2006, section 226C as described above would apply by virtue of CA 2006, section 215(5)).

If a company enters into a transaction with one of its directors or a person connected with such a director and in doing so exceeds any limitations placed on its powers by its articles of association or any shareholder resolutions then, subject to certain exceptions:

- the transaction is voidable at the instance of the company; and
- the director who is party to the transaction (or any person connected with the director and who is party to that transaction) and any director of the company who authorised the transaction will be liable to account to the company for any direct or indirect gain he or she has made from the transaction and to indemnify the company for any loss or damage that it may suffer as a result of the transaction (CA 2006, section 41).

Company directors must also declare the nature and extent of any interest that they have in proposed or existing transactions or arrangements with the company. However, they need not declare such an interest: if it cannot reasonably be regarded as likely to give rise to a conflict of interest; if, or to the extent that, the other directors are already aware of it; or if, or to the extent that, it concerns terms of his or her service contract that have been or are to be considered by a meeting or committee of the directors (CA 2006, sections 177 and 182).

Company directors should also have regard to their duty to avoid conflicts of interest when entering into transactions with the company (CA 2006, section 175). They should also ensure that such transactions do not put them in breach of their obligations not to abuse any inside information that they have about the company, particularly during a 'close period' (that is, the period surrounding the announcement of the company's most recent results) (see also question 36).

29 Remuneration of senior management

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

The remuneration of a company's most senior management will normally be overseen by its remuneration committee (see question 25). The Code states that the remuneration committee should recommend and monitor the level and structure of remuneration for senior management (Code, provision D.2.2). Companies should also have regard to the IMA's principles on executive remuneration when determining the remuneration of their most senior managers (see question 28).

Senior managers should also ensure that certain transactions with the company do not put them in breach of the requirements not to abuse any inside information that they have about the company, particularly during a 'close period' (that is, the period surrounding the announcement of the company's most recent results), in respect of which, see question 36.

30 D&O liability insurance

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

Companies are permitted to maintain directors' and officers' liability insurance (D&O liability insurance) by CA 2006, section 233, although they are not obliged to do so. D&O liability insurance protects directors and officers from financial liability for any claims made against them in respect of the performance of their duties to the company.

A typical D&O liability insurance policy will provide cover for directors, officers, managerial and supervisory employees and the company itself, to the extent that it has indemnified such persons (see question 31). D&O policies generally cover losses such as court costs and damages in respect of claims brought for the wrongful acts of the insured. However, certain types of claim will not be covered by a D&O liability insurance policy, such as those for fraud and dishonesty or property damage or personal injury.

Companies that maintain a D&O liability insurance policy will also be acting in accordance with the Code, which recommends that the company should arrange appropriate insurance cover in respect of legal actions against its directors (Code, provision A.1.3). The ICSA in its January 2013 guidance (ICSA guidance on liability of non-executive directors: care, skill and diligence) recommends that D&O liability insurance should include 'run-off' cover for a period after the director's resignation. It suggests that six years might be considered an appropriate period.

31 Indemnification of directors and officers

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

A company generally may not exempt a director from liability for any negligence, default, breach of duty or breach of trust in relation to the company, nor indemnify him or her in respect of such behaviour (CA 2006, sections 232(1) and (2)). However, a company may maintain insurance for a director in respect of such liability (see question 30) and provide directors with an indemnity in respect of such liability by way of a qualifying third-party indemnity provision (QTPIP) or a qualifying pension scheme indemnity provision (QPSIP) (CA 2006, section 232(2)).

A QTPIP indemnifies a director in respect of liability incurred to a third party (that is, a liability that is not incurred by the director to the company itself or to an associated company) (CA 2006, section 234(2)). However, a QTPIP must not indemnify a director in respect of fines imposed in criminal proceedings, regulatory penalties, the liabilities incurred in defending the director against criminal proceedings in which he or she is convicted, the liabilities incurred in defending civil proceedings brought by the company in which judgment is given against him or her or certain applications for relief in which the court refuses to grant him or her relief (CA 2006, section 234(3)).

A QPSIP indemnifies a director of a company that is a trustee of an occupational pension scheme against liability incurred in connection with the company's activities as trustee of the scheme (CA 2006, section 235(2)). A QPSIP must not indemnify a director in respect of fines imposed in criminal proceedings, regulatory penalties or liability incurred by the director in defending criminal proceedings in which he or she is convicted (CA 2006, section 235(3)). The existence of either a QTPIP indemnity or a QPSIP indemnity must be disclosed in the directors' report (CA 2006, section 236(1)).

A company may also provide directors with funds to pay for their expenses in defending any criminal or civil proceedings in connection with:

- any alleged negligence, default, breach of duty or breach of trust in relation to the company or an associated company; or
- making applications for relief under CA 2006, sections 661 and 1157 (CA 2006, sections 205(1) and (5)). Shareholder approval is not required (CA 2006, section 205(1)). These funds must be repaid if the director is convicted, receives an adverse judgment or is refused relief in respect of the proceedings (CA 2006, section 205(2)).

A company may also advance funds to a director to meet the costs of defending any regulatory investigation or action concerning him or her. Unlike loans made to a director to fund the costs of defending criminal and civil proceedings, loans made in respect of defending regulatory proceedings or action by a regulatory authority do not need to be repaid if judgment is given against the director. Shareholder approval is not required (CA 2006, section 206).

32 Exculpation of directors and officers

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

Generally, any provision that purports to exempt a company director from liability that would otherwise attach to him or her in connection with negligence, default, breach of duty or breach of trust in relation to the company, is void (CA 2006, section 232(1)). As mentioned in questions 30 and 31, there are exceptions to this rule for the provision of insurance, QTPIP indemnification and QPSIP indemnification provisions (CA 2006, section 232(2)).

A company's board may pre-authorise a director to enter into an arrangement that would otherwise amount to a conflict between the director's interests and those of the company, provided that the board is explicitly permitted to authorise such a conflict by the company's constitution (CA 2006, sections 175(4)(b) and (5)(b)). This authorisation will only be effective if:

- the meeting at which such authorisation is granted is capable of being quorate without the participation of the director to whom the authorisation relates; and
- the resolution granting this authorisation is passed without him or her voting on it (CA 2006, section 175(6)). If such authorisation is granted, the transaction will not be liable to be set aside by any common law rule that requires the company's shareholders to consent to such an arrangement (CA 2006, section 180(1)(a)).

Directors will also not be liable for entering into an arrangement that could amount to a breach of their duties to avoid conflicts of interest and to not accept benefits from third parties under CA 2006, sections 175 and 176, if the company's shareholders have approved that arrangement under CA 2006, chapter 4 of part 10 (which relates to transactions between a company and its directors requiring shareholder approval (see question 4)), or in respect of which that chapter provides that approval is not required (CA 2006, section 180(2)).

A company may also preclude the liability of a director for a breach of his or her duty to avoid conflicts of interest by including provisions in its articles of association under which a director may enter into certain arrangements that would otherwise amount to a breach of this duty (CA 2006, section 180(4)(b)). Further, the company may pre-authorise a breach of duty by a director in accordance with a relevant rule of law (for example, by the common law rule that a company may authorise a breach of duty if full and frank disclosure is made of all material facts (although, a company may not authorise an unlawful act)) (CA 2006, section 180(4)(a)).

Companies may also relieve their directors of liability for any negligence, default, breach of duty or breach of trust in relation to the company by ratifying such conduct after it has occurred, by way of a shareholder resolution (CA 2006, sections 239(1) and (2)). This resolution will only be effective if it passed without the director or any shareholder connected with him or her voting in favour of it (although, such persons are not prevented from counting in the quorum for the meeting) (CA 2006, section 239(4)). However, it is unlikely that shareholders will be permitted to ratify unlawful acts (CA 2006, section 239(7)).

33 Employees

What role do employees play in corporate governance?

Employees do not play a formal role in corporate governance, however, in practice, the most senior employees will be involved in the formulation of board practices and policies. A company's directors must have regard to the interests of its employees when discharging their duty to promote the success of the company (CA 2006, section 172(1)(b)).

A company's auditor may also demand such information from the company's employees as he or she requires to perform his or her duties as an auditor (CA 2006, section 499(1) and (2)).

34 Board and director evaluations

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

One of the main principles of the Code addresses the effectiveness of the board and this is addressed specifically in Code provision B.6. The main principle sets out that the board should undertake a formal and rigorous annual evaluation of its own performance and that of its committees and individual directors. Evaluation of the board should consider the balance of skills, experience, independence and knowledge of the company on the board, its diversity (including gender), how the board works together as a unit and other factors relevant to its effectiveness.

The board should state in the annual report how performance evaluation of the board, its committees and individual directors has been conducted. Evaluation of the board of FTSE 350 companies should be externally facilitated at least every three years. The external facilitator should be identified in the annual report and a statement made as to whether they have any other connection with the company. The non-executive directors, led by the senior independent director, should be responsible for performance evaluation of the chairman, taking into account the views of the executive directors (Code Provisions B.6.1, B.6.2 and B.6.3). The chairman should act on the results of the performance evaluation by recognising the strengths and addressing the weaknesses of the board and, where appropriate, proposing new members to be appointed or seeking the resignation of directors (see question 1).

Disclosure and transparency

35 Corporate charter and by-laws

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

The memorandum and articles of association of companies incorporated in England and Wales are publicly available from Companies House in Cardiff or London and can be accessed online without charge. Many companies also make their articles of association available on their websites.

36 Company information

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

The principal information that companies must disclose is as follows (however, this list is not exhaustive).

From 3 July 2016, the UK's market abuse provisions in FSMA 2000 were replaced by a new regime under the Market Abuse Regulation (596/2014/EU) (MAR) and the Market Abuse Regulation Instrument 2016. There are implications regarding, among other things, inside information, share dealings and market manipulation.

People with significant control (PSC) register

Section 81 and Schedule 3 of the SBEEA 2015 added a new Part 21A into the CA 2006, pursuant to which companies were required from 6 April 2016 to identify and record the people with 'significant control' over the company in a public register (PSC Register). Part 21A applies to all companies other than those to which chapter 5 of the DTRs applies. Limited liability partnerships and UK Societates Europaeae are not caught by the revised CA 2006 but must abide by the same requirements as they are carried across by the Limited Liability Partnerships (Register of People with Significant Control) Regulations 2016, which came into force on 30 June 2016. A PSC Register must be kept in addition to existing registers such as the register of directors and register of members. The PSC information must be filed with the central public register at Companies House.

A PSC is an individual who meets one or more of the following conditions in relation to a company:

- directly or indirectly holds more than 25 per cent of the shares;
- directly or indirectly holds more than 25 per cent of the voting rights;
- directly or indirectly holds the right to appoint or remove the majority of directors (this is defined as the directors holding the majority of voting rights);
- otherwise has the right to exercise, or actually exercises, significant influence or control over the company; or
- has the right to exercise, or actually exercises, significant influence or control over the activities of a trust or firm (not being a legal person, such as a partnership), which itself satisfies one or more of the first four conditions.

If any of the conditions listed above is met by a trust or firm, statutory guidance assists in identifying who should be in the PSC Register.

Financial and operating results of the company

A listed company is required to make public an annual financial report containing its audited financial statements, a management report and responsibility statements by the persons within the company who are responsible for its accounts. The annual financial report must be made public at the latest four months after the end of each financial year, and it must remain publicly available for at least 10 years (DTR4.1.3R, DTR4.1.4R and DTR4.1.5R).

A listed company must also make public a half-yearly report containing a condensed set of financial statements, an interim management report and responsibility statements. The half-yearly financial report must cover the first six months of the financial year and should be published as soon as possible but no later than three months after the end of the period to which the report relates, and it must remain publicly available for at least 10 years (DTR4.2.2R and DTR4.2.3R). A company may be liable to compensate any person who has acquired securities and suffered loss as a result of any untrue or misleading statement in or omission from the company's financial reports (section 90A FSMA 2000).

Share capital and voting rights

A person must notify the company of the percentage of the company's voting rights held by him or her (including voting rights held through that person's holding of financial instruments) if that percentage reaches, exceeds or falls below the following thresholds: 3, 4, 5, 6, 7, 8, 9, 10 per cent and each 1 per cent threshold thereafter up to 100 per cent (DTR5.1.2R). On receiving such a notification, a company must as soon as possible, and in any event by not later than the end of the trading day following receipt of the notification, make public all information contained in that notification (DTR5.8.12R(1)).

If a listed company acquires or disposes of its own shares, it must make public the percentage of voting rights attributable to those shares it holds as a result of the transaction as a whole where the percentage reaches, exceeds or falls below the threshold of 5 per cent or 10 per cent of the voting rights. This must be done as soon as possible, and in any event not later than four trading days after the acquisition or disposal of these shares (DTR5.5.1R). A listed company must also, at the end of each month during which an increase or decrease has occurred, make public the total number of voting rights and capital in respect of each class of issued shares and the total number of voting rights attaching to the shares that it holds in treasury (DTR5.6.1R). In addition, a listed company must also disclose the total number of voting rights as soon as possible (and no later than the end of the following business day) after an increase or decrease in the total number of voting rights following the completion of a transaction – unless the fluctuation in voting rights is deemed to be immaterial (DTR5.6.1AR). It is for the company to decide if an increase or decrease in the total number of voting rights is immaterial, but the FCA views a fluctuation of 1 per cent or more to be material both to the issuer and the public (DTR5.6.1BG).

Members of the board and key executives

A company must disclose certain information relating to its board and senior managers, including their names, addresses, functions, experience and expertise, previous directorships, criminal convictions and certain details of bankruptcies, receiverships or liquidations with which that person was associated (PR annex I of appendix 3, paragraph 14.1). A company must make similar disclosures when a new director is appointed (LR9.6.13R). A company must also notify a regulated information service (RIS) of any change to its board, including the appointment of a new director, the resignation, removal or retirement of an existing director or when there are important changes in the role, functions or responsibilities of a director (LR9.6.11R). A company must also notify an RIS of a current director's new directorships in any other publicly quoted company and of certain changes in a current director's circumstances (LR9.6.14R). Question 27 deals with the disclosure requirements of listed companies in relation to board practices under the Code.

Remuneration

The Directors' Remuneration Report Regulations 2002 require quoted companies to publish a report on their directors' remuneration, which must include specified information and be approved by the board of directors. These provisions are restated by CA 2006, sections 420 to 422.

For companies with financial years ending on or after 30 September 2013, the directors' remuneration reports are now required to be prepared and put to the shareholders in two distinct parts: the annual report on remuneration, which sets out remuneration payments made to directors in the year under review and a statement describing how the company intends to implement the approved remuneration policy in the next financial year; and the directors' remuneration policy setting out the company's policy on remuneration of directors. Copies of the report, which forms part of the annual report and accounts, must be sent to the registrar of companies (CA 2006, section 441).

The company must give its shareholders the opportunity to approve the remuneration report, including the remuneration policy, by way of an ordinary resolution (CA 2006, sections 439 and 439A) (see questions 4, 28 and 37). The report on directors' remuneration is subject to an advisory vote by shareholders on an annual basis; the remuneration policy is subject to a binding shareholder vote at least every three years and, once approved, sets the boundaries in which the company can remunerate its directors.

The annual report on remuneration must contain, inter alia, a single total figure of remuneration paid in the financial year being reported on for each person who served as a director at any time during that year, broken down to show salary, benefits and performance-related pay. The remuneration policy must contain, inter alia, description of each of the components of the remuneration package for directors, including the maximum amount payable under each component of remuneration, and details of performance measures (if applicable).

Inside information

MAR prescribes a regime for the disclosure and control of inside information (with further guidance contained in chapter 2 of the DTRs). Inside information is defined as precise information, which has not been made public, relating, directly or indirectly, to the company, and which, if it were made public, would be likely to have a significant effect on the price of the company's listed securities. Information is likely to have a 'significant effect' on price if it is information that a reasonable investor would be likely to use as part of the basis of his or her investment decisions. The definition of 'inside information' is wider under MAR than the previous regime, capturing inside information relating to spot commodity contracts.

A listed company (and one whose securities are the subject of an application for admission to listing) must disclose publicly as soon as possible any inside information that directly concerns it (article 17(1) MAR). There is an exception to the general obligation of disclosure, whereby the company may delay the public disclosure of inside information so as not to prejudice its own legitimate interests, as long as the omission would not be likely to mislead the public and the company can ensure the confidentiality of the information (article 17(4)). Immediately upon delayed inside information being publicly disclosed, the company must inform the FCA that disclosure was delayed, and, if requested by the FCA, provide a written explanation of how the above conditions were satisfied in respect of the delay.

An issuer may also be able to delay immediate public disclosure of inside information where it is a financial institution and disclosure of the information (for example, that relating to a liquidity problem) entails a risk of undermining the financial stability of the issuer and of the financial system (article 17(5)).

Share dealing

Under article 19 MAR, which has replaced chapter 3 of the DTRs and the Model Code, persons discharging managerial responsibilities (PDMRs) and any 'persons closely associated' with them must notify an issuer, and the FCA, of the occurrence of all transactions conducted on their own account relating to the shares or debt instruments of that issuer (or derivatives or other financial instruments linked thereto). This provision is only applicable once transactions of a value totalling at least €5,000 have been carried out in respect of that company's shares within a calendar year. Notifications must be made promptly and no later than three business days after the date of the transaction, and should set out details relating to the transaction, including, inter alia, the name of the person concerned, the reason for the notification, and the price and volume of the transaction. The company must then ensure that the information notified to it is made public promptly and no later than three business days after the transaction (in practice, this would occur via a Regulatory Information Service).

Furthermore, a PDMR must not conduct any transactions relating to the financial instruments of the relevant issuer during a closed period of 30 calendar days before the issuer releases any interim financial report or year-end report required by national law or the rules of the relevant securities exchange. MAR does not, however, retain the Model Code's requirement that PDMRs seek to prohibit their 'connected persons' from dealing in the issuer's securities in close periods.

There are limited exemptions to the closed period rule. These include certain transactions relating to employee share schemes, transactions where the beneficial interest in the relevant security does not change, and where there are exceptional circumstances that require the immediate sale of shares. Certain exemptions which were available under the Model Code are not reproduced in MAR, however, such as those that permit certain dealings connected to a rights issue or a takeover or dealings under a trading plan where the PDMR has no influence or discretion.

Governance structure and policies

Companies with a premium listing are required to include a statement in their annual report setting out how they have applied the main principles of the Code (LR9.8.6R(5)) (see question 1). This statement must be made in a manner that would enable shareholders to evaluate how these main principles have been applied.

The annual report must also include a statement as to whether the premium listed company has complied throughout the accounting period with all relevant provisions set out in the Code and provide reasons for any non-compliance (LRs 9.8.6R(6) and 9.8.7R) (see question 1). The Code also requires a number of other disclosures, and these are outlined in question 27. The DTRs require listed companies to make a corporate governance statement in the directors' report (DTR7.2.1R). This statement must outline which corporate governance code the company is subject to and whether it has complied with its provisions, or alternatively it must explain any reasoning for non-compliance (DTRs 7.2.2R and 7.2.3R). Companies with a premium listing should adhere to the Code (see question 1), and by applying the Code's 'comply or explain' approach a company will also satisfy the DTRs (DTR7.2.4G). However, companies with a standard listing are not subject to the Code and DTR7.2.1R creates an additional disclosure requirement to 'comply or explain', albeit separate from the Code.

Audit committees or bodies carrying out equivalent functions

Companies with a premium listing or a standard listing must make a statement available to the public disclosing which body it has appointed to carry out the audit committee functions set out in DTR7.1.3R and how it is composed (DTR7.1.5R). This statement should include the names of the chairman and members of the audit committee and the qualifications of all members of the audit committee during the relevant period. It may be included in the corporate governance statement that the company is required to make under DTR7.2 (DTR7.1.6G).

If the company is a FTSE 350 company, a statement of compliance with the provisions of the CMA Order 2014 (article 7.1 CMA Order 2014), which applies to financial years beginning on or after 1 January 2015, is required.

Class announcements

The Listing Rules classify transactions by reference to a number of different percentage ratios that are set out in annex 1 to LR10 (the class tests) (see question 4). Under LR10 there are two classes of transactions: class 1 and class 2. The disclosure requirements for these two classes of transaction are currently defined as follows:

Class 1

A premium listed company must, in relation to a class 1 transaction (where any percentage ratio is 25 per cent or more), send an explanatory circular to the company's shareholders requesting prior shareholder approval in a general meeting. Any agreement effecting the transaction should be conditional on obtaining that approval (LR10.5.1R). The company must notify an RIS in accordance with the provisions of LR10.4.1R (LR10.5.1R(1)). This notification should be made as soon as possible after the terms of the transaction have been agreed (LR10.4.1R).

A supplementary notification must be made to an RIS as soon as possible if there is a significant change affecting any matter in the announcement, or a significant matter arises that should have been mentioned if it had arisen at the time of preparation of the notification (LR10.4.2R). This supplementary notification must comply with the provisions of LR10.4.2R. LR10.5.4R, which came into force on 1 October 2012 (as amended in April 2013 to reflect the changes to the UK regulatory framework), also requires a supplementary circular to be sent to shareholders if, before the date of the general meeting to approve the transaction, a listed company becomes aware of a material change affecting the matter that required disclosure in the explanatory circular, or of a new matter that would have required disclosure in a circular. It should be noted that in certain circumstances, where the listed company is in severe financial difficulty and is making a class 1 disposal, the FCA may waive the requirement for an explanatory circular and shareholder consent if certain requirements are met (LR10.8).

Where this is a material change to the terms of the transaction (which the FCA generally considers to be an increase of 10 per cent or more in the consideration payable (LR10.5.3G)), the requirements of LR10.5.1R must be complied with again, separately (LR10.5.2R). The FCA amended LR10.5.2R, effective from 1 October 2012, so that it only applies to material changes occurring after shareholder approval has initially been obtained. This is intended to avoid overlap with LR10.5.4R.

Class 2

A premium listed company must, in relation to a class 2 transaction (where any percentage ratio is 5 per cent or more but each is less than 25 per cent), notify an RIS. This notification must be made as soon as possible after the terms of the transaction are agreed (LR10.4.1R). The information that must be included in the notification (which is the same information that must be included in a class 1 transaction notification) is set out in LR10.4.1R(2). A supplementary notification must also be made where a significant change or significant matter arises (LR10.4.2R).

Reverse takeover

Owing to concerns about reverse takeovers being used as a 'back-door' listing route, the requirements for reverse takeovers that were previously contained in LR10.6 were removed and replaced with requirements under a new LR5.6 as of 1 October 2012. These requirements are aimed at incorporating concepts from the UKLA Technical Note: Reverse Takeovers. LR5.6 has increased the scope of the acquisitions defined as reverse takeovers, and made the requirements of the reverse takeover regime more proportionate and less onerous. To facilitate these changes a broader definition of 'reverse takeover' has been inserted at LR5.6.4R. The existing exemption from the reverse takeover regime has also been restricted such that only a listed company acquiring a company that is listed in the same listing category will be exempt (LR5.6.2R). In addition, companies with standard listings now fall within the reverse takeovers regime (LR5.6.1R(2)).

In particular, the rules now require a company to contact the FCA as early as possible before announcing a reverse takeover, that has been agreed or is in contemplation, to discuss whether a suspension of listing is required (LR5.6.6R(1)). Where a leak of transaction details has occurred an issuer must contact the FCA to request a suspension as early as possible (LR5.6.6R(2)). In December 2012 the FSA published new guidance on when a suspension of listing would be necessary under new LR5.6.6R and LR5.6.7G (UKLA Technical Note: Reverse Takeovers). This guidance suggests that a reverse takeover would be in contemplation where an approach has been made to the target's board, or an exclusivity period has been entered into with the target, or the issuer has been given access to begin due diligence. If the FCA is satisfied that there is sufficient publicly available information about the proposed transaction and the issuer then a suspension will not be required (LR5.6.8G). LR5.6.10G to LR5.6.18R set out circumstances in which the FCA will generally be satisfied that a suspension is not required (LR5.6.9G), however RIS announcements will be required from the issuer under LR5.6.10G, LR5.6.12G and LR5.6.15G.

An issuer with a premium listing must in relation to a reverse takeover comply with the requirements of class 1 requirements in LR10.5 for that transaction (preparation of a class 1 circular and shareholder approval) (LR5.6.3).

Related-party transactions

Related-party transactions are classified by the nature of the relationship between the parties to the transaction. Definitions of a 'related party' and of a 'related-party transaction' can be found under LR11.1.4R and LR11.1.5R respectively and include directors and substantial shareholders. A substantial shareholder means any person who holds or controls the exercise of 10 per cent or more of the voting rights in a company (LR11.1.4AR). The definition of 'substantial shareholder' includes a carve-out that allows the voting rights of shares to be disregarded when calculating this percentage if the shares are held for a period of five days or less, the voting rights are not exercised during this period, no attempt has been made directly or indirectly to influence the management and the shares are held in the ordinary course of business (LR11.1.4AR(2)). The definition of an 'associate' of a related party has been expanded to include partnerships in which a related party holds or controls a voting interest of 30 per cent or more in the partnership (LR appendix 1).

The FSA also published a consultation paper CP12/25 (Enhancing the Effectiveness of the Listing Regime and Feedback on CP12/2), which proposed additional requirements for premium-listed issuers with a 'controlling shareholder'. A controlling shareholder is a shareholder who itself, or together with persons acting in concert with it, holds, either directly or indirectly, 30 per cent of the shares or voting power in the issuer or its parent, or both. Feedback to this consultation resulted in a further consultation, CP13/15 (Feedback on CP12/25: Enhancing the Effectiveness of the Listing Regime and Further Consultation), published in November 2013. CP13/15 confirmed that the FCA intends to proceed with the requirement that 'relationship' agreements be mandatory for all premium-listed companies with a 'controlling shareholder', and feedback to CP13/15 was published in May 2014, following which this requirement became effective subject to transitional provisions.

LR15.5.3G provides that closed-ended investment funds are also covered by the related party transaction provisions of LR11 and LR15.5.4R provides that an investment manager of a closed-ended investment fund is a related party for the purposes of LR11. However, closed-ended investment funds and the investment managers of such funds are exempt from the provisions of LR11.1.7R to LR11.1.11R in certain circumstances set out in LR15.5.5R. In the context of a related-party transaction, a premium listed company must notify an RIS of the transaction in accordance with the provisions of LR10.4.1R (notifications of class 2 transactions) and also provide the name of the related party and the details of the nature and extent of the related party's interest in the transaction or arrangement (LR11.1.7R(1)). An explanatory circular, approved by the FCA and containing the information required by LR13.3 and LR13.6, should also be sent to shareholders (LR11.1.7R(2)). Under LR8.2.1R(7) a sponsor is required to provide the confirmation needed under LR13.6.1R(5). Shareholder approval is required before the transaction is entered into or, if obtaining shareholder approval is a condition of the transaction, prior to completion. The related party and its associates should not vote on any resolution to approve the transaction (LR11.1.7R(4)).

LR11.1.7AR has included the material change requirement referred to under 'Class 1' in LR11 so that shareholders are also protected for related party transactions. In addition, the exemptions from the requirements of related party transactions in LR11 annex 1R have been expanded to include loans to fund defence and regulatory investigations, as these operate in a similar way to indemnities and are permitted under CA 2006, section 206.

Gender pay gap reporting

In parallel with the increased focus on diversity at board level discussed in the response to question 23, there have been recent government efforts, via regulations enacted under section 78 of the Equality Act 2010, to improve transparency in respect of gender pay in both the private and public sectors. Under the Equality Act 2010 (Gender Pay Gap Information) Regulations 2017 (SI 2017/353), which came into force on 6 April 2017, private and voluntary sector employers with 250 or more employees must analyse their gender pay gap as at the 'snapshot date' of 5 April each year, and publish relevant pay information at any time within 12 months of that date, both on the employer's website and a designated government website. The first report must therefore be published by 4 April 2018, and must include information detailing the difference between the average earnings of male and female employees, expressed as a percentage of male earnings.

To help employers adapt to the new regime, the Government Equalities Office and Acas (the Advisory, Conciliation and Arbitration

Update and trends

New developments:

- The new DTR 7.2.8A (transposing EU Directive 2014/95 into national law) is applicable to large issuers for financial years commencing on or after 1 January 2017. The corporate governance statements of those affected must now contain additional disclosures in respect of certain environmental and social matters (including diversity) (see question 23).
- Certain private and public sector employers must publish annually information relating to their gender pay gaps, due to regulations enacted under section 78 of the Equality Act 2010, which came into force on 6 April 2017 (see question 36).
- Under section 54 of the Modern Slavery Act 2015, certain commercial organisations must disclose the steps taken to ensure that slavery and human trafficking are not taking place in their supply chains or businesses (see question 36).

Prospective developments:

- The government is currently analysing feedback from the consultation on its Green Paper published in November 2016, in preparation for possible corporate governance reform. The FRC will be carrying out a fundamental review of the Code in 2017 to support this process (see question 1).
- The United Kingdom has triggered the negotiation process for withdrawing from the European Union. With effect from 29 March 2019, the UK will cease to be a member of the EU and will cease to be bound by European legislation, except to the extent that it has been incorporated into domestic legislation and not repealed. It is, however, too early to speculate on the consequences of this for corporate governance in the UK.

Service) have published non-statutory guidance, entitled 'Managing gender pay reporting'.

Modern Slavery Act Transparency Statement
A further notable development has been the introduction of the Modern Slavery Act 2015. In accordance with section 54 of the Modern Slavery Act 2015, certain commercial organisations must disclose (including on their website) steps (or a lack thereof) taken to ensure that slavery and human trafficking are not taking place in their supply chains or any part of their business. This applies to organisations which carry on a business in the supply of goods or services in the UK and have a total annual turnover of not less than £36 million and applies to financial years ending on or after 31 March 2016. Relevant entities must publish the statement as soon as reasonably practical after the end of the financial year, with Home Office guidance recommending publication within six months of this date.

Hot topics

37 Say-on-pay

Do shareholders have an advisory or other vote regarding executive remuneration? How frequently may they vote?

A quoted company must give its shareholders the opportunity to approve its directors' remuneration report once a year by way of an ordinary resolution at its annual general meeting and must notify its shareholders of its intention to move such a resolution at that meeting (CA 2006, sections 439(1) and (4)). The company must also notify its shareholders of its intention to move, as an ordinary resolution, a resolution approving the directors' remuneration policy at least every three years (CA 2006, section 439A(1)) (see questions 4 and 28 for further detail). Many companies (notably, those with a December year-end) are due to put remuneration policies to a binding ordinary shareholder resolution in accordance with section 439A CA 2006 in the 2017 AGM season, as this year marks the third anniversary since they were first required to do so in 2014.

Sections 227B and 227C CA 2006 prohibit a quoted company from making a remuneration payment or payment for loss of office unless the payment is consistent with the approved remuneration policy, or such payment is otherwise approved by the shareholders. Long-term incentive plans and employee share schemes for listed companies generally require separate shareholder approval (LR9.4.1R).

Failure to comply with the requirements of CA 2006, sections 439 or 439A means an offence is committed by every director in default (CA 2006, section 440(1)). Failure to put the resolutions to a vote at the meeting means an offence is committed by each existing director (CA 2006, section 440(2)). An offence under CA 2006, section 440 could lead to the company's directors being subject to a fine not exceeding £1,000 (CA 2006, section 440(1), (2) and (4)). Shareholders holding five per cent or more of the share capital carrying voting rights may also requisition a vote on any matter under the general meetings requisition procedure under CA 2006, section 303.

38 Shareholder-nominated directors

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

In practice, shareholders do on occasion suggest possible directors to boards and boards sometimes seek shareholder views on proposed directors. However, the only manner in which a shareholder can nominate a director without the recommendation of the board is by requiring the board to put a resolution on the agenda at the company's annual general meeting or to convene an extraordinary general meeting to consider such a resolution (see questions 3 and 7).

39 Shareholder engagement

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

Traditionally, directors engaged with shareholders at the annual general meeting and delegated shareholder engagement to the company's investor relations team. The increasing powers accorded to shareholders in relation to directors' remuneration has led to increasing interaction between directors and shareholders outside AGM season. Most companies will have an investor relations team and will set up calls with investors which will be attended by directors or senior management. However, except as described in this chapter, shareholder engagement is a commercial matter for the relevant company. In general, the largest shareholders expect regular updates on company performance and strategy as well as consultation on major changes to the business, such as large corporate transactions, analysis of the company's response to major events that could have a serious impact on the business and meetings instigated by the shareholder to discuss particular issues. Smaller shareholders may make use of their membership of an investment organisation in order to gain access to information and analysis which would otherwise only be available to larger shareholders. It is not uncommon for institutional shareholders to criticise a company's approach in the media.

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Sources of corporate governance rules and practices

1 Primary sources of law, regulation and practice

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

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

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

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

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

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

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

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

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

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

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

- CII, Corporate Governance Policies;
- Teachers Insurance and Annuity Association – College Retirement Equities Fund (TIAA-CREF), TIAA-CREF Policy Statement on Corporate Governance;
- California Public Employees' Retirement System (CalPERS), Global Governance Principles; and
- Proxy voting policies of large institutional investors such as BlackRock, Vanguard, State Street and Fidelity.

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

Unlike many corporate governance codes in the European Union and other parts of the world that call for voluntary adoption of their substantive provisions or 'comply or explain' disclosure requirements, the corporate governance rules in the US are generally mandatory. However, most US federal securities regulation of listed issuers is disclosure-driven and, even where substantive matters are addressed, disclosure is most often used as the vehicle to achieve a desired objective or to add transparency to matters deemed worthy of public attention. For example, with respect to executive compensation, the rules provide for extensive disclosure requirements rather than substantive requirements. In addition, the Sarbanes-Oxley Act mandates disclosure of whether a company has adopted a code of ethics with specified provisions or whether a company has an audit committee financial expert but does not require that a listed issuer have either.

2 Responsible entities

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

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

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

The views of proxy advisory firms Institutional Shareholder Services and Glass Lewis are also influential.

The rights and equitable treatment of shareholders

3 Shareholder powers

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

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

For many years, it was common practice for directors to be elected by a plurality of shareholders that can either vote in favour of, or withhold their votes from, the director candidates nominated by the board; 'withheld' votes are not counted. Accordingly, absent a contested election, the candidates nominated by the board are automatically elected whether or not a majority of shareholders vote for them. Relatively recently, shareholders have pressed companies for the ability to veto the election of a particular director nominee or nominees in the context of an uncontested election. This can be achieved through the adoption of charter or by-law provisions requiring that director nominees receive the approval of a 'majority of the votes cast' to be elected, or, in lieu of a charter or by-law provision, the adoption of corporate policies that effectively require a director who has not received a majority of the votes cast to resign. In 2006, the Delaware legislature adopted amendments to the DGCL that facilitate both of these options. Specifically, the amended DGCL, section 141(b) expressly permits a director to irrevocably tender a resignation that becomes effective if he or she fails to receive a majority vote in an uncontested election. The amended DGCL, section 216 provides that a by-law amendment adopted by shareholders specifying the vote required to elect directors may not be repealed or amended by the board alone (generally by-law provisions may be amended by the board).

The proportion of companies in the Standard & Poor's (S&P) 500 that have adopted some form of majority voting in uncontested director elections has increased dramatically from 16 per cent in 2006 to over 95 per cent in 2016.

Shareholders can also nominate their own director candidates either before or at the annual general meeting (AGM). To solicit the proxies needed to elect their candidates, however, at a company that has not adopted 'proxy access' (discussed in question 38) a shareholder must mail to all other shareholders, at his or her own expense, an independent proxy solicitation statement that complies with the requirements of section 14 of the Exchange Act. Given these constraints, independent proxy solicitations are rare and usually undertaken only in connection with an attempt to seize corporate control (see also question 38).

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

Shareholders' liability for corporate actions is generally limited to the amount of their equity investment. In keeping with their limited liability, shareholders play a limited role in the control and management of the corporation. As discussed in question 4, a number of corporate decisions require shareholder approval. In addition, shareholders can typically enjoin ultra vires acts (see DGCL, section 124), and vote on certain issues of fundamental importance at the AGM, including the election of directors (see DGCL, section 216 and question 4).

4 Shareholder decisions

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

Under state corporate law, shareholders typically have a right to participate in the following types of decisions:
- election of directors, held at least annually;
- approval or disapproval of amendments to the corporation's certificate of incorporation or by-laws, although the board is also typically authorised (in the certificate of incorporation) to amend the by-laws without shareholder approval (see DGCL, sections 109, 241 and 242);
- approval or disapproval of fundamental changes to the corporation not made in the regular course of business, including mergers, dissolution, compulsory share exchanges, or disposition of substantially all of the corporation's assets (see, for instance, DGCL, sections 251(c), 271 and 275); and
- authorisation of additional shares for future issuance by the corporation. Upon shareholder authorisation, the board has discretion to determine when and how many shares to issue at any time.

Commencing in 2011, the Dodd-Frank Act requires US public companies to conduct a separate shareholder advisory vote on:
- executive compensation – to be held at least once every three calendar years;
- whether the advisory vote on executive compensation should be held every year, every two years or every three years – to be held at least once every six calendar years; and

- certain 'golden parachute' compensation arrangements in connection with a merger or acquisition transaction that is being presented to shareholders for approval.

The rules of the NYSE and Nasdaq also require that shareholder approval be obtained prior to:
- any adoption of a stock option or purchase plan pursuant to which officers or directors may acquire stock, subject to limited exceptions;
- issuance of common stock to directors, officers, substantial security holders or their affiliates if the number of shares of common stock to be issued exceeds either 1 per cent of the number of shares of common stock or 1 per cent of the voting power outstanding before the issuance, with some exceptions including in connection with certain transactions by early stage companies (NYSE), or could result in an increase in outstanding common shares or voting power of 5 per cent or more (Nasdaq);
- issuance of common stock that will have voting power equal to or greater than 20 per cent of the voting power prior to such issuance or that will result in the issuance of a number of shares of common stock that is equal to or greater than 20 per cent of the number of shares of common stock outstanding prior to such issuance, subject to certain exceptions; and
- issuance of securities that will result in a change of control of the company.

5 Disproportionate voting rights

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

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

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

The CII and CalPERS have recently expressed their opposition to non-voting shares.

6 Shareholders' meetings and voting

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

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

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

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

DGCL, section 211 permits a Delaware corporation to hold a meeting of shareholders virtually if it adopts measures to enable shareholders to participate in and vote at the meeting and verify voter identity, and maintains specified records. A growing number of US companies have held virtual annual shareholder meetings, typically in one of two formats: exclusively online with no ability for a shareholder to attend an in-person meeting; or a hybrid approach whereby an in-person meeting is held that is open to online participation by shareholders who are not physically present at the meeting. The primary benefits of virtual shareholder meetings are increased shareholder participation and cost savings. In April 2017, the New York City Pension Funds announced a campaign to vote against governance committee members at companies that hold exclusively virtual annual shareholder meetings.

7 Shareholders and the board

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

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

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

Under circumstances detailed in Rule 14a-8 under the Exchange Act, a reporting company must include a shareholder's proposal in the company's proxy materials and identify the proposal in its proxy form. The shareholder may also submit a 500-word supporting statement for inclusion in the company's proxy solicitation materials. This allows the proponent to avoid the costs associated with an independent solicitation. To qualify, a shareholder must have continuously held at least US$2,000 in market value or 1 per cent of the company's securities entitled to vote for at least one year by the date the shareholder submits the proposal. The shareholder must continue to hold those securities until the date of the meeting. Under specific circumstances, a company is permitted to exclude a shareholder proposal from its proxy solicitation, but only after demonstrating to the SEC that it is entitled to the exclusion (for example, if the proposal deals with a matter relating to the company's ordinary business operations).

Effective since September 2011, companies can no longer exclude from their proxy materials shareholder proposals (precatory or binding) relating to by-law amendments establishing procedures for shareholder nomination of director candidates and inclusion in the company's proxy materials, as long as the proposal is otherwise not excludable under Rule 14a-8. This amendment to Rule 14a-8 is facilitating the development of 'proxy access' via private ordering at companies chartered in states where permissible, as shareholders are able to institute a shareholder nomination regime via binding by-law amendment or request, via precatory shareholder proposal, that such a by-law be adopted by the board. The private ordering process has gained considerable momentum since the beginning of 2015; see question 38.

As noted in question 6, shareholders may act by written consent without a meeting unless the certificate of incorporation provides otherwise. The majority of companies in the S&P 500 do not permit shareholder action by written consent.

8 Controlling shareholders' duties

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

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

9 Shareholder responsibility

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

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

Corporate control

10 Anti-takeover devices

Are anti-takeover devices permitted?

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

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

Variations on the traditional poison pill have been designed to make it even more difficult for potential hostile acquirers by restricting the ability of newly placed directors to redeem the poison pill. For example, a 'dead-hand' provision in a poison pill provides that only the specific directors who originally approved the adoption of the poison pill may redeem it. A 'no-hand' poison pill cannot be redeemed at all, and a 'chewable' poison pill gives the incumbent directors a specific period to negotiate before the pill becomes effective. Some states allow the use of dead-hand, no-hand and chewable poison pills (although Delaware does not permit the use of dead-hand or no-hand poison pills). Note that shareholder activists and proxy advisory firms tend to disfavour poison pills that have not been approved by shareholders.

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

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

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

Under the NYSE and Nasdaq listing rules, listed companies are prohibited from using defensive tactics that discriminate among shareholders.

11 Issuance of new shares

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

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

- any adoption of a stock option or purchase plan pursuant to which officers or directors may acquire stock, subject to limited exceptions;
- issuance of common stock to directors, officers, substantial security holders or their affiliates if the number of shares of common stock to be issued exceeds either 1 per cent of the number of shares of common stock or 1 per cent of the voting power outstanding before the issuance, with some exceptions including in connection with certain transactions by early stage companies (NYSE), or could result in an increase in outstanding common shares or voting power of 5 per cent or more (Nasdaq);
- issuance of common stock that will have voting power equal to or greater than 20 per cent of the voting power prior to such issuance or that will result in the issuance of a number of shares of common stock that is equal to or greater than 20 per cent of the number of shares of common stock outstanding prior to such issuance, subject to certain exceptions; and
- issuance of securities that will result in a change of control of the company.

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

12 Restrictions on the transfer of fully paid shares

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

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

13 Compulsory repurchase rules

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

Under DGCL, section 253, a corporation owning at least 90 per cent of the outstanding shares of each class of the stock of a corporation may merge that other corporation into itself without requiring shareholder approval (known as a 'freeze-out' or 'short-form' merger). Minority shareholders who object to the merger are entitled to appraisal rights (see question 14).

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

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

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

14 Dissenters' rights

Do shareholders have appraisal rights?

Under DGCL, section 262, shareholders who do not vote in favour of a merger or consolidation are entitled to an appraisal by the Delaware Court of Chancery of the fair value of their shares unless:
- the shares were listed on a national securities exchange (for example, the NYSE or Nasdaq);
- the shares were held of record by more than 2,000 holders; or
- the merger or consolidation did not require a shareholder vote.

Notwithstanding the applicability of the above points, appraisal rights will be available if shareholders are required to accept anything other than:
(i) shares of the surviving or resulting company;
(ii) shares listed on a national securities exchange;
(iii) cash in lieu of fractional shares; or
(iv) any combination of (i) to (iii).

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

The responsibilities of the board (supervisory)

15 Board structure

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

The predominant board structure for listed companies in the US is one-tier. DGCL, section 141 states that 'the business and affairs of every corporation organised under this chapter shall be managed by or under the direction of a board of directors, except as may be otherwise provided in this chapter or in its certificate of incorporation'. The board of directors delegates managerial responsibility for day-to-day operations to the CEO and other senior executives. Members of senior management may serve on the board, but they are not organised as a separate management board.

16 Board's legal responsibilities

What are the board's primary legal responsibilities?

The primary legal responsibility of the board is to direct the business and affairs of the corporation (see DGCL, section 141). While the functions of a board are not specified by statute, it is generally understood, as noted in the ALI's Principles of Corporate Governance and other codes of best practice, that board functions typically include:
- selecting, evaluating, fixing the compensation of and, where appropriate, replacing the CEO and other members of senior management;
- developing, approving and implementing succession plans for the CEO and senior executives;
- overseeing management to ensure that the corporation's business is being run properly;
- reviewing and, where appropriate, approving the corporation's financial objectives and major corporate plans, strategies and actions;
- understanding the corporation's risk profile and reviewing and overseeing the corporation's management of risks;
- reviewing and approving major changes in the auditing and accounting principles and practices to be used in preparing the corporation's financial statements;
- establishing and monitoring effective systems for receiving and reporting information about the corporation's compliance with its legal and ethical obligations, and articulating expectations and standards related to corporate culture and the 'tone at the top';
- understanding the corporation's financial statements and monitoring the adequacy of its financial and other internal controls, as well as its disclosure controls and procedures;
- evaluating and approving major transactions such as mergers, acquisitions, significant expenditures and the disposition of major assets;
- providing advice and counsel to senior management;
- reviewing the process for providing adequate and timely financial and operational information to management, directors and shareholders;
- establishing the composition of the board and its committees, board succession planning and determining governance practices;
- retaining independent advisers in performance of committee duties and decision-making;
- assessing the effectiveness of the board, its committees or individual directors, or both; and
- performing such other functions as are necessary.

17 Board obligees

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

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

18 Enforcement action against directors

Can an enforcement action against directors be brought by, or on behalf of, those to whom duties are owed?

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

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

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

19 Care and prudence

Do the board's duties include a care or prudence element?

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

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

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

In 2003, the Delaware Court of Chancery rendered an important opinion concerning the 'duty of good faith' of corporate directors (*In Re The Walt Disney Co* (Del Ch 2003)). In this opinion, the court held that directors who take an 'ostrich-like approach' to corporate governance and 'consciously and intentionally disregard their responsibilities', adopting a 'we don't care about the risks' attitude may be held liable for breaching their duty to act in good faith. The opinion was rendered on a motion to dismiss for failure to state a claim. The opinion is notable for its sharp focus on the importance of good faith, in addition to due care and loyalty, when considering director conduct. By characterising the alleged lack of attention by directors as a breach of the duty of good faith rather than a breach of the duty of care, the court effectively stripped the directors of the protection afforded by the Delaware Director Protection Statute (which is described in greater detail in question 32).

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

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

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

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

20 Board member duties

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

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

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

21 Delegation of board responsibilities

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

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

- adopt, amend or repeal any by-law of the corporation;
- amend the corporation's certificate of incorporation (except that a board committee may make certain specified decisions relating to the rights, preferences or issuance of authorised stock, to the extent specifically delegated by the board);
- adopt an agreement of merger or consolidation;
- recommend to shareholders the sale, lease or exchange of all or substantially all of the corporation's property and assets;
- recommend to shareholders a dissolution of the corporation or a revocation of a dissolution;
- approve, adopt or recommend to shareholders any action or matter that is required to be submitted to shareholders for approval;
- declare a dividend, unless that power is expressly provided for in the certificate of incorporation, resolution or by-laws; and
- authorise the issuance of stock or adopt a certificate of ownership and merger, unless that power is expressly provided for in the certificate of incorporation, resolution or by-laws.

The Sarbanes-Oxley Act and the NYSE and Nasdaq listing rules also require that each listed company have an audit committee comprising independent directors who have responsibility for certain audit and financial reporting matters. As required by the Dodd-Frank Act, NYSE and Nasdaq listing rules also require that each listed company have a compensation committee comprising independent directors who are responsible for certain matters relating to executive compensation. NYSE listing standards require that each listed company have a nominating or corporate governance committee comprising independent directors who are responsible for director nominations and corporate governance. Nasdaq listing rules require independent directors (or a committee of independent directors) to have responsibility for certain decisions relating to director nominations. (See questions 25 and 27.) These committees are permitted to delegate their responsibilities to subcommittees solely comprising one or more members of the relevant committee.

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

22 Non-executive and independent directors

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

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

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

- a person who is an employee of the listed company or is an immediate family member of an executive officer of the listed company;
- a person who receives, or is an immediate family member of a person who receives, compensation directly from the listed company, other than director compensation or pension or deferred compensation for prior service (provided such compensation is not contingent in any way on continued service), of more than US$120,000 per year;
- a person who is a partner of, or employed by, or is an immediate family member of a person who is a partner of, or employed (and works on the listed company's audit) by a present or former internal or external auditor of the company;
- a person, or an immediate family member of a person, who has been part of an interlocking compensation committee arrangement; or
- a person who is an employee or is an immediate family member of a person who is an executive officer, of a company that makes payments to or receives payments from the listed company for property or services in an amount that in a single fiscal year exceeds the greater of 2 per cent of such other company's consolidated gross revenues or US$1 million.

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

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

23 Board size and composition

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

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

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

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

The SEC requires companies to provide the following proxy statement disclosures relating to board composition:

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

There is increasing concern in the institutional investor community about the lack of gender and racial diversity on public company boards of directors, as well as long-tenured directors and lack of board refreshment. SEC rules currently require companies to provide proxy statement disclosure regarding whether and, if so, how the nominating committee considers diversity in identifying nominees for director and, if the nominating committee has a policy with regard to the consideration of diversity in identifying director nominees, how this policy is implemented and how the nominating committee or the board assesses the effectiveness of its policy. In March 2017, State Street Global Advisors published guidance in connection with a new initiative to promote greater gender diversity on corporate boards. State Street indicated that it will initially target companies that do not have any female directors and, beginning in 2018, it may vote against the chair of a nominating or governance committee of a company that fails to take action to increase the number of women on its board.

24 Board leadership

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

There is no legal requirement or listing rule that mandates that the positions of board chairman and CEO be held separately or jointly. Corporate boards are generally free to decide for themselves the leadership structure of the board and company (although the corporate charter or by-laws could provide otherwise). Shareholder proposals calling for a separation of the board chairman and CEO roles have become increasingly common in recent years.

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

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

Several best practice codes recommend a clear division of responsibilities between a board chairman and CEO to ensure that the board maintains its ability to provide objective judgement concerning management. Some recommend that the board should separate the roles of board chairman and CEO, while others recommend designating a lead outside or independent director for certain functions. For example, the NACD's Report on Director Professionalism recommends appointing an independent board leader to:

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

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

- the scope of the proposal, such as whether it is precatory or binding;
- the company's current board leadership structure, including recent transitions in board leadership and the designation and responsibilities of an independent lead director;
- the company's governance structure and practices to assess whether more independent oversight at the company may be advisable; and
- the company's financial performance compared to its peers and the market as a whole.

Common practice is to combine the roles of CEO and chairman; however, separation of the roles has become increasingly prevalent at S&P 500 companies over the past 10 years – the roles were separated at 48 per cent of S&P 500 companies in 2016 up from 33 per cent in 2006. Chairmen who qualified as independent were in place at 27 per cent of S&P 500 companies in 2016 compared to 10 per cent in 2006. The vast majority of companies that do not have an independent chairman have appointed a lead or presiding director.

25 Board committees

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

Since 1999, the NYSE and Nasdaq listing rules have required that listed companies have audit committees consisting entirely of independent directors (prior to that time, a majority of independent directors had been a long-standing audit committee requirement for companies listed on the NYSE). In 2003, the NYSE and Nasdaq adopted listing rules that also require companies to have compensation and nominating or governance committees (or committees that perform those functions) consisting entirely of independent directors, although Nasdaq permits nomination decisions (and, until 2014, permitted certain executive compensation decisions) to be made by a majority of independent directors (definitions of independence are provided in question 22). The Sarbanes-Oxley Act requires that all boards of companies with listed securities have audit committees composed entirely of directors who receive no compensation from the company other than directors' fees and are not affiliated with the company. In addition, companies are required to disclose the name of at least one audit committee member who is an 'audit committee financial expert' as defined by the SEC, or explain why they do not have one. The NYSE and Nasdaq rules also require that the audit committee comprises at least three members and impose requirements with respect to the financial literacy of audit committee members. Effective beginning in 2014, each Nasdaq listed company must have, and certify that it has and will continue to have, a compensation committee of at least two members, each of whom must be an independent director; the NYSE does not require a minimum number of members of the compensation committee. As required by the Dodd-Frank Act, the NYSE and Nasdaq each adopted heightened independence standards for compensation committee members that became effective in 2014 and take into account the source of compensation received by the director and whether the director is affiliated with the company or any subsidiary.

26 Board meetings

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

Under state law, the corporation's by-laws or certificate of incorporation prescribe the requirements for board meetings and may or may not prescribe a set number of meetings. Generally, it is believed that a board should meet at least once per financial-reporting quarter. However, most boards of large publicly traded corporations meet more frequently. For example, companies represented on the S&P 500 held 8.5 board meetings on average in 2016. SEC rules require companies to disclose the total number of board and committee meetings held during the past year and provide details regarding director attendance at such meetings.

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

27 Board practices

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

As discussed in response to question 36, the SEC requires disclosure of certain board practices, including disclosures about the identity and compensation of directors and the composition and activities of the audit, compensation and nominating committees.

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

- qualification standards for directors;

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

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

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

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

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

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

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

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

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

The Nasdaq listing rules also require an audit committee to have a charter addressing all of its duties and responsibilities under the Sarbanes-Oxley Act, including: having the sole power to hire, determine funding for and oversee the outside auditors; having the authority to consult with and determine funding for independent counsel and other advisers; and having the responsibility to establish procedures for receipt of complaints.

In addition, both the NYSE and Nasdaq rules require that companies adopt and disclose a code of conduct applicable to directors, officers and employees that addresses conflicts of interest and legal compliance. The NYSE rules also require that the code address corporate opportunities, confidentiality, fair dealing and protection of company assets.

Public companies post their corporate governance guidelines, board committee charters, codes of conduct and other governance documents on their corporate websites, typically under a heading such as 'Corporate Governance' or 'Investor Relations'.

28 Remuneration of directors

How is remuneration of directors determined? Is there any law, regulation, listing requirement or practice that affects the remuneration of directors, the length of directors' service contracts, loans to directors or other transactions or compensatory arrangements between the company and any director?

The remuneration of directors is generally a matter for the board of directors, or a committee of the board (usually, the compensation committee or the nominating or governance committee), to determine.

In determining the appropriate amount of compensation to be paid to directors, many boards and compensation or nominating or governance committees rely on the advice of independent compensation consultants, whose expertise lies in analysing compensation trends in industry or other market segments. As discussed in question 36, the SEC recently amended its regulations to require enhanced disclosure with respect to a company's use of compensation consultants.

Boards should exercise caution when approving equity compensation plans that permit equity awards to be made to non-employee directors. Such plans should include meaningful limits on the amount of equity that directors can award themselves, to ensure that awards made under the plan are entitled to business judgement rule protection (*Seinfeld v Slager* (Del Ch 2012), *Calma v Templeton* (Del Ch 2015), *In Re Investors Bancorp, Inc* (Del Ch 2017)).

Compensation given to all directors must be disclosed by reporting companies. Under the Sarbanes-Oxley Act, audit committee members can only receive director's fees (including fees for committee work) from the companies they serve. In addition, as discussed in questions 22 and 25, the board must consider the source of compensation of a director when considering his or her suitability for compensation committee service. As discussed in question 27, the NYSE requires listed companies to adopt and disclose corporate governance guidelines, which are required to address, among other things, the compensation of directors. Since 2016, Nasdaq listed companies have been required to disclose compensatory arrangements between directors or nominees and third parties in connection with that person's candidacy or service as a director ('golden leashes').

There is no law, regulation or listing requirement that affects the length of directors' service contracts. Rather, directors are elected for a term by the shareholders and it is up to each company to determine whether to place any limits on the number or length of such terms, although NYSE listing rules provide that directors' terms of office should not exceed three years.

Term limits are very rare among large public companies but retirement age policies are common. The average tenure of directors at S&P 500 companies is 8.3 years. Eighteen per cent of S&P 500 boards have an average director tenure of five years or less, 63 per cent have an average director tenure between six and ten years, and 19 per cent have an average tenure of eleven or more years. Institutional Shareholder Services recently announced updates to its corporate governance assessment tool that tracks the proportion of non-executive directors who have served for less than six years, which suggests that ISS considers a term of longer than six years to be lengthy. While most institutional investors do not support individual term and age limits applicable to directors, some are adopting policies focused on average director tenure or individual director tenure (eg, by generally considering long-tenured directors to not be independent).

Section 402 of the Sarbanes-Oxley Act prohibits companies from extending or maintaining personal loans to their directors, other than certain consumer credit arrangements (such as home improvement or credit card loans) made in the ordinary course of business of a type generally made available by the company to the public and on market terms or terms no more favourable than offered by the company to the general public.

The duty of loyalty restricts directors from competing with the corporation. Thus, while directors are not precluded from engaging in other businesses, they may not:

- use their position as directors to prevent the corporation from competing with their other businesses;
- divert corporate assets to their own uses or the uses of their other businesses;
- disclose the corporation's trade secrets or confidential information to others;
- lure corporate opportunities, business or personnel away from the corporation; or
- receive, unbeknown to the corporation, a commission on a corporate transaction.

Under the corporate opportunity doctrine, directors cannot divert to themselves an opportunity that belongs to the corporation. An opportunity belongs to the corporation if the corporation has a right to it, a property interest in it, an expectancy interest in it or if by 'justice' it should belong to the corporation. The corporation may renounce any interest or expectancy in an opportunity in its certificate of incorporation or by action of its board of directors (see DGCL, section 122(17)). At times, a director's interest may still conflict with the interests of the corporation. Conflicts that cannot be avoided must be fully disclosed by the interested director and any action that needs to be taken should be taken by vote of the disinterested directors.

29 Remuneration of senior management

How is the remuneration of the most senior management determined? Is there any law, regulation, listing requirement or practice that affects the remuneration of senior managers, loans to senior managers or other transactions or compensatory arrangements between the company and senior managers?

The remuneration of a corporation's CEO and senior management is generally a matter for the board of directors, or a committee of the board (usually, the compensation committee), to determine.

NYSE listing rules require that a compensation committee comprising independent directors determine the amount of compensation paid to the CEO, and make recommendations to the board with respect to non-CEO executive officer compensation. These provisions are interpreted broadly, such that a compensation committee or group of independent directors, as the case may be, must approve each specific element of CEO compensation at all listed companies. Since 2014, Nasdaq listing rules have required that CEO and executive officer compensation be determined by a compensation committee comprising at least two independent directors.

In addition, applicable tax and securities rules require the approval of independent directors to grant equity-based awards (such as, stock option and restricted stock awards) to senior management and best practice would have the board or compensation committee approve the compensation paid to key members of senior management. Under Internal Revenue Code section 162(m), the tax code provides tax incentives for certain performance-based compensation decisions when made by a committee of outside directors. As a result, the responsibility between the board (or compensation committee) and the CEO in determining the elements and amount of compensation paid to senior managers (other than the CEO) differs from company to company and, even within a company, from element of compensation to element of compensation.

In determining the appropriate amount of compensation to be paid to the CEO and other senior managers, many boards and compensation committees rely on the advice of independent compensation consultants, whose expertise lies in analysing compensation trends in industry or other market segments. As discussed in question 36, the SEC recently amended its regulations to require enhanced disclosure with respect to a company's use of compensation consultants.

Section 402 of the Sarbanes-Oxley Act prohibits companies from extending or maintaining personal loans to their executive officers, other than certain consumer credit arrangements (such as home improvement or credit card loans) made in the ordinary course of business of a type generally made available by the company to the public and on market terms or terms no more favourable than offered by the company to the general public.

30 D&O liability insurance

Is directors' and officers' liability insurance permitted or common practice? Can the company pay the premiums?

Companies may purchase and typically do maintain directors' and officers' liability insurance to protect directors and officers against the risk of personal liability (see DGCL, section 145(g)). Although such coverage has become substantially more expensive, it is usually available and has not been limited by legislative and regulatory actions. Companies are allowed to pay the premiums for directors' and officers' liability insurance.

31 Indemnification of directors and officers

Are there any constraints on the company indemnifying directors and officers in respect of liabilities incurred in their professional capacity? If not, are such indemnities common?

A company may indemnify a director for liability incurred if that director: acted in good faith; acted in a manner that he or she reasonably believed was in the best interests of the company; and in the case of a criminal proceeding, had no reasonable cause to believe his or her conduct was unlawful (see DGCL, section 145). Many companies employ such indemnities (see also the discussion of the duty of good faith in question 19).

32 Exculpation of directors and officers

To what extent may companies or shareholders preclude or limit the liability of directors and officers?

The Delaware Director Protection Statute allows the shareholders of a corporation to provide additional protection to corporate directors through the adoption of a provision in the certificate of incorporation 'eliminating or limiting the personal liability of a director to the corporation or its stockholders for monetary damages for breach of a fiduciary duty as a director' (DGCL, section 102(b)(7)). Such a provision, however, may not shield directors from liability for: breaches of the duty of loyalty; 'acts or omissions not in good faith or which involve intentional misconduct or a knowing violation of law'; unlawful payments of dividends or unlawful stock purchases or redemptions; or 'any transaction from which the director derived an improper personal benefit' (see also the discussion of fiduciary duties in question 19).

33 Employees

What role do employees play in corporate governance?

Employees play no formal role in corporate governance at public companies in the US. However, it is not uncommon for employees to own shares of the corporation's stock directly or through employee stock option or retirement plans. Stock ownership enables employees to participate in corporate governance as shareholders.

34 Board and director evaluations

Is there any law, regulation, listing requirement or practice that requires evaluation of the board, its committees or directors? How regularly are such evaluations conducted and by whom? What do companies disclose in relation to such evaluations?

Under the NYSE listing rules, listed companies are required to adopt and disclose 'corporate governance guidelines' that address, among other things, an annual performance evaluation of the board. According to the rules, the 'board should conduct a self-evaluation at least annually to determine whether it and its committees are functioning effectively'. The NYSE listing rules also require that each of the audit, compensation and nominating and governance committee charters provide for an annual performance evaluation of the committee. Companies listed on Nasdaq do not have similar requirements, but many still engage in self-evaluation as a matter of good governance practice. In addition, independent auditors often inquire into the board's evaluation of the audit committee as part of the auditor's assessment of the internal control environment.

There has been a greater focus on director evaluations in recent years as investors are increasingly concerned about board quality and refreshment mechanisms in light of long director tenures, rising mandatory retirement age limits and perfunctory director renomination decisions. A robust performance evaluation of individual directors can help inform the renomination decision process.

In 2016, 99 per cent of boards at S&P 500 companies reported conducting an annual performance evaluation. Fifty-four per cent of S&P 500 boards evaluate the full board and committees and 32 per cent evaluate the full board, committees and individual directors annually. The practice of individual director evaluations is on the rise, nearly doubling in the past five years among S&P 500 companies.

The NYSE listing rules include 'overseeing the evaluation of the board and management' as a responsibility of the nominating or governance committee that must be included in its committee charter. Boards should determine the evaluation methodology, for example, the use of a written survey or interviews, or both, followed by a facilitated discussion, and will determine who will lead the evaluation process (eg, the Chair, lead director or a third-party facilitator). A composite report of the feedback and any related recommendations are typically distributed to the board, committee or individual directors by the party leading the evaluation and discussed at a meeting.

In 2014, the CII issued a report calling for enhanced disclosure relating to board evaluation. Specifically, the CII provided 'best in class' examples of disclosure that explain the mechanisms of the evaluation process and discuss the key takeaways from the most recent evaluation. The CII acknowledged that the latter type of disclosure is uncommon among US public companies but is more prevalent in Europe and Australia. US public companies can expect more pressure to disclose their self-evaluation processes, especially in circumstances where shareholders have concerns about governance failures, the absence of regular director turnover or board composition generally.

Disclosure and transparency

35 Corporate charter and by-laws

Are the corporate charter and by-laws of companies publicly available? If so, where?

Corporate certificates of incorporation are publicly available for a small fee from the office of the secretary of state in the state of incorporation. By-laws of private companies are generally not publicly available because they are not required to be filed with the secretary of state. If the corporation is a reporting company, its certificate of incorporation and by-laws are also available as exhibits to various forms filed with the SEC, which can be accessed over the internet free of charge from EDGAR, the SEC database, which is accessible via the SEC's website (www.sec.gov).

36 Company information

What information must companies publicly disclose? How often must disclosure be made?

Federal securities laws and SEC rules require reporting companies (or companies making public offerings) to disclose a wide variety of information in annual and quarterly reports, as well as in proxy statements and public offering prospectuses. In general, a company must disclose all information that would be material to investors. This includes:

- a business description;
- a description of material legal proceedings;
- detailed disclosure of the risks associated with the business and market risk;
- related person transaction disclosure;
- the number of shareholders of each class of common equity;
- management's discussion and analysis of the company's financial condition and results of operations (MD&A);
- a statement as to whether the company has had any disagreements with its accountants;
- disclosure regarding the effectiveness of disclosure controls and procedures, and changes in internal control over financial reporting;
- financial information;
- executive and director compensation; and
- a signed opinion of the company's auditors with respect to the accuracy of the financial information.

Corporations are expected to keep all of this public information current by filing 'current' reports whenever certain specified events occur, as well as issuing press releases and providing website disclosure.

Since the passage of the Sarbanes-Oxley Act and its accompanying SEC implementing rules, reporting companies are also required to disclose all material off-balance-sheet transactions, arrangements, obligations (including contingent obligations) and certain other relationships of the company with unconsolidated entities or other persons. In addition, the Sarbanes-Oxley Act requires that a reporting company's financial reports reflect 'all material correcting adjustments' identified by outside auditors.

Section 404 of the Sarbanes-Oxley Act requires that a reporting company's annual report include an internal control report from management containing a statement of the responsibility of management for establishing and maintaining an adequate internal control structure and procedures for financial reporting and an assessment at the end of the company's most recent fiscal year of the effectiveness of the company's internal control structure and procedures for financial reporting. The company's registered public accounting firm must also attest to, and report on, the effectiveness of the company's internal control over financial reporting.

Reporting companies are also required to disclose the 'total compensation' received by the corporation's CEO, its CFO, and its three most highly compensated executive officers other than the CEO and CFO (together, the named executive officers) and directors. The information is required to be presented in the form of a summary compensation table listing the name of the employee, the year, salary, bonus, other annual compensation, stock and option awards, changes in pension value and non-qualified deferred compensation earnings, all other forms of compensation and total compensation, as well as several other tables relating to grants of plan-based awards, outstanding equity awards, option exercises and vested stock, pension benefits, non-qualified deferred compensation and director compensation. In addition, reporting companies are required to include a 'compensation discussion and analysis' section in their disclosure documents that explains all material elements of the company's compensation of the named executive officers, and includes a description of the company's compensation philosophy and objectives.

The JOBS Act affords 'emerging growth companies' (companies that conducted an IPO after 8 December 2011 and have total annual revenues of less than US$1 billion) the flexibility to provide reduced disclosures relating to financials, MD&A and compensation for a maximum period of five years.

SEC regulations also require the disclosure of certain information concerning any beneficial owner known to the company to possess more than 5 per cent of any class of the corporation's voting securities, including the amount of ownership and percentage and title of the class of stock owned. Note that any person acquiring more than 5 per cent of the equity of a reporting company also must publicly disclose its intentions with respect to such acquisition. In addition, the Exchange Act requires that officers, directors and beneficial owners of 10 per cent or more of a company's equity securities file a statement of ownership each time there has been a change in that person's beneficial ownership of the company's securities.

In addition, special attention is given to corporate governance. Reporting companies must include a copy of the audit committee report in their annual proxy statements. This report must disclose, inter alia, whether the committee has reviewed the audited financial statements with management, recommended that the audited statements be included in the corporation's annual report to the board, and discussed certain matters with independent auditors to assess their views on the auditors' independence, the quality of the corporation's financial reporting and the name of the committee member with financial expertise (if any). Under section 406 of the Sarbanes-Oxley Act, companies are required to disclose whether they have adopted a code of ethics for their senior financial officers. If a company has not adopted such a code it must explain why it has not done so. Certain changes to or waivers of any provision of the code must also be disclosed.

Under the Sarbanes-Oxley Act, the reliability and accuracy of the financial and non-financial information disclosed in a company's periodic reports has to be certified by the company's CEO and CFO. In each quarterly report both officers must certify, among other things, that:
- they reviewed the report;
- to their knowledge the report does not contain a material misstatement or omission and that the financial statements and other financial information in the report fairly present, in all material respects, the financial condition of the company, its results of operations and cash flows for the periods covered in the report;
- they are primarily responsible for the company's controls and procedures governing the preparation of all SEC filings and submissions, not just the periodic reports subject to certification; and
- they evaluated the 'effectiveness' of these controls and procedures and reported to the audit committee any significant deficiencies or material weaknesses in the company's financial reporting controls, together with any corrective actions taken or to be taken. Their conclusions must be disclosed in the certified report.

NYSE-listed companies are required to disclose their corporate governance guidelines. Committee charters (if any) must be disclosed as described in detail in question 27.

In 2003, the SEC adopted rules that require reporting companies to disclose in their proxy statements or annual reports certain information regarding the director nomination process, including:
- whether the company has a nominating committee and, if not, how director nominees are chosen;
- whether the members of the nominating committee are independent;
- the process by which director nominees are identified and evaluated;
- whether third parties are retained to assist in the identification and evaluation of director nominees;
- minimum qualifications and standards used in identifying potential nominees;
- whether nominees suggested by shareholders are considered; and
- whether nominees suggested by large, long-term shareholders have been rejected.

These rules also require reporting companies to disclose certain information regarding shareholder communications with directors, including:
- the process by which shareholders can communicate with directors (and, if the company does not have an established process, why it does not);
- whether communications are screened and, if so, how;
- any policies regarding the attendance of directors at AGMs; and
- the number of directors that attended the preceding year's AGM.

In 2006, the SEC adopted rules that require reporting companies to disclose in their proxy statements or annual reports certain information regarding the corporate governance structure that is in place for considering and determining executive and director compensation, including:
- the scope of authority of the compensation committee;
- the extent to which the compensation committee may delegate any authority to other persons, specifying what authority may be so delegated and to whom;
- any role of executive officers in determining or recommending the amount or form of executive and director compensation; and
- any role of compensation consultants in determining or recommending the amount or form of executive and director compensation, identifying such consultants, stating whether such consultants are engaged directly by the compensation committee or any other person, describing the nature and scope of their assignment and the material elements of the instructions or directions given to the consultants with respect to the performance of their duties under the engagement.

Moreover, in late 2009, the SEC adopted rules requiring companies to provide the following enhanced proxy statement disclosures:
- for each director and nominee, the particular experience, qualifications, attributes or skills that led the board to conclude that the person should serve as a director of the company;
- other directorships held by each director or nominee at any public company during the previous five years (rather than only current directorships);
- expanded legal proceedings disclosure relating to the past ten years (rather than five years);
- whether and, if so, how the nominating committee considers diversity in identifying nominees for director; if the nominating committee has a policy with regard to the consideration of diversity in identifying director nominees, how this policy is implemented and how the nominating committee or the board assesses the effectiveness of its policy;
- the board's leadership structure and why the company believes it is the best structure for the company; whether and why the board has chosen to combine or separate the CEO and board chairman positions; where these positions are combined, whether and why the company has a lead independent director and the specific role the lead independent director plays in the leadership of the company;
- the board's role in the oversight of risk management and the effect, if any, that this has on the company's leadership structure;
- the company's overall compensation policies or practices for all employees generally, not just executive officers, 'if the compensation policies and practices create risks that are reasonably likely to have a material adverse effect on the company'; and
- fees paid to and services provided by compensation consultants and their affiliates if the consultants provide consulting services related to director or executive compensation and also provide other services to the company in an amount valued in excess of US$120,000 during the company's last fiscal year.

In early 2010, the SEC also issued an interpretive release on disclosure relating to climate change, which is intended to provide guidance to reporting companies on the application of existing disclosure requirements to climate change and other matters. In addition, in September 2010, the SEC issued an interpretive release relating to disclosure of liquidity and funding risks posed by short-term borrowing practices.

The SEC issued disclosure guidance relating to cyber-security (October 2011) and European sovereign debt exposure (January 2012), among other matters.

In 2011, the SEC approved final rules relating to advisory votes on executive compensation (say-on-pay) pursuant to the Dodd-Frank Act, which also require companies to include a discussion in the proxy statement as to whether and, if so, how the company has considered the results of the most recent say-on-pay vote in determining compensation policies and decisions and, if so, how that consideration has affected the company's executive compensation decisions and policies.

In 2012, the SEC approved final rules mandated by the Dodd-Frank Act requiring proxy statement disclosure regarding compensation consultant conflicts of interest. Such disclosure became required to be included in proxy statements for annual meetings occurring on or after 1 January 2013.

In August 2012, the Exchange Act was amended by the Iran Threat Reduction and Syria Human Rights Act of 2012 to require public companies to provide disclosure if the company or any of its affiliates (including its directors and officers) has knowingly engaged in certain enumerated activities subject to US trade sanctions involving Iran or specified Iranian entities or nationals as well as certain other non-Iranian persons or entities deemed to promote terrorist activities or the proliferation of weapons of mass destruction. Such disclosure became required to be included in quarterly and annual reports beginning in February 2013.

The Dodd-Frank Act amended the Exchange Act to require disclosure relating to 'conflict minerals' (gold, tantalum, tin and tungsten) originating from the Democratic Republic of Congo or an adjoining country. Beginning in May 2014, public companies were required to make various disclosures where conflict minerals are necessary to the functionality or production of a product that is either manufactured by the company or by a third party with which the company contracts for such manufacture. A group of business groups filed litigation challenging the conflict minerals rule on several grounds, including that the required disclosure would violate the First Amendment to the US Constitution. In April 2014, the US Court of Appeals for the District of Columbia Circuit found that one disclosure provision of the conflict minerals rule violated the First Amendment but upheld the remainder of the rule. The Court reaffirmed its original ruling in August 2015 and final judgment in the case was entered in April 2017. In January 2017, the acting chair of the SEC had requested comments on the rule and related guidance through March 2017. In April 2017, the Staff of the SEC's Division of Corporation Finance announced that it will not recommend enforcement action if a company fails to comply with certain aspects of the rule relating to due diligence on the source and chain of custody of conflict minerals and an independent private sector audit. The acting chair of the SEC released a statement on the same day announcing that this relief is appropriate because the primary purpose of those requirements is to enable companies to make the disclosure that was found to violate the First Amendment. He directed the SEC Staff to develop a recommendation for future SEC action on the rule after taking into consideration the public comments received.

In addition, the Dodd-Frank Act amended the Exchange Act to require 'resource extraction issuers' to disclose specified information regarding payments made to a foreign government or the US federal government for the purpose of commercial development of oil, natural gas or minerals. The SEC adopted a resource extraction disclosure rule in August 2012 that was vacated by the US District Court for the District of Columbia in July 2013. In September 2013, the SEC announced that it would redraft the resource extraction rule rather than appeal the ruling. The SEC reproposed the resource extraction rule in December 2015. The SEC rule was repealed in February 2017, but the underlying Dodd-Frank Act mandate for SEC rule-making remains intact.

The Dodd-Frank Act requires several new disclosures requiring SEC rule-making, including in relation to 'pay versus performance', 'internal pay equity' (requiring disclosure of the median of the annual total compensation of all company employees except the CEO, the CEO's total annual compensation and the ratio of the former to the latter), 'clawback' policies requiring the recovery of excess compensation paid to executives and corporate policies on hedging of company stock by directors and employees. The SEC has adopted rules relating to the 'internal pay equity' disclosure requirements and has proposed rules relating to the 'pay versus performance' disclosure requirements, 'clawback' policies and corporate hedging policies. In February 2017, the acting chair of the SEC released a statement soliciting comment from US public companies subject to the 'internal pay equity' rule as to any unexpected compliance difficulties they have experienced and announcing that he directed the SEC staff to reconsider the implementation of the rule and to determine whether additional guidance or relief may be appropriate.

In April 2016, the SEC issued a concept release seeking public comment on modernising certain business and financial disclosures required to be included in US public companies' periodic reports. In August 2016, the SEC requested public comment through October 2016 on the compensation and corporate governance information to be included in US public companies' proxy statements. These actions are part of the SEC's 'disclosure effectiveness project' discussed in 'Update and trends'.

Hot topics

37 Say-on-pay

Do shareholders have an advisory or other vote regarding executive remuneration? How frequently may they vote?

Commencing in 2011, the Dodd-Frank Act requires US public companies to conduct a separate shareholder advisory vote on:

- executive compensation – to be held at least once every three calendar years;
- whether the advisory vote on executive compensation should be held every year, every two years or every three years – to be held at least once every six calendar years; and
- certain 'golden parachute' compensation arrangements in connection with a merger or acquisition transaction that is being presented to shareholders for approval.

The predominant practice is to hold a shareholder advisory vote on executive compensation every year.

See question 29 for further details about the remuneration of executives.

38 Shareholder-nominated directors

Do shareholders have the ability to nominate directors and have them included in shareholder meeting materials that are prepared and distributed at the company's expense?

Since September 2011, companies can no longer exclude from their proxy materials shareholder proposals (precatory or binding) relating to by-law amendments establishing procedures for shareholder nomination of director candidates and inclusion in the company's proxy materials, as long as the proposal is not otherwise excludable under Rule 14a-8. This amendment to Rule 14a-8 facilitates the development of 'proxy access' via private ordering at companies chartered in states where permissible, as shareholders are able to institute a shareholder nomination regime via binding by-law amendment or request, via precatory shareholder proposal, that such a by-law be adopted by the board.

The private ordering process gained considerable momentum during 2015, which saw a significant increase in the number of shareholder proxy access proposals submitted (over 100) and shareholder support for such proposals (60 per cent of the total proposals voted on passed), as well as an increased frequency of negotiation and adoption of proxy access via board action – including an accelerating trend towards board adoption without receipt of a shareholder proposal. These trends continued into 2016 and the first half of 2017. Nearly 60 per cent of S&P 500 companies have adopted proxy access as of spring 2017. The market standard that has emerged gives a group of up to 20 shareholders who hold 3 per cent of the company's common stock for at least three years the right to nominate up to 20 per cent of the company's directors (or at least two directors) using the company's proxy materials. Proxy access provisions typically include limitations on the use of proxy access (eg, in contested election situations) and require detailed information to be provided in relation to the nominee and the nominating group, among other requirements.

Furthermore, the SEC proposed changes to the federal proxy rules in October 2016 to require the use of universal proxy cards, which would allow shareholders to vote for a mix of management and dissident nominees in a contested director election.

39 Shareholder engagement

Do companies engage with shareholders? If so, who typically participates in the company's engagement efforts and when does engagement typically occur?

Shareholder influence is more potent than ever and continued attention to the quality of shareholder relations has become paramount. Companies are engaging with their key large institutional investors more directly and more frequently to hear their interests and concerns, including from a governance perspective. Whereas engagement with shareholders used to occur primarily during the annual meeting season, companies are now engaging with their shareholders throughout the year. There are several reasons for this including:

Update and trends

In July 2016, a coalition of 13 executives from large public companies and institutional investors in the US issued a set of corporate governance principles named the 'Commonsense Principles of Corporate Governance' that were designed to 'provide a basic framework for sound, long-term oriented governance' at US public companies and encourage further discussion on the topic. The principles are high-level and reflect widely accepted corporate governance best practices. The coalition acknowledges that the principles would have to be tailored based on a company's size, business and leadership structure.

Since 2016, Nasdaq listed companies have been required to disclose compensatory arrangements between directors or nominees and third parties in connection with that person's candidacy or service as a director ('golden leashes').

The SEC is continuing to work to implement the remaining mandates of the Dodd-Frank Act in the area of corporate governance. These include the adoption of rules regarding disclosure of 'pay versus performance', corporate policies on hedging of company stock by employees and directors and policies requiring the recovery of executive compensation. The SEC has not announced any timeline by which it expects to adopt these rules in final form and their adoption date is tenuous as the change in presidential administration in the US has hindered SEC rule-making. In 2015, the SEC adopted final rules requiring disclosure of 'internal pay equity' (see question 36). In February 2017, the acting chair of the SEC released a statement soliciting comment from US public companies subject to the 'internal pay equity' rule as to any unexpected compliance difficulties they have experienced and announcing that he directed the SEC staff to reconsider the implementation of the rule and to determine whether additional guidance or relief may be appropriate.

Since early 2014, the SEC has engaged in a 'disclosure effectiveness project'. The goal of the project is to review existing disclosure requirements to determine whether modifications should be made to reduce the costs and burdens on public companies while also promoting the disclosure of material information to investors and eliminating duplicative disclosures. In September 2015, the SEC requested comment on the form and content of financial statement disclosures required under Regulation S-X. In April 2016, the SEC issued a concept release seeking public comment on modernising certain business and financial disclosures required by Regulation S-K to be included in public companies' periodic reports. In August 2016, the SEC requested public comment through October 2016 on the compensation and corporate governance information to be included in US public companies' proxy statements. In August 2016, the SEC proposed rules intended to update and simplify certain disclosure requirements by eliminating redundant, overlapping, outdated and superseded requirements due to changes in disclosure rules, accounting principles and technology. In March 2017, the SEC approved rules that will require US public companies to provide hyperlinks to the exhibits to their SEC filings, which will become effective for the largest category of filers in September 2017.

The SEC is under increasing pressure to require new or enhanced disclosure relating to various topics including climate change, board diversity, cyber-expertise on the board and political contributions. Calls for such disclosure have come from a variety of sources, including members of Congress.

The boards of directors of US public companies are under ever-growing pressure as shareholder efforts to intervene in and influence corporate decisions increase. The elimination of takeover defences in the name of 'good governance' has shifted power to shareholders and made boards and companies more vulnerable to intervention. The emergence of and reliance on proxy advisory firms and greater shareholder voting rights have also played a role in increasing the power and coordination of shareholders.

In recent years the focus of shareholder proposals has shifted from highly successful campaigns to remove antitakeover protections (ie, classified boards, plurality voting in uncontested director elections) to proxy access and other efforts to influence board composition. Proxy access has gained considerable momentum since the beginning of 2015 through private ordering, as discussed in question 38. More than 100 shareholder proposals requesting proxy access were submitted for the 2015 proxy season and 60 per cent of such proposals voted on in 2015 passed. More than 200 shareholder proxy access proposals were submitted for the 2016 proxy season and 52 per cent of such proposals voted on in 2016 passed. In response to such proposals and increasing pressure from institutional investors and proxy advisory firms, over 425 companies have adopted proxy access, including nearly 60 per cent of S&P 500 companies. In the past year, shareholder proponents have shifted from submitting proposals asking companies to adopt proxy access to proposals asking companies to amend certain provisions of their existing proxy access by-laws. Most commonly, they seek to increase or eliminate the limit on the number of shareholders that may aggregate to form a nominating group. These proposals have either largely been excludable if the SEC has agreed that the company has substantially implemented the proposal or failed to receive majority support.

Institutional Shareholder Services and Glass Lewis recently revised their policies whereby, beginning for the 2017 proxy season, they will recommend votes against a non-executive director who sits on more than five (down from six) public company boards. Glass Lewis also revised its policy so that it will generally recommend against a public company executive officer who sits on more than two (down from three) public company boards.

In October 2016, the SEC proposed amendments to the federal proxy rules that would require participants in a proxy contest to use universal proxy cards that include the names of all duly nominated director candidates. Universal proxy cards would allow shareholders voting by proxy to vote for their preferred combination of registrant and dissident nominees in a contested election of directors. Under the current proxy rules, shareholders who wish to vote a split ticket must generally attend the shareholder meeting and vote in person. The purpose of the proposed rules is to afford shareholders who vote by proxy the same voting choices available to shareholders who vote in person. The proposed rules set forth certain notice, filing, minimum solicitation and formatting requirements that would apply to universal proxy cards.

The SEC is under increasing pressure to reform the shareholder proposal process. Business Roundtable, an association representing CEOs of US companies, published a report in October 2016 urging the SEC to make various reforms such as making the eligibility requirements applicable to shareholder proponents more onerous and enabling more proposals to be excluded, particularly repeat proposals that have garnered very low support in prior years.

Shareholders are increasingly seeking to engage with companies outside of the shareholder proposal mechanism. For example, in addition to more frequent one-on-one meetings between the company and shareholders, it is becoming more common for large institutional investors to send letters on specific issues of concern to portfolio companies. In recent years, public campaigns of this sort have urged CEOs to disclose a long-term strategic plan to shareholders, the adoption of proxy access and more direct engagement between directors and shareholders. BlackRock's 2017 annual letter to CEOs advocated for governance practices that maximise long-term value creation and encouraged companies to adapt their strategies in light of globalisation, technological changes and ESG issues such as sustainability. State Street's annual 2017 letter announced that it plans to focus on board oversight of environmental and social sustainability issues and their relationship to long-term strategies.

In January 2017, the Investor Stewardship Group, a collection of large US-based institutional investors and global asset managers representing US$17 trillion in assets under management, launched the Framework for US Stewardship and Governance including standards focused on corporate governance principles for US public companies and investment stewardship principles for institutional investors. Key themes of the standards include the promotion of long-term value creation and investor protection.

In March 2017, State Street Global Advisors published guidance in connection with a new initiative to promote greater gender diversity on corporate boards. State Street indicated that it will initially target companies that do not have any female directors and, beginning in 2018, it may vote against the chair of the nominating or governance committee of a company that fails to take action to increase the number of women on the board.

In April 2017, the New York City Pension Funds announced a campaign to vote against governance committee members at companies that hold exclusively virtual annual shareholder meetings.

- the advent of the shareholder advisory vote on executive compensation;
- a rise in hedge fund activism;
- proxy advisory firm policies that expect companies to respond to shareholder advisory votes that receive significant (but less than passing) support; and
- shareholder expectations.

Shareholders are also increasingly seeking to engage with companies outside of the shareholder proposal mechanism. For example, in addition to more frequent one-on-one meetings between the company and shareholders, it is becoming more common for large institutional investors to send letters on specific issues of concern to portfolio companies. In recent years, public campaigns of this sort have urged CEOs to disclose a long-term strategic plan to shareholders, the adoption of proxy access and more direct engagement between directors and shareholders. In particular, Vanguard Group and BlackRock Inc, two of the US' largest institutional investors, have recently become more assertive in pushing for corporate governance reforms and increased director-shareholder engagement at the companies in which they invest.

Members of senior management (eg, CEO and CFO) are typically the company representatives who engage with shareholders. Investor relations personnel may also be involved in shareholder engagement efforts. Outside counsel rarely participates. Directors are becoming more involved in shareholder engagement. Which director is involved depends on the topics to be discussed. Often the lead director or the relevant committee chair will meet with the shareholder along with a member of senior management. For example, the compensation committee chair may be called upon to meet with an investor who has concerns with the company's executive compensation programme.

Directors of US public companies should understand the composition and particular interests of their shareholder base and be actively involved in overseeing the company's shareholder engagement and investor relations efforts. Many companies are also engaging with a broader group of shareholders rather than just the top few holders. Companies are also increasingly providing disclosure regarding their shareholder engagement efforts in their annual meeting proxy statements. In 2015, the CII issued a report calling for enhanced disclosure relating to company-shareholder engagement. Specifically, the CII provided 'best in class' examples of disclosure of engagement policies and practices.

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Sources of corporate governance rules and practices

1 Primary sources of law, regulation and practice

What are the primary sources of law, regulation and practice relating to corporate governance? Is it mandatory for listed companies to comply with listing rules or do they apply on a 'comply or explain' basis?

The Law on Enterprises (LOE), which took effect from 1 July 2015, is the primary source of corporate laws that encompass the establishment, governance and operation of companies in Vietnam. For public companies, which are those made public by the offer of shares, or having shares listed on the stock exchange or a securities trading centre, or having shares owned by at least 100 investors excluding professional securities investors and having paid-up charter capital of 10 billion dong or more, the Law on Securities (LOS) and the legal guiding documents thereof including Circular 121/2012/TT-BTC provide further regulations on corporate governance as part of their public status. Additionally, for companies that are joint ventures between foreign investors and Vietnamese partners engaging in the services as committed to by Vietnam under the commitments on specific services in accession to the World Trade Organization (joint venture companies), Resolution No. 71/2006/NQ-QH11 still appears to function as another source of law relating to corporate governance of joint venture companies despite the fact that certain laws under this Resolution are amended, replaced or due to be replaced (eg, law on enterprises, law on promulgating legal normative).

As a matter of principle, listed companies shall comply with both listing rules and the relevant laws for matters that are not specifically regulated by listing rules. As such, it is mandatory for listed companies to comply with listing rules.

2 Responsible entities

What are the primary government agencies or other entities responsible for making such rules and enforcing them? Are there any well-known shareholder groups or proxy advisory firms whose views are often considered?

The Ministry of Planning and Investment mainly drafts bills for laws and governmental decrees on corporate regulations and issues its own guidance and clarification whenever necessary. Likewise, the State Securities Commission of Vietnam and its direct parent agency, which is the Ministry of Finance, are in charge of the sector of public companies, whether unlisted or listed. Enforcement of the laws and regulations is carried out by various competent authorities, including the Ministry of Planning and Investment, the local people's committees, the local authorities for planning and investment, or the State Securities Commission itself for the securities sector.

There are no well-known shareholder activist groups or proxy advisory firms in Vietnam that would have a material influence on companies' policies or corporate governance-related issues.

The rights and equitable treatment of shareholders

3 Shareholder powers

What powers do shareholders have to appoint or remove directors or require the board to pursue a particular course of action? What shareholder vote is required to elect or remove directors?

A shareholder or a group of shareholders in a joint-stock company may nominate candidates for the board if they have held at least 10 per cent of the total ordinary shares for a consecutive period of six months or more (major shareholders) unless a lower percentage is set forth in the company's charter (articles 114.2 and 114.4 of the LOE). Any share with a voting right can be counted in a vote at a shareholders' meeting, including a meeting for the election of directors. Cumulative voting is a compulsory measure for the election of directors; the total number of votes of each shareholder shall be equal to the total number of the shareholder's shares multiplied by the total number of vacant positions (although shares with preferential votes will be entitled to a greater number of votes in accordance with the company's charter) and each shareholder may exercise all of his or her votes in favour of a single candidate or a number of candidates (article 144.3 of the LOE). However, a different mechanism for the election of directors may be applied if so regulated under the company's charter (article 144.3 of the LOE).

Successful candidates will be selected from those with the highest number of votes to those with the lowest number of votes, in descending order, until the total number of vacant positions has been filled, and where there are two or more candidates receiving the same number of votes for the last vacant position, another vote taken on such candidates will be held, or the director shall be selected in accordance with the criteria set forth in the voting rules or the company's charter (article 144.3 of the LOE). The directors are elected at the shareholders' meeting (article 144.3 of the LOE) and may only be removed by a resolution passed by the shareholders' meeting (article 135.2(c) of the LOE). By the default in law, a resolution removing a director shall be passed if it is agreed by shareholders representing at least 51 per cent of the total number of voting slips of all attending shareholders. However, the law permits the charter of the company to provide for a higher specific percentage (articles 144.1 and 144.2 of the LOE).

The shareholders' meeting, comprising shareholders with voting rights, is the highest decision-making body in the company. While the board should follow the resolution of the shareholders' meeting, a shareholder or a group of shareholders cannot, without resolution of the shareholders' meeting, impose obligations upon the board, except for the right to require the board to convene the general meeting of shareholders (see question 7). However, a shareholder or a group of shareholders holding shares of the company for at least one year may require the board to stop the implementation of any decision or resolution that has been passed by the board contrary to the laws or the company's charter, thereby causing loss to the company (article 149.4 of the LOE). Additionally, a shareholder or a group of shareholders holding at least 1 per cent of the total ordinary shares for six consecutive months have the right to directly, or on behalf of the company, make a claim for civil liability against the director, manager or general director under certain circumstances (article 161 of the LOE).

4 Shareholder decisions

What decisions must be reserved to the shareholders? What matters are required to be subject to a non-binding shareholder vote?

The following decisions are subject to the authority of the shareholders' meeting:

- to adopt the development strategy of the company (article 135.2(a) of the LOE);
- to decide on the class and total amount of shares of each class that may be issued by the company; and the amount of dividend per share of each class on an annual basis (article 135.2(b) of the LOE);
- to elect, remove and dismiss directors of the board and members of the supervisory board (article 135.2(c) of the LOE);
- to decide on investment or approve the sale of 35 per cent or more of the total value of assets recorded in the company's latest financial statement, unless a different percentage is provided for in the company's charter (article 135.2(d) of the LOE);
- to approve contracts or transactions, executed between the company and a related party, as defined under the laws, of 35 per cent or more of the total value of assets recorded in the company's latest financial statement unless a different percentage is provided for in the company's charter (article 162.3 of the LOE);
- to decide on amendment of or supplement to the company's charter (article 135.2(dd) of the LOE);
- to approve annual financial statements (article 135.2(e) of the LOE);
- to decide on redemption of more than 10 per cent of issued shares of each class (article 135.2(g) of the LOE);
- to consider and decide on breaches committed by the board of directors or the supervisory board that cause damage to the company and the shareholders (article 135.2(h) of the LOE);
- to decide on the restructuring or dissolution of the company (article 135.2(i) of the LOE); and
- other rights and duties as provided for in the laws and the company's charter (article 135.2(k) of the LOE).

Notwithstanding the foregoing, decisions that are subject to the authority of the shareholders' meeting of a joint venture company (defined in question 1) may be, subject to meeting statutory conditions (see Official Letter No. 771-BKH-TCT of the Ministry of Planning and Investment), regulated differently in the company's charter. Further, additional items that do not fall within the statutory authority of other statutory bodies of the company may be added to the charter to be subject to the resolution of the shareholders' meeting.

5 Disproportionate voting rights

To what extent are disproportionate voting rights or limits on the exercise of voting rights allowed?

In principle, each ordinary share of a joint-stock company is granted only one vote (article 114.1(a) of the LOE). However, the company is permitted to issue shares with preferential votes, which are granted a larger number of votes than that of ordinary shares, provided, however, that only founding shareholders or organisations as authorised by the government may hold shares with preferential votes and, even in such cases, such shares may be held by founding shareholders only for a period of three years after the company is established (articles 113.3 and 116 of the LOE). Additionally, the company may issue shares with preferential dividends or preferential redemption rights that have no voting right (articles 117 and 118 of the LOE). The company may decide to issue other kinds of preferential shares in accordance with the company's charter (article 113.2(d) of the LOE).

6 Shareholders' meetings and voting

Are there any special requirements for shareholders to participate in general meetings of shareholders or to vote? Can shareholders act by written consent without a meeting? Are virtual meetings of shareholders permitted?

In principle, the company shall not restrict its eligible shareholders from attending the shareholders' meeting (article 6.2 of Circular 121/2012/TT-BTC). Based on the company's register of shareholders at the time of having a decision on convening the shareholders' meeting (article 137.1 of the LOE) or based on the cut-off date of the shareholders' list describing the shareholders entitled to attend the shareholders' meeting that is applied to a public company, any shareholder holding ordinary shares or shares with preferential votes may participate in the shareholders' meeting and exercise the voting rights associated with their respective shares, except for those shareholders holding preferential shares without a voting right (as outlined in answers to question 5).

In cases of related-party transactions that require approval of the shareholders' meeting, the shareholders who have interests in such transactions may not vote on the approval (article 162.3 of the LOE). In a similar manner, a founding shareholder may not vote on the approval of his or her transfer of the shares within three years from the issuance date of the enterprise registration certificate of the company (article 119.3 of the LOE).

Besides physical meetings, it is worth noting that the shareholders may adopt resolutions via a process of collecting written opinions (article 145 of the LOE). In such a case, the minimum vote for adopting any resolution shall be 51 per cent of the total voting shares (article 144.4 of the LOE).

Virtual meetings of shareholders are permitted as long as the location of meetings (eg, the location of the chairman if the meeting is carried out in multiple locations at once) is within the territory of Vietnam (article 136.1 of the LOE). Shareholders may attend and vote at meetings conducted via online conference (article 140.2(c) of the LOE).

7 Shareholders and the board

Are shareholders able to require meetings of shareholders to be convened, resolutions and director nominations to be put to a shareholder vote against the wishes of the board, or the board to circulate statements by dissident shareholders?

A shareholders' meeting may be convened by major shareholders (as defined in question 3) if either the board of directors or supervisory board fails to convene the meeting in accordance with the laws or the company's charter (article 136.6 of the LOE). Regardless of who convenes the meeting, the major shareholders can always propose matters to the meeting agenda for discussion unless the procedures or contents of such proposals are contrary to the laws or the company's charter (article 138.2 of the LOE). The meeting convenor is required to include the proposed matters in the draft programme and agenda for the meeting, except for those that fall under cases wherein the convenor may refuse the proposed matter. The draft programme and agenda are sent together with the notice of invitation to all shareholders entitled to attend the meeting (articles 138.4 and 139.3 of the LOE). The proposed matters are added officially to the programme and agenda if the shareholders' meeting so agrees (article 138.4 of the LOE). There is no requirement by the laws for the board of directors to circulate the statements or opinions of the dissident shareholders other than the requirement that the minutes of the vote-counting result and the minutes of the shareholders' meeting, which may contain a summary of the statements of the dissident shareholders, must be forwarded to the shareholders within a certain period of time (articles 145.6 and 146.3 of the LOE).

8 Controlling shareholders' duties

Do controlling shareholders owe duties to the company or to non-controlling shareholders? If so, can an enforcement action be brought against controlling shareholders for breach of these duties?

Controlling shareholders of a public company (shareholders directly or indirectly holding at least 5 per cent of the total shares with voting rights of the company) are required not to exploit their advantages to cause any damage to the rights and other benefits of the company and other shareholders (including non-controlling shareholders) (articles 6.9 and 29 of the LOS; article 4 of Circular 121/2012/TT-BTC).

Transactions, contracts between the company and a shareholder holding more than 10 per cent of the total ordinary shares under the LOE (or their related person) must be approved by the board of directors or the shareholders' meeting, depending on the value of such transactions, which otherwise shall be void and invalid (article 162.1(a) of the LOE).

A corporate shareholder holding more than 50 per cent of the total ordinary shares, or capable of directly or indirectly appointing all or most of the board of directors, or otherwise capable of amending the company's charter shall be considered a 'parent company' (article 189.1 of the LOE) and be subject to the duties of a parent company under the laws, which include bearing liability for damages in cases of non-arm's-length transactions undertaken by the company as a result of the shareholder's intervention (article 190 of the LOE).

Failure to perform the duties that controlling shareholders owe to the company will result in such controlling shareholders being subject to liability for damage incurred and injunctions.

9 Shareholder responsibility

Can shareholders ever be held responsible for the acts or omissions of the company?

If a 'parent company' shareholder (as defined in question 8) intervenes in the operation of the company beyond the normal authority of a shareholder and causes the company to undertake non-arm's-length transactions or otherwise non-profitable transactions without compensation, such a shareholder shall be liable for damage incurred by the company (article 190 of the LOE).

Corporate control

10 Anti-takeover devices

Are anti-takeover devices permitted?

Anti-takeover devices are not expressly governed by Vietnamese laws. As a rule of thumb, it is permissible to apply anti-takeover devices or customisation of the company's charter, provided that no statutory rights of shareholders or the board or otherwise are expressly violated. For example, an anti-takeover device in the form of a preferential share plan is permitted under the laws as part of the right of the company (article 113.2(d) of the LOE), but a super-voting preferential share plan, which is offered to shareholders other than founding shareholders or organisations as authorised by the government or offered to any entity that is not an organisation as authorised by the government after the period of three years from the date on which the company is issued with the enterprise registration certificate, may be held invalid as a breach of the legal provisions on shares with preferential voting power (article 113.3 of the LOE).

11 Issuance of new shares

May the board be permitted to issue new shares without shareholder approval? Do shareholders have pre-emptive rights to acquire newly issued shares?

Issuance of new shares or a new class of shares must be approved by the shareholders' meeting (article 135.2(b) of the LOE), although the board of directors may decide on an offer of new shares within the authorised number of shares for each class as approved by the shareholders' meeting (article 149.2(c) of the LOE). Existing shareholders are granted pre-emptive rights to acquire newly issued shares in proportion to their shareholding ratio at the time of issuance (article 114.1(c) of the LOE). However, it appears from the LOS and the legal guiding documents thereof that the shareholders' meeting of a public company may waive such pre-emptive rights of the shareholders by a valid resolution (article 5.6 of the model charter issued together with Circular 121/2012/TT-BTC), though there is the possibility that the legal validity of such resolution would be challenged in practice by the court.

12 Restrictions on the transfer of fully paid shares

Are restrictions on the transfer of fully paid shares permitted and, if so, what restrictions are commonly adopted?

Except for circumstances as provided for by law, and certain restrictions on the transferability of shares that may be set forth under the company's charter and the validity of which is enforced by way of stipulating the same on the respective share certificates (article 126.1 of the LOE), any shares are freely transferable (article 126.1 of the LOE). On the other hand, the securities laws also allow certain restrictions to be placed on the transfer of shares in a public company's charter or by a resolution of the shareholders' meeting (article 3.1(a) of Circular 121/2012/TT-BTC).

A number of restrictions expressly provided by law include the case in which a founding shareholder transfers its shares to non-founding shareholders of the company, which transfer will be subject to approval of the shareholders' meeting within the period of three years from the date of establishment (article 119.3 of the LOE), or the case in which shareholders hold shares in a public company that were issued through a private placement where such shares are subject to transfer restrictions within the period of at least one year from the date of completion of the private placement (article 10a.2(b) of the amended LOS).

13 Compulsory repurchase rules

Are compulsory share repurchases allowed? Can they be made mandatory in certain circumstances?

In relation to shareholders, acceptance of a share repurchase offer is not compulsory under the laws (article 130.3 of the LOE). The procedures and circumstances of share repurchase are expressly provided for in the laws, so it may be illegal to enforce repurchase of any shares without consent of the relevant shareholders. On the other hand, in relation to a company, share repurchase may become compulsory in certain circumstances. Specifically, the company may have to make a share repurchase at the request of shareholders who object to a decision on the reorganisation of the company or a change in the shareholders' rights and obligations in the charter (article 129.1 of the LOE), as explained in question 14.

Additionally, the company may make a share repurchase in respect of redemption preference shares whenever so requested by the shareholder holding such shares or pursuant to conditions stipulated in the respective share certificates of such shares (article 118 of the LOE).

On a related note, unless exempted by statute, a public company will be required to conduct a tender offer when it repurchases ordinary shares leading to the total amount of treasury shares being equivalent to 25 per cent or more of the total outstanding shares of the same class (article 37.1(dd) of Decree 58/2012/ND-CP); however, the shareholders' acceptance is not compulsory in this case either.

14 Dissenters' rights

Do shareholders have appraisal rights?

Shareholders who object to the restructuring of the company or changes to the company's charter in respect of the shareholders' rights and obligations may request that the company buy back their shares at a fair value or a price regulated under the company's charter (article 129.1 of the LOE). In case the company fails to reach an agreement on such transfer price, the company shall introduce at least three professional appraisal firms to enable the shareholders to select one firm and the price appraised by such selected firm shall be final and binding upon the parties (article 129.2 of the LOE). The current LOE (unlike its previous version) keeps silent on the possibility of the shareholders to transfer such shares to other parties in this case.

The responsibilities of the board (supervisory)

15 Board structure

Is the predominant board structure for listed companies best categorised as one-tier or two-tier?

The board structure for listed companies is categorised as two-tier including the board of directors (which assumes management functions as to the business operation of the company) and the supervisory board (which assumes supervisory functions as to the management and operation of the company by the board of directors and general director (or CEO)). With regard to the structure of the board of directors, it needs to maintain a balance between executive directors and non-executive directors, so that at least one-third of the directors must be non-executive directors (article 11.2 of Circular 121/2012/TT-BTC). Additionally, the board of directors needs to be supplemented with specialist committees (article 32 of Circular 121/2012/TT-BTC). If the company prefers not to establish such committees, independent directors must be assigned such special duties instead (article 32.4 of Circular 121/2012/TT-BTC).

It should be noted that a company may choose not to establish a supervisory board, even where it has 11 shareholders or more, or where the shareholders are organisations holding 50 per cent or more of the total shares; provided, however, that in such case at least 20 per cent of the directors are independent directors and there is an internal auditing board belonging to the board of directors (article 134.1(b) of the LOE). It remains unclear whether a listed company will be permitted to go with such one-tier option.

16 Board's legal responsibilities

What are the board's primary legal responsibilities?

Except for the matters reserved for the shareholders' meeting as mentioned in question 4, the board of directors is primarily in charge of all other matters of the company (article 149.2 of the LOE), although certain day-to-day activities and lower level decisions are within the authority of the general director of the company (article 157 of the LOE). Meanwhile, the supervisory board is primarily in charge of supervising activities of the board of directors as well as the general director in management and operation of the company (article 165.1 of the LOE).

17 Board obligees

Whom does the board represent and to whom does it owe legal duties?

The board of directors acts on behalf of the company to decide and exercise the rights and duties of the company (article 149.1 of the LOE) and owes legal duties to the company and the shareholders (article 14.2 of Circular 121/2012/TT-BTC; article 160.1 of the LOE). The board is required to be loyal to the interests of the company and shareholders; it must, however, show impartial treatment to shareholders (article 14.3 of Circular 121/2012/TT-BTC).

In respect of the supervisory board, it is required to be loyal to the interests of the company and shareholders (article 168.3 of the LOE).

18 Enforcement action against directors

Can an enforcement action against directors be brought by, or on behalf of, those to whom duties are owed?

Eligible shareholders may request suspension of decisions that have been passed by the board of directors contrary to the laws or the company's charter and that cause loss to the company (article 149.4 of the LOE). Such shareholders may directly make such a claim against the director without going through the supervisory board regardless of the fact that the company has a supervisory board under the LOE (article 161 of the LOE). When the case is brought to the court, temporary injunctive relief or enforcement, or both, may be taken by the courts in accordance with the rules of civil procedure. If a director is found by the supervisory board to have breached his or her duties, the supervisory board shall immediately notify such a breach in writing to the board of directors and request that the director cease the act constituting a breach and take proper measures to remedy the consequences (article 165.8 of the LOE). In addition, a shareholder or a group of shareholders holding 10 per cent or more of the total shares for at least six consecutive months, or a lower percentage as provided for in the company's charter, may also convene a shareholders' meeting when a director allegedly prejudices the rights of shareholders, violates its managerial duties or makes a decision exceeding his or her authority (article 114.3(a) of the LOE) to dismiss such director or take other appropriate action within the authority of the shareholders' meeting.

Similarly, where a member of the supervisory board is found by the board of directors to have breached the law, the board of directors shall immediately notify such a breach in writing to the supervisory board and request that the member cease the act constituting a breach as well as take proper measures to remedy the consequences (article 168.6 of the LOE).

19 Care and prudence

Do the board's duties include a care or prudence element?

Yes, both the directors and members of the supervisory board must carry out their assigned duties with honesty, care and the best lawful interests of the company and the shareholders in mind (articles 160.1(b) and 168.2 of the LOE).

20 Board member duties

To what extent do the duties of individual members of the board differ?

All of the directors on the board have the same duties under the laws and the members of the supervisory board are subject to the same duties, except for the chairman of the board and head of the supervisory board, who are subject to further rights and duties. In addition, if the company is a listed company or a large-scale public company, which means a company having shareholder's equity of at least 120 billion dong as reflected in its latest audited annual financial statement (article 2.2 of Circular 155/2015/TT-BTC), certain directors may be assigned specialist duties according to the resolution of the shareholders' meeting (article 32.1 of Circular 121/2012/TT-BTC).

The law requires that the directors must have professional expertise and experience in the business management of the company and not necessarily be company shareholders, unless otherwise stipulated in the company charter (article 151.1(b) of the LOE). The members of the supervisory board are not required to have any specific skills or experience unless otherwise regulated in the company's charter (article 164.1(d) of the LOE), except that the head of the supervisory board must be a professional accountant or auditor and must work full-time at the company (article 163.2 of the LOE) and for public companies, at least one member of the supervisory board must be an accountant or auditor and the head of the supervisory board must have professional accounting knowledge (article 19 of Circular 121/2012/TT-BTC).

21 Delegation of board responsibilities

To what extent can the board delegate responsibilities to management, a board committee or board members, or other persons?

The board of directors cannot delegate a responsibility expressly and exclusively assigned to the board of directors to other internal bodies. Other than that, some of the duties or responsibilities of the board may be delegated to the general director in accordance with the company's charter and resolution of the board of directors (article 157.3(i) of the LOE) and the board committee or a dedicated director may be in charge of specific matters such as human resources, remuneration and bonuses (see question 25). However, the board of directors is still held liable for such duties assigned to other internal bodies.

22 Non-executive and independent directors

Is there a minimum number of 'non-executive' or 'independent' directors required by law, regulation or listing requirement? If so, what is the definition of 'non-executive' and 'independent' directors and how do their responsibilities differ from executive directors?

Non-public companies are not required to have non-executive or independent directors under law, whereas at least one-third of the total directors of the board of a public company must be non-executive directors (article 11.2 of Circular 121/2012/TT-BTC). A non-executive director is defined as a person who is not the general director, deputy general director, chief accountant or any other executive person as appointed by the company (article 2.2 of Circular 121/2012/TT-BTC).

At least one-third of the total directors of the board of a large public company or listed company as mentioned in question 15, however, must be independent directors (article 30.2 of Circular 121/2012/TT-BTC). A director is considered independent if:

- he or she is a non-executive director and not a related party of the general director, deputy general director, chief accountant or other executive persons as appointed by the company;
- he or she does not hold the position of director of the board, general director or deputy general director of any subsidiary, affiliate or company controlled by such a company;
- he or she is not a major shareholder or a representative of a major shareholder or a related person of any major shareholder of the company;
- he or she has not previously worked at a legal or auditing firm providing services to the company for the last two years; and
- he or she is not a partner or a related person of any partner who has an annual transaction with the company the value of which accounts for 30 per cent of the total revenue or total value of the product or service purchased by the company for the previous two years (article 2.3 of Circular 121/2012/TT-BTC).

There appears to be no statutory difference between non-executive or independent directors and other directors in respect of responsibilities according to the laws except that if a board committee is not established within the board of directors of a large-scale public company or listed company, the board of directors is required to appoint independent directors to be in charge of certain matters individually (article 32.4 of Circular 121/2012/TT-BTC). Under the LOE, the appointment of independent directors is also required if the company is structured without having a supervisory board as discussed in question 15.

23 Board size and composition

How is the size of the board determined? Are there minimum and maximum numbers of seats on the board? Who is authorised to make appointments to fill vacancies on the board or newly created directorships? Are there criteria that individual directors or the board as a whole must fulfil? Are there any disclosure requirements relating to board composition?

The LOE sets forth criteria for board members including independent directors, as outlined below.

Criteria for board members

Board members must:

- have full civil capacity and not be prohibited from management of companies in general (article 151.1(a) of the LOE);
- have appropriate experience or professional knowledge in business administration; members of the board of directors are not necessarily shareholders of the company, unless otherwise prescribed by the company's charter (article 151.1(b) of the LOE); and
- with regard to subsidiaries 50 per cent of whose charter capital is held by the state, members of the board of directors must not be spouses, parents, adoptive parents, children, adopted children, or siblings of the director/general director and other managers; must not be related persons of the manager and the person competent to designate the manager of the parent company (article 151.1(d) of the LOE).

Criteria for independent board members

Independent board members must:

- not be a current employee of the company or its subsidiaries and not be a person that used to work for the company or the company's subsidiaries over the previous three consecutive years (article 151.2(a) of the LOE);
- not be a person receiving a salary or wage from the company, except for the benefits to which members of the board of directors are entitled (article 151.2(b) of the LOE);
- not have a spouse, birth parent, adoptive parent, birth child, adopted child or sibling being a major shareholder of the company, being a manager of the company or the company's subsidiary (article 151.2(c) of the LOE);
- not directly or indirectly hold at least 1 per cent of the company's voting shares (article 151.2(d) of the LOE); and
- not have held the position of member of the board of directors or the supervisory board for at least the previous five consecutive years (article 151.2(dd) of the LOE).

The LOE also requires that more than half of the members of the supervisory board permanently reside in Vietnam, and the chief of the supervisory board must be a professional accountant or auditor and has to work full-time at the company, unless higher standards are prescribed by the company's charter (article 163.2 of the LOE). Members of the supervisory board must:

- have full civil capacity (article 164.1(a) of the LOE);
- not be prohibited from establishment and management of a company (article 164.1(a) of the LOE);
- not be a spouse, birth parent, adoptive parent, birth child, adopted child or sibling of any member of the board of directors, director or general director, or any other managers (article 164.1(b) of the LOE). A member of the supervisory board is not permitted to hold a managerial position in the company and is not necessarily a shareholder or employee of the company, unless otherwise prescribed by the company's charter (article 164.1(c) of the LOE); and
- satisfy other standards and conditions of relevant regulations of law and the company's charter (article 164.1(d) of the LOE).

Members of the supervisory board of a public company have additional criteria imposed and must have qualifications, such as specialised knowledge and expertise or possess accounting knowledge applicable to the head of the supervisory board (articles 18 and 19 of Circular 121/2012/TT-BTC). Similar to changes to the board of directors, a change in the supervisory board of a public company is subject to a public disclosure obligation in accordance with law (article 9.1(n) of Circular 155/2015/TT-BTC).

Disclosure requirements

For public companies, any change of the board must be publicly disclosed in accordance with the securities laws (article 9.1(n) of Circular 155/2015/TT-BTC). Under the LOE, certain information related to changes of the board shall be publicly disclosed (see question 36).

Minimum and maximum number of seats

Generally speaking, the board of directors must comprise three to 11 directors, the specific number of directors is stipulated in the company's charter (article 150.1 of the LOE). The board of directors of a public company must comprise three to 11 members regardless of the company's charter (article 11.1 of Circular 121/2012/TT-BTC), and for a large-scale public company or a listed company, five to 11 members regardless of the company's charter (article 30.1 of Circular 121/2012/TT-BTC).

In public companies the supervisory board must have three to five members regardless of the company's charter (article 19.1 of Circular 121/2012/TT-BTC). Under the LOE, the number of members of the supervisory board is also fixed at three to five members (article 163.1 of the LOE).

Vacancy

In the case of a vacancy, by default vacant positions will be filled by appointment of the shareholders' meeting (article 135.2(c) of the LOE). Also, the board of directors may appoint a temporary director to fill a vacancy until an official director is appointed at the next shareholders' meeting (article 11.3 of Circular 121/2012/TT-BTC).

It is also worth noting that, in the model charter for public companies, a temporary director may be approved at the next shareholders' meeting. In such case, the temporary director's appointment will be retroactively valid and effective from the time of appointment by the board of directors; otherwise, a new director will be appointed at the next shareholders' meeting, but all decisions of the board of directors up to the time of that shareholders' meeting will still be valid and effective (article 24.5 of the model charter attached to Circular 121/2012/TT-BTC).

24 Board leadership

Is there any law, regulation, listing requirement or practice that requires the separation of the functions of board chairman and CEO? If flexibility on board leadership is allowed, what is generally recognised as best practice and what is the common practice?

The chairman of the board of directors and the general director are two separate positions with different powers under the laws, although a single person can simultaneously hold the two positions (article 10.3 of Circular 121/2012/TT-BTC; article 152.1 of the LOE).

Under the LOE, a company may have one or multiple legal representatives (article 13.2 of the LOE). If there is only one legal representative, the chairman of the board of directors or the general director/director shall be the legal representative; unless otherwise prescribed by the company's charter, the chairman of the board of directors shall be the legal representative of the company. If there is more than one legal representative, both the chairman of the board of directors and the general director/director shall be the legal representatives of the company (article 134.2 of the LOE). It is common practice in non-public companies for a single person to act as both the chairman and the general director at the same time, whereas, for public companies, the chairman is often a separate person who leads the board and who is different from the general director.

25 Board committees

What board committees are mandatory? What board committees are allowed? Are there mandatory requirements for committee composition?

Normal public companies are not required to have any board committee or dedicated director. For a large-scale public company or a listed company, as mentioned in question 15, board committees are merely optional. These companies may choose not to form board committees, provided that they have dedicated directors for specific matters instead. Default committees available under the laws include committees of development policy, human resources, remuneration and bonuses. Additional committees can be stipulated under the resolution of the shareholders' meeting. The heads of the committee of human resources and committee of remuneration and bonuses, or the two dedicated directors for these matters if no committee is formed, must be independent directors (articles 32 of Circular 121/2012/TT-BTC).

Under the LOE, as noted in question 15, where a company that has 11 shareholders or more, or where the shareholders are organisations holding 50 per cent or more of the total shares, decides not to set up a supervisory board it must establish an internal auditing board belonging to the board of directors.

26 Board meetings

Is a minimum or set number of board meetings per year required by law, regulation or listing requirement?

At least one regular board meeting must be held every quarter of a calendar year according to law (article 153.3 of the LOE), although the chairman can convene a board meeting at any time.

In respect of the supervisory board, the law does not provide for a certain number of required meetings in a non-public company, although such meetings must be held at least twice a year in a public company (article 21.2 of Circular 121/2012/TT-BTC).

27 Board practices

Is disclosure of board practices required by law, regulation or listing requirement?

Under the LOE, certain information related to board practices is required to be disclosed (see question 36). For listed companies, the laws require them to make a disclosure of the company management, including members of the board, number of meetings, and adopted decisions, among others, twice a year (article 11.6 of Circular 155/2015/TT-BTC) and non-listed public companies are required to make disclosure of the company management once a year in their annual report (article 8.2 of Circular 155/2015/TT-BTC).

28 Remuneration of directors

How is remuneration of directors determined? Is there any law, regulation, listing requirement or practice that affects the remuneration of directors, the length of directors' service contracts, loans to directors or other transactions or compensatory arrangements between the company and any director?

Remuneration of directors is determined in accordance with the basis and method as provided for under the company's charter. If the charter does not specify, the directors by default shall be entitled to remuneration based on the total working days and pay rates per day, all of which shall be estimated by unanimous agreement of the board, provided that the total remuneration of the board does not exceed the amount as approved by the shareholders' meeting (article 16 of Circular 121/2012/TT-BTC; article 158.2(a) of the LOE). There is no specific regulation for service contracts between the directors and the company, but the laws generally deem any transaction between the directors and the company as transactions with related parties, which must be approved by the board of directors or the shareholders' meeting, depending on the value of such transactions (article 162 of the LOE). For public companies, no loans may be granted to the directors by the company unless approved by the shareholders' meeting (article 23.4 of Circular 121/2012/TT-BTC).

Under the LOE, members of the supervisory board may also receive salaries in accordance with a decision of the shareholders' meeting unless provided otherwise by the company's charter (article 167 of the LOE). For public companies, no loans may be granted to members of the supervisory board by the company unless approved by the general meeting of shareholders (article 23.4 of Circular 121/2012/TT-BTC).

A director may also be held liable for compensation with respect to damage or loss incurred by the company in certain cases of violation of the laws in his or her role as a director (articles 136.4 and 162.4 of the LOE). It is optional for the companies to have compensatory arrangements with directors. The model charter for public companies provides for a standard clause that directors may be compensated or held harmless by the company in certain cases against damage, loss, claims, among others, in their role as directors as well as covered with directors' liability insurance policy (article 36 of the model charter issued with Circular 121/2012/TT-BTC).

29 Remuneration of senior management

How is the remuneration of the most senior management determined? Is there any law, regulation, listing requirement or practice that affects the remuneration of senior managers, loans to senior managers or other transactions or compensatory arrangements between the company and senior managers?

Aside from the board of directors and the supervisory board, the laws only govern remuneration and other benefits given to the general director and other managerial positions. Accordingly, the general director and other officers of the company are paid wages and bonuses as determined by the board of directors unless the company's charter requires otherwise (articles 158.2(c) and 149.2(i) of the LOE). Transactions between the company and the members of the board of directors including the general director must also be approved by the board of directors or shareholders' meeting in the same manner as in the directors' cases (article 23.4 of Circular 121/2012/TT-BTC; article 162 of the LOE). There is neither special nor separate regulation on compensatory arrangements with senior management.

30 D&O liability insurance

Is directors' and officers' liability insurance permitted or common practice? Can the company pay the premiums?

For public companies, D&O liability insurance is expressly regulated under the laws, premiums of which can be paid by the company itself if

Update and trends

The Ministry of Finance is still updating the regulations on the management of public companies, which shall replace Circular 121/2012/TT-BTC (the Draft). The Draft provides further regulations on the management of public companies to enhance transparency in finance, as well as strictly controls the activities of such public companies. Certain notable provisions of the Draft include:

- the registration of a legal representative in charge of the securities sector of the company (article 6 of the Draft);
- the term of the board of management and election of directors on the board (article 13 of the Draft);
- an internal audit with clear criteria and conditions and duties of the internal audit (article 19 of the Draft);
- regulation on avoiding conflicts of interest which prohibits the managerial personnel from dividing any related transactions of the company into a series of transactions (article 28.3 of the Draft); and
- further conditions and requirements with respect to related transactions of the company (article 30 of the Draft).

There will also be an updated model charter attached with the Draft.

A new bill on amendments of laws related to business and investment is also being prepared by the National Assembly. The current bill is still at the early stage of drafting and it contains minor revisions but may be extended later to cover a variety of topics and issues, from enterprises to land.

so determined by the shareholders' meeting, provided that such a policy does not cover liability arising from breaches of laws or the company's charter (article 13.6 of Circular 121/2012/TT-BTC). For non-public companies, D&O liability insurance is not regulated by the laws and it is not a very common practice that D&O liability insurance is purchased by the company for its directors.

31 Indemnification of directors and officers

Are there any constraints on the company indemnifying directors and officers in respect of liabilities incurred in their professional capacity? If not, are such indemnities common?

No comprehensive and unified legislation exists in respect of indemnities made by the company for the directors and officers for such liabilities. However, under the model charter regulated in Circular 121/2012/TT-BTC as issued by the Ministry of Finance for public companies, the directors and other officers of the company shall be indemnified by the company in such circumstances, only if they have not committed any breach of law or the company's charter or in their other duties and obligations.

32 Exculpation of directors and officers

To what extent may companies or shareholders preclude or limit the liability of directors and officers?

The laws by default hold the directors, general director and members of the supervisory board liable for certain acts or omissions, such as failure to comply with the law, charter or the resolutions of the shareholders' meeting. However, to the extent that such liability is civil in nature, it would be possible for the shareholders' meeting, as the highest authority in the company, to preclude, limit or waive such liability in relation to the company, although the courts might have different interpretations on this issue. The shareholders may, and cause the company to, provide for limit of liability and compensatory arrangements in the company's charter and directors' liability insurance policy, such as the sample clause in the model charter for public companies (article 36 of the model charter issued with Circular 121/2012/TT-BTC).

33 Employees

What role do employees play in corporate governance?

Employees are not generally involved in corporate governance unless otherwise regulated by the corporate documents of the company, such as the company's charter or policies.

34 Board and director evaluations

Is there any law, regulation, listing requirement or practice that requires evaluation of the board, its committees or directors? How regularly are such evaluations conducted and by whom? What do companies disclose in relation to such evaluations?

As explained in question 15, a company may choose to establish a supervisory board (article 134.1(a) of the LOE) that supervises the management and operation of the company by the board of directors and general director (or CEO). The law does not prescribe how often such evaluations are conducted; however, the supervisory board is required to submit evaluation reports during the annual shareholders' meeting (article 165.3 of the LOE). The supervisory board may use an independent consultant or the internal audit department of the company to perform any of its assigned duties (article 165.10 of the LOE). Companies are required to provide all information and documents relating to their management, administration and business operations upon demand of the supervisory board (article 166.5 of the LOE).

Disclosure and transparency

35 Corporate charter and by-laws

Are the corporate charter and by-laws of companies publicly available? If so, where?

A public company is required by law, within six months from becoming public, to have its charter, internal management rules, and prospectus, among others, disclosed on its official website in the shareholders section (articles 5.2(a) and (c) of Circular 155/2015/TT-BTC). The LOE requires the non-public company's charter to be published on the company's website (article 171.2(a) of the LOE) (see question 36).

36 Company information

What information must companies publicly disclose? How often must disclosure be made?

The laws provide for two kinds of disclosure for public companies, namely, regular and extraordinary disclosures. Regular disclosure includes the disclosure of audited financial statements, annual reports, contents of general meetings of shareholders, offering and report on use of funds, and foreign ownership ratio. Extraordinary disclosure includes the disclosure of any important event, including dissolution of the company, decisions of share buyback, new share issuance, dividend distributions or any change in executive officers, among others. In certain circumstances, such as any event that may have a material effect on the shareholders' benefits, public companies may be requested by the authorities to make disclosures (chapter II of Circular 155/2015/TT-BTC).

Under the LOE, after the enterprise registration certificate of a new company is issued, the company must make a public announcement regarding its business lines and list of founding shareholders and shareholders who are foreign investors through the National Business Registration Portal (the Portal) (article 33.1 of the LOE). Additionally, where there are changes to the enterprise registration contents, the company shall also make a public announcement on such changes through the Portal (article 33.2 of the LOE). Moreover, the company shall post the following information on its website (article 171.2 of the LOE):

- the company's charter;
- curricula vitae, qualifications, and professional experience of directors, members of the supervisory board, the general director or director of the company;
- annual financial statements ratified by the shareholders' meeting; and
- annual reports of the business made by the board of directors and the supervisory board.

Hot topics

37 Say-on-pay

Do shareholders have an advisory or other vote regarding executive remuneration? How frequently may they vote?

The shareholders' meeting only votes on the total amount and calculation method of executive remuneration and bonuses, which will be binding and valid (articles 158.2(a) and 167.1 of the LOE). The board of directors shall then make specific decisions of remuneration and bonuses according to such resolutions. The exact power may be customised in the company's charter. There is no say-on-pay vote in Vietnamese law, although it is not explicitly prohibited.

38 Shareholder-nominated directors

Do shareholders have the ability to nominate directors and have them included in shareholder meeting materials that are prepared and distributed at the company's expense?

A shareholder or a group of shareholders in a company may nominate directors for the board if they have held at least 10 per cent of the total ordinary shares for a consecutive period of six months or more (major shareholders) unless a lower percentage is set forth in the company's charter (articles 114.2 and 114.4 of the LOE). Therefore, unless a shareholder holds a minimum ratio of shareholding that provides the power to nominate directors, such a shareholder must solicit proxy voting in order to exercise such a right. The nomination of directors proposed by major shareholders shall be included in the agenda of the shareholders' meeting upon the written proposal of such major shareholders (article 138.2 of the LOE). Such proposal must be sent to the company no later than three working days prior to the opening date of the shareholders' meeting (unless the company's charter provides for another time limit) (article 138.2 of the LOE). Of note, the proposal must specify the names of shareholders, the amount of each type of shares and the issues proposed to the agenda (eg, the nomination of the directors with details of the candidates) (articles 136.7(dd) and 138.2 of the LOE).

39 Shareholder engagement

Do companies engage with shareholders? If so, who typically participates in the company's engagement efforts and when does engagement typically occur?

Engagement or transaction between the company and its shareholders are allowed at any time, provided that such engagement or transaction shall comply with the conditions in law, such as conditions for related-party transactions, disclosure procedure, among others.

Typically, certain persons are designated as authorised representatives to communicate with the company on behalf of the shareholders, who shall concurrently participate in general meetings of shareholders (article 16 of the LOE). Also, for corporate shareholders, their legal representatives, who have the right to enter into and perform civil transactions on behalf of and in the interests of the shareholders under the law, may also engage or transact with the company on behalf of the shareholders (article 141.2 of the Civil Code).

The frequency of direct engagement between the shareholders and the company should vary case by case.

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